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RURAL TELEPHONE SUPPLEMENTAL FINANCING

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HEARINGS

BEFORE THE

COMMITTEE ON AGRICULTURE

HOUSE OF REPRESENTATIVES

NINETIETH CONGRESS

FIRST SESSION

ON

H.R. 12066

AUGUST 23 AND 24, 1967

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RURAL TELEPHONE SUPPLEMENTAL FINANCING

WEDNESDAY, AUGUST 23, 1967

HOUSE OF REPRESENTATIVES,
COMMITTEE ON AGRICULTURE,
Washington, D.C.

The committee met, pursuant to notice, at 10:05 a.m., in room 1301, Longworth House Office Building, Washington, D.C., the Honorable W. R. Poage, chairman, presiding.

Present: Representatives Poage, Gathings, McMillan, Abbitt, Jones of Missouri, Stubblefield, Purcell, O'Neal, Jones of North Carolina, Dow, Rarick, Belcher, Teague of California, Dole, Hansen, Wampler, Miller, Burke, Mathias, Mayne, Zwach, Kleppe, Price, and Myers.

Also present: Christine S. Gallagher, clerk; Hyde H. Murray, assistant counsel; and Francis LeMay, consultant.

The CHAIRMAN. The committee will please come to order.

This morning we have with us Mr. Harold R. Bollinger, president of the Pioneer Telephone Co. of Minnesota, accompanied by Robert Fegan, president of the Junction City Telephone Co., and Hugh Barnhart, president of the Rochester Telephone Co. of Indiana.

We will be glad to hear from you gentlemen now and we will place in the record at this point the bill H.R. 12066.

(H.R. 12066, introduced by Mr. Poage, is as follows:)

[H.R. 12066, 90th Cong., first sess.]

A BILL To amend the Rural Electrification Act of 1936, as amended, to provide an additional source of financing for the rural telephone program, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That it is hereby declared to be the policy of the Congress that the growing capital needs of the rural telephone systems require the establishment of a rural telephone bank which will furnish assured and viable sources of supplementary financing with the objective that said bank will become an entirely privately owned, operated, and financed corporation. The Congress further finds that many rural telephone systems require financing under the terms and conditions provided in title II of the Rural Electrification Act of 1936, as amended. In order to effectuate this policy, the Rural Electrification Act of 1936, as amended (7 U.S.C. 921-924) is amended as hereinafter provided.

SEC. 2. The Rural Electrification Act of 1936, as amended, is amended by adding the following two new titles:

"TITLE III

"SEC. 301. RURAL TELEPHONE ACCOUNT.—(a) There is hereby established in the Treasury of the United States an account, to be known as the rural telephone account, consisting of:

"(1) all notes, bonds, obligations, and property delivered or assigned to the Administrator pursuant to loans heretofore or hereafter made under section 201 of this Act, including notes, bonds, obligations, and property held in trust by him on behalf of the Secretary of the Treasury, as of the effective date of this title, which shall be transferred to and be assets of the rural telephone account;

"(2) undisbursed balances of telephone loans made under section 201, which, as of the effective date of this title, shall be transferred to and be assets of the rural telephone account;

"(3) all collections of principal and interest received on and after July 1, 1967, on notes, bonds, judgments, or other obligations made or held under title II of this Act, which shall be paid into and be assets of the rural telephone accounts;

"(4) all appropriations for telephone loans made under the authority of section 3 of this Act and funds obtained in accordance therewith and the unexpended balances of any funds available on the effective date of this title for telephone loans under section 201 of this Act, including any funds made available for telephone loans under the item 'Rural Electrification Administration,' in the Department of Agriculture Appropriation Acts current on the date of enactment of this title, and said appropriations, balances, and funds shall be assets of the rural telephone account; and

"(5) shares of the capital stock of the Rural Telephone Bank acquired by investment of the rural telephone account pursuant to section 302(b)(3) of this title, and moneys received from said bank upon retirement of said shares of stock in accordance with the provisions of title IV of this Act, which said shares and moneys shall be assets of the rural telephone account.

"SEC. 302. LIABILITIES AND USES OF ACCOUNT.—(a) The notes of the Administrator issued to the Secretary of the Treasury to obtain funds for loans under section 201 of this Act, and all other liabilities against the appropriations or assets in the rural telephone account in connection with telephone loan operations shall be liabilities of the rural telephone account, and all other obligations against such appropriations or assets arising out of telephone loan operations shall be obligations of the rural telephone account.

"(b) The assets of the rural telephone account shall be available for the following purposes:

"(1) loans under section 201 of this Act and for advances in connection therewith, except that no such loans shall be made in any year in excess of the amounts previously authorized therefor in appropriation Acts for such year or available pursuant to section 3 of this Act; the amounts so authorized for loans and advances shall remain available until expended;

"(2) payment of interest as it accrues on loans to the Administrator from the Secretary of the Treasury for telephone purposes pursuant to section 3(a) of this Act;

"(3) investment in the capital stock of the Rural Telephone Bank in accordance with section 406(a) of this Act: *Provided*, That such investment shall be deemed paid in capital of the said bank notwithstanding that funds representing the proceeds from the purchase of such stock shall remain in the rural telephone account until required for actual disbursement in cash by the said bank; and

"(4) payment of principal when due on loans to the Administrator from the Secretary of the Treasury for telephone purposes pursuant to section 3(a) of this Act.

"SEC. 303. DEPOSIT OF ACCOUNT MONEYS.—Moneys in the rural telephone account shall remain on deposit in the Treasury of the United States until disbursed.

"TITLE IV

"SEC. 401. ESTABLISHMENT, GENERAL PURPOSES, AND STATUS OF THE TELEPHONE BANK.—(a) There is hereby established a body corporate to be known as the Rural Telephone Bank (hereinafter called the telephone bank).

"(b) The general purposes of the telephone bank shall be to obtain an adequate supply of supplemental funds to the extent feasible from non-Federal sources, to utilize said funds in the making of loans under section 408 of this title, and to conduct its operations to the extent practicable on a self-sustaining basis.

"(c) The telephone bank shall be deemed to be an instrumentality of the United States, and shall, for the purposes of jurisdiction and venue, be deemed a citizen and resident of the District of Columbia. The telephone bank is authorized to make payments to State, territorial, and local governments in lieu of property taxes upon real property and tangible personal property which was subject to State, territorial, and local taxation before acquisition by the telephone bank. Such payment may be in the amounts, at the times, and upon such terms as the telephone bank deems appropriate, but the telephone bank shall be guided by the policy of making payments not in excess of the taxes which would have been payable upon such property in the condition in which it was acquired.

"SEC. 402. GENERAL POWERS.—To carry out the specific powers herein authorized, the telephone bank shall have power to (a) adopt, alter, and use a corporate seal; (b) sue and be sued in its corporate name; (c) make contracts, leases, and cooperative agreements, or enter into other transactions as may be necessary in the conduct of its business, and on such terms as it may deem appropriate; (d) acquire, in any lawful manner, hold, maintain, use, and dispose of property: *Provided*, That the telephone bank may only acquire property needed in the conduct of its banking operations or pledged or mortgaged to secure loans made hereunder or in temporary operation or maintenance thereof: *Provided further*, That any such pledged or mortgaged property so acquired shall be disposed of as promptly as is consistent with prudent liquidation practices, but in no event later than five years after such acquisition; (e) accept gifts or donations of services, or of property in aid of any of the purposes herein authorized; (f) appoint such officers, attorneys, agents, and employees, vest them with such powers and duties, fix and pay such compensation to them for their services as the telephone bank may determine; (g) determine the character of and the necessity for its obligations and expenditures, and the manner in which they shall be incurred, allowed, and paid; (h) execute, in accordance with its bylaws, all instruments necessary or appropriate in the exercise of any of its powers; (i) collect or compromise all obligations assigned to or held by it and all legal or equitable rights accruing to it in connection with the payment of such obligations until such time as such obligation may be referred to the Attorney General for suit or collection; and (j) exercise all such other powers as shall be necessary or incidental to carrying out its functions under this title.

"SEC. 403. SPECIAL PROVISIONS GOVERNING TELEPHONE BANK AS AN AGENCY OF THE UNITED STATES UNTIL CONVERSION OF OWNERSHIP, CONTROL, AND OPERATION.—Until the ownership, control, and operation of the telephone bank is converted as provided in section 410 (a) of this title and not thereafter—

"(a) the telephone bank shall be an agency of the United States and shall be subject to the supervision and direction of the Secretary of Agriculture (hereinafter called the Secretary): *Provided, however*, That the telephone bank shall at no time be entitled to transmission of its mail free of postage, nor shall it have the priority of the United States in the payment of debts out of bankrupt, insolvent, and decedents' estates;

"(b) in order to perform its responsibilities under this title, the telephone bank may partially or jointly utilize the facilities and the services of employees of the Rural Electrification Administration or of any other agency of the Department of Agriculture, without cost to the telephone bank and without charge to administrative expenses recoverable by the telephone bank under section 408(b)(3) of this title, but the compensation and expenses of members of the Telephone Bank Board who are not Federal officers or employees, and of officers and employees engaged solely on telephone bank activities, and procurement for the telephone bank, shall be administrative expenses recoverable under said subsection;

"(c) notwithstanding the provisions of the second sentence of subsection (d) of section 303 of the Government Corporation Control Act, as amended (31 U.S.C. 863), all telephone debentures issued by the telephone bank shall be issued at such times, bear interest at such rates, and contain such other terms and conditions as have been or may be approved by the Secretary of the Treasury;

"(d) the telephone bank may without regard to the civil service classification laws appoint and fix the compensation of such officers and employees of the telephone bank as it may deem necessary;

"(e) the telephone bank shall be subject to the provisions of sections 517, 519, and 2679 of title 28, United States Code.

"SEC. 404. GOVERNOR.—Subject to the provisions of section 410, the Administrator of the Rural Electrification Administration shall serve as the chief executive officer of the telephone bank (herein called the Governor of the telephone bank). Except as to matters specifically reserved to the Telephone Bank Board in this title, the Governor of the telephone bank shall exercise and perform all functions, powers, and duties of the telephone bank.

"SEC. 405. BOARD OF DIRECTORS.—(a) The management of the telephone bank, within the limitations prescribed by law, shall be vested in a board of directors (herein called the Telephone Bank Board) consisting of thirteen members.

"(b) The Administrator of the Rural Electrification Administration and the Governor of the Farm Credit Administration shall be members of the Telephone Bank Board. Five other members of the Telephone Bank Board shall be designated

by the President to serve at his pleasure, three of whom shall be officers or employees of the Department of Agriculture but not officers or employees of the Rural Electrification Administration, and two of whom shall be from the general public and not officers or employees of the Federal Government. The Administrator and other officers and employees of the Department of Agriculture and the Governor of the Farm Credit Administration shall serve as members without additional compensation.

"(c) As soon as practicable after enactment of this title, the President of the United States shall appoint six additional members of the initial Telephone Bank Board to be selected from the directors, managers, and employees of any entities eligible to borrow from the telephone bank and of organizations controlled by such entities, with due regard to fair representation of the rural telephone systems of the Nation. The six members thus appointed shall serve until their successors shall have been duly elected in accordance with subsection (d).

"(d) Within twelve months following the appointment of the six members of the initial Board as provided in subsection (c), the Governor of the telephone bank shall call a meeting of all entities then eligible to borrow from the telephone bank and organizations controlled by such entities for the purpose of electing members of the Telephone Bank Board. Each such entity and organization shall be entitled to notice of and shall have one noncumulative vote at said meeting. Six members of the Telephone Bank Board shall be elected for a two-year term, three from among the directors, managers, and employees of cooperative-type entities eligible to vote and organizations controlled by such entities, and three from among the managers, directors, and employees of commercial-type entities eligible to vote and organizations controlled by such entities. These six members shall be elected by majority vote of the entities and organizations eligible to vote and such entities and organizations may vote by proxy.

"(e) Thereafter, in accordance with the bylaws of the telephone bank, the six members of the Telephone Bank Board shall be elected by holders of class B and class C stock, three from among the directors, managers, and employees of cooperative-type entities and organizations controlled by such entities holding class B or class C stock, and three from among the directors, managers, and employees of commercial-type entities and organizations controlled by such entities holding class B or class C stock. These six members shall be elected by majority vote of the entities and organizations eligible to vote and such entities and organizations may vote by proxy.

"(f) Any Telephone Bank Board member may continue to serve after the expiration of the term for which he is elected until his successor has been elected and has qualified. Telephone Bank Board members designated from the general public, pursuant to subsection (b), or appointed or elected pursuant to subsections (c), (d), and (e), shall receive \$100 for each day or part thereof, not to exceed one hundred days per year for the first three years after enactment of this title and not to exceed fifty days per year thereafter, spent in the performance of official duties, and shall be reimbursed for travel and other expenses in such manner and subject to such limitations as the Telephone Bank Board may prescribe.

"(g) The Telephone Bank Board shall prescribe bylaws, not inconsistent with law, regulating the manner in which the telephone bank's business shall be conducted, its directors and officers elected, its stock issued, held, and disposed of, its property transferred, its bylaws amended, and the powers and privileges granted to it by law exercised and enjoyed.

"(h) The Telephone Bank Board shall meet at such times and places as it may fix and determine, but shall hold at least four regularly scheduled meetings a year, and special meetings may be held on call in the manner specified in the bylaws of the telephone bank.

"(i) The Telephone Bank Board shall make an annual report to the Secretary for transmittal to the Congress on the administration of this title IV and any other matters relating to the effectuation of the policies of title IV, including recommendations for legislation.

"SEC. 406. CAPITALIZATION.—(a) The telephone bank's capital shall consist of capital subscribed by the United States, by borrowers from the telephone bank, by corporations and public bodies eligible to become borrowers from the telephone bank, and by organizations controlled by such borrowers, corporations, and public bodies. Beginning with the fiscal year 1968 and for each fiscal year thereafter, the United States shall furnish capital for the purchase of class A stock and there are hereby authorized to be appropriated from net collection proceeds in the rural telephone account created under title III of this Act such

amounts, not to exceed \$30,000,000 annually, for such purchases until such class A stock shall equal \$300,000,000: *Provided*, That on or before July 1, 1972, the Secretary shall make a report to the President for transmittal to the Congress on the status of capitalization of the telephone bank by the United States with appropriate recommendations. As used in this section, the term 'net collection proceeds' shall be deemed to mean payments from and after July 1, 1967, of principal and interest on loans heretofore or hereafter made under section 201 of this Act, less an amount representing interest payable to the Secretary of the Treasury on loans to the Administrator for telephone purposes pursuant to section 3(a) of this Act.

"(b) The capital stock of the telephone bank shall consist of three classes, class A, class B, and class C, the rights, powers, privileges, and preferences of the separate classes to be as specified, not inconsistent with law, in the bylaws of the telephone bank. Class B and class C stock shall be voting stock, but no holder of said stock shall be entitled to more than one vote, nor shall class B and class C stockholders, regardless of their number, which are owned or controlled by the same person, group of persons, firm, association, or corporation, be entitled in any event to more than one vote.

"(c) Class A stock shall be issued only to the Administrator of the Rural Electrification Administration on behalf of the United States in exchange for capital furnished to the telephone bank pursuant to subsection (a), and such class A stock shall be redeemed and retired by the telephone bank as soon as practicable after June 30, 1982, but not to the extent that the Telephone Bank Board determines that such retirement will impair the operations of the telephone bank: *Provided*, That the minimum amount of class A stock that shall be retired each year after said date and after the amount of class A and class B stock issued totals \$400,000,000, shall equal the amount of class B stock sold by the telephone bank during such year. Class A stock shall be entitled to a return, payable from income, at the rate of 2 per centum per annum on the amounts of said class A stock actually paid into the telephone bank. Such return shall be cumulative and shall be payable annually into miscellaneous receipts of the Treasury.

"(d) Class B stock shall be held only by recipients of loans under section 408 of this Act. Borrowers receiving loan funds pursuant to section 408(a) (1) or (2) shall be required to invest in class B stock 5 per centum of the amount of loan funds so provided. No dividends shall be payable on class B stock. All holders of class B stock shall be entitled to patronage refunds in class B stock under terms and conditions to be specified in the bylaws of the telephone bank.

"(e) Class C stock shall be available for purchase and shall be held only by borrowers, or by corporations eligible to borrow under section 408 of this Act, or by organizations controlled by such borrowers and corporations, and shall be entitled to dividends in the manner specified in the bylaws of the telephone bank. Such dividends shall be payable only from income and, until all class A stock is retired, shall not exceed the current average rate payable on its telephone debentures.

"(f) If a firm, association, corporation, or public body is not authorized under the laws of the jurisdiction in which it is organized to acquire stock of the telephone bank, the telephone bank shall, in lieu thereof, permit such organization to pay into a special fund of the telephone bank a sum equivalent to the amount of stock to be purchased. Each reference in this title to capital stock, or to class B, or class C stock, shall include also the special fund equivalents of such stock, and to the extent permitted under the laws of the jurisdiction in which such organization is organized, a holder of special fund equivalents of class B, or class C stock, shall have the same rights and status as a holder of class B or class C stock, respectively. The rights and obligations of the telephone bank in respect of such special fund equivalent shall be identical to its rights and obligations in respect of class B or class C stock, respectively.

"(g) After payment of all operating expenses of the telephone bank, including interest on its telephone debentures, setting aside appropriate funds for reserves for losses, and making payments in lieu of taxes, and returns on class A stock as provided in section 406(c), and on class C stock, the Telephone Bank Board shall annually set aside the remaining earnings of the telephone bank for patronage refunds in accordance with the bylaws of the telephone bank.

"SEC. 407. BORROWING POWER.—The telephone bank is authorized to obtain funds through the public or private sale of its bonds, debentures, notes, and other evidences of indebtedness (herein collectively called 'telephone debentures'). Telephone debentures shall be issued at such times, bear interest at such rates, and contain such other terms and conditions as the Telephone Bank Board shall

determine: *Provided, however,* That the amount of the telephone debentures which may be outstanding at any one time pursuant to this section shall not exceed eight times the paid-in capital and retained earnings of the telephone bank. The telephone bank shall insert in all its telephone debentures appropriate language indicating that such telephone debentures, together with interest thereon, are not guaranteed by the United States and do not constitute a debt or obligation of the United States or of any agency or instrumentality thereof other than the telephone bank. Telephone debentures shall not be exempt, either as to principal or interest, from any taxation now or hereafter imposed by the United States, by any territory, dependency, or possession thereof, or by any State or local taxing authority. Telephone debentures shall be lawful instruments and may be accepted as security for all fiduciary, trust, and public funds, the investment or deposit of which shall be under the authority and control of the United States or any officer or officers thereof.

"SEC. 408. LENDING POWER.—(a) The Governor of the telephone bank is authorized on behalf of the telephone bank to make loans, in conformance with policies approved by the Telephone Bank Board, to corporations and public bodies which have received a loan or loan commitment pursuant to section 201 of this Act, (1) for the same purposes and under the same limitations for which loans may be made under section 201 of this Act, (2) for the purposes of financing, or refinancing, the construction, improvement, expansion, acquisition, and operation of telephone lines, facilities, or systems, in order to improve the efficiency, effectiveness, or financial stability of borrowers financed under sections 201 and 408 of this Act, and (3) for the purchase of class B stock required to be purchased under section 406(d) of this Act but not for the purchase of class C stock, subject, as to the purposes set forth in (2) hereof, to the following provisos: That in the case of any such loan for the acquisition of telephone lines, facilities, or systems, the acquisition shall be approved by the Secretary, the location and character thereof shall be such as to improve the efficiency, effectiveness, of financial stability of the telephone system of the borrower, and in respect of exchange facilities for local services, the size of each acquisition shall be not greater than the borrower's existing system at the time it receives its first loan from the telephone bank, taking into account the number of subscribers served, miles of line, and plant investment.

"(b) Loans under this section shall be on such terms and conditions as the Governor of the telephone bank shall determine, subject, however, to the following restrictions:

"(1) All loans made hereunder shall be fully amortized over a period not to exceed fifty years.

"(2) Notwithstanding any other provision of law, all loans made pursuant to this Act for facilities for telephone systems with an average subscriber density of three or fewer per mile shall be made under section 201 of this Act but this provision shall not preclude the making of such loans from the telephone bank at the election of the borrower.

"(3) Intermediate loans shall bear interest at a rate equal to (i) a rate determined by the Secretary of the Treasury, taking into consideration the current average market yield, during the month of May preceeding the fiscal year in which the loans are made, on outstanding marketable obligations of the United States with remaining periods to maturity comparable to the average maturities of such loans, or (ii) 4 per centum per annum, whichever is lower. All other loans made hereunder shall bear interest at a rate which shall reflect the average cost of moneys to the telephone bank, including (a) interest on its debentures, and (b) the return on funds provided by the United States for the purchase of class A stock pursuant to section 406(a) of this Act, and (c) administrative expenses, and (d) reserves, and (e) estimated losses of the telephone bank. Intermediate loans shall not be made to a borrower which is determined by the Governor of the telephone bank, under standards to be established by the Secretary, to be capable of both paying the interest rate applicable hereunder to loans other than intermediate loans and achieving the objectives of the Federal rural telephone loan program. The authority to make intermediate loans hereunder shall terminate on June 30, 1982, or such earlier date as conversion take place under section 410(a): *Provided,* That on or before July 1, 1972, the Secretary shall make a report to the President for transmittal to the Congress on the status of the intermediate loan program with recommendations concerning its continuation thereafter.

"(4) Loans shall not be made unless the Governor of the telephone bank finds and certifies that in his judgment the security therefor is reasonably adequate and such loan will be repaid within the time agreed.

"(5) No loan shall be made in any State which now has or may hereafter have a State regulatory body having authority to regulate telephone service and to require certificates of convenience and necessity to the applicant unless such certificate from such agency is first obtained. In a State in which there is no such agency or regulatory body legally authorized to issue such certificates to the applicant, no loan shall be made under this section unless the Governor of the telephone bank shall determine (and set forth his reasons therefor in writing) that no duplication of lines, facilities, or systems, providing reasonably adequate services will result therefrom.

"(6) As used in this section, the term 'telephone service' shall have the meaning prescribed for this term in section 203(a) of this Act, and the term 'telephone lines, facilities, or systems' shall mean lines, facilities, or systems used in the rendition of such telephone service.

"(7) No portion of any loan made under this Act shall be used to finance any political activities prohibited under sections 600, 601, 610, 611, and 612 of title 18, United States Code, and prior to the making of any loan the borrowing entity shall agree in writing not to engage in any such prohibited political activities during the term of such loan. If the Telephone Bank Board finds a violation of this provision to have occurred, it shall so notify such borrower in writing and thirty days thereafter such loan shall become due and payable in full.

"(8) Notwithstanding any other provision of law, no borrower of funds under section 201 or 408 of this Act shall, without approval of the Administrator, sell or dispose of its property, rights, controlling interest, or franchise to a holding company, until all indebtedness, including all interest charges, to the Rural Electrification Administration or the telephone bank shall have been repaid.

"(c) The Governor of the telephone bank is authorized under rules established by the Telephone Bank Board to adjust, on an amortized basis, the schedule of payments of interest or principal of loans made under this section upon his determination that with such readjustment there is reasonable assurance of repayment: *Provided, however*, That no adjustment shall extend the period of such loans beyond fifty years.

"SEC. 409. TELEPHONE BANK RECEIPTS.—Any receipts from the activities of the telephone bank shall be available for all obligations and expenditures of the telephone bank.

"SEC. 410. CONVERSION OF OWNERSHIP, CONTROL, AND OPERATION OF TELEPHONE BANK.—(a) Whenever after retirement of class A stock issued to the United States has begun pursuant to section 406(c) of this title, the total amount in stated value of class B and class C stock outstanding equals two-thirds of the total amount in stated value of class A, class B, and class C stock outstanding, as determined by the Secretary—

"(1) the powers and authority of the Governor of the telephone bank granted to the Administrator of the Rural Electrification Administration by this title IV shall vest in the Telephone Bank Board, and may be exercised and performed through the Governor of the telephone bank, to be selected by the Telephone Bank Board, and through such other employees as the Telephone Bank Board shall designate;

"(2) the five members of the Telephone Bank Board designated by the President pursuant to section 405(b) shall cease to be members, and the number of Board members shall be accordingly reduced to eight unless other provision is thereafter made in the bylaws of the telephone bank;

"(3) the telephone bank shall cease to be an agency of the United States, but shall continue in existence in perpetuity as an instrumentality of the United States and as a banking corporation with all of the powers and limitations conferred or imposed by this title IV except such as shall have lapsed pursuant to the provisions of this title.

"(b) When all class A stock has been fully redeemed and retired, loans made by the telephone bank shall continue to be subject to the restrictions prescribed in the provisos to section 408(a) (2).

"(c) Congress reserves the right to review the continued operations of the telephone bank after all class A stock has been fully redeemed and retired.

"SEC. 411. LIQUIDATION OR DISSOLUTION OF THE TELEPHONE BANK.—In the case of liquidation or dissolution of the telephone bank, after the payment or

retirement, as the case may be, first, of all liabilities; second, of all class A stock at par; third, of all class B stock at par; fourth, of all class C stock at par; then any surpluses and contingency reserves existing on the effective date of liquidation or dissolution of the telephone bank shall be paid to the holders of class A and class B stock issued and outstanding before the effective date of such liquidation or dissolution, pro rata, and any remaining surplus and contingency reserves shall be distributed to those entities to which they are allocated on the books of the bank at the time of the liquidation or dissolution."

SEC. 2. (a) Subsection (f) of section 3 of the Rural Electrification Act of 1936, as amended, is amended by inserting "rural electrification" immediately following the words "interest on" in both places where it appears in said subsection and by inserting the words "for rural electrification purposes" after the words "Secretary of the Treasury" the second time they appear in said subsection.

(b) Section 201 of the Rural Electrification Act of 1936, as amended, is amended by inserting "to public bodies now providing telephone service in rural areas", immediately after the word "areas" in the first sentence and also immediately after the word "areas" in the first proviso of the second sentence.

SEC. 3. Section 201 of the Government Corporation Control Act, as amended (31 U.S.C. 856), is amended by striking "and" immediately before "(5)" and by inserting "and (6) the Rural Telephone Bank" immediately before the period at the end.

SEC. 4. The second sentence of subsection (d) of section 303 of the Government Corporation Control Act, as amended (31 U.S.C. 868), is amended by inserting "the Rural Telephone Bank," immediately following the words "shall not be applicable to".

SEC. 5. The right to repeal, alter, or amend this Act is expressly reserved.

SEC. 6. This Act shall take effect upon enactment.

STATEMENT OF HAROLD R. BOLLINGER, PRESIDENT OF PIONEER TELEPHONE CO. (A MINNESOTA CORPORATION); ACCOMPANIED BY ROBERT FEGAN, PRESIDENT OF THE JUNCTION CITY TELEPHONE CO. (KANSAS); AND HUGH BARNHART, PRESIDENT OF THE ROCHESTER TELEPHONE CO. (INDIANA)

Mr. BOLLINGER. Mr. Chairman and members of the committee, before I read my testimony, I would like to introduce my associates who are here with me.

On my right is Hugh Barnhart, president of the Rochester Telephone Co., of Indiana, and on my left is Mr. Robert Fegan, president of the Junction City Telephone Co., of Kansas. And I am Harold R. Bollinger. All three of us have had a long and continuing, and very sincere, interest in the telephone industry—the independent telephone industry.

We welcome this opportunity to appear here before you to present our facts on this legislation, this proposed bill.

As it is presently drafted we would be opposed to it, but with minor amendments, which we will comment on here shortly, we would support this bill.

Also associated with us are the companies listed as follows:

Pioneer Telephone Co., Minnesota.

Central Telephone Co. and affiliates.

Ellensburg Telephone Co., Washington.

General Telephone & Electronics Corp.

Geneseo Telephone Co., Illinois.

Illinois Consolidated Telephone Co., Illinois.

Junction City Telephone Co., Kansas.

Lincoln Telephone & Telegraph Co., Nebraska.

Rochester Telephone Co., Inc., Indiana.

United Utilities, Inc.,

Urban Telephone Corp., Wisconsin.

Viroqua Telephone Co., Wisconsin.

These companies also support the position which we will present to you.

Mr. Barnhart, on my right, operates the Rochester Telephone Co., Inc., of Indiana, and he has in this one exchange 4,600 telephones.

Mr. Bob Fegan, on my left, operates the Junction City Telephone Co., of Kansas, and he has five exchanges of 9,000 telephones. Both of these gentlemen have long and continuing interest in the business: Mr. Barnhart since the early 1930's, and Mr. Fegan since the 1920's. Also Mr. Fegan's father started the telephone company in Junction City in 1910. Both of these gentlemen have been active in the association's affairs, both in their own States and in the national association. Mr. Fegan served as a director of our national association for a number of years. Mr. Barnhart is presently a member of the board of directors of our national association and also a past president.

My own company operates in Minnesota and North Dakota, and we have 52 exchanges. We operate 54,000 telephones.

I will now proceed with my prepared statement.

Mr. Chairman, members of the committee, I am Harold R. Bollinger, president of Pioneer Telephone Co., a Minnesota corporation, which will become a United Utilities, Inc., subsidiary later this year. With me today are Robert Fegan, president of Junction City Telephone Co., of Kansas; and Hugh Barnhart, president of the Rochester Telephone Co. of Indiana.

I have been president of Pioneer since 1963. Between 1945 and 1963, I was vice president and general manager, the chief operating executive, of Pioneer. My telephone career started in June of 1922, and between that date and 1963 I worked principally in rural telephone exchanges in Minnesota, Iowa, Illinois, and Wisconsin.

In keeping with my longstanding interest in the independent telephone industry which serves principally the smaller communities and rural areas of America, I was president of the Minnesota Telephone Association in 1954 and 1955, and was president of the U.S. Independent Telephone Association (USITA) for the 1962-63 term.

The telephone companies which I have already named and which appear on the cover sheet of this prepared testimony have asked me to present to you this statement on behalf of all of us. After you have heard my presentation, if any of the committee members have questions concerning our position on any aspect of this proposed legislation, as related to rural telephone company operations, we will attempt to answer them for you.

Mr. Chairman, first let me assure you we are not here to oppose the broad objectives of H.R. 12066. We are here to suggest and recommend some clarifying changes and some amendments to the bill which, we believe, will better serve the interest of the public and rural telephony.

The Rural Electrification Act provides a needed source of financing for telephone companies which serve the more sparsely populated rural areas. Certainly, low-cost loan funds are necessary if adequate service is to be provided in exchange areas where there may be three or fewer subscribers per square mile and a low level of economic activity and development.

On the other hand, however, there is no requirement for low-cost loan financing in populous and prosperous areas. In these instances, it is clearly feasible to provide adequate telephone service because the revenues will support loans obtained from conventional private sources.

There is a middle group between these two extremes, however, where the telephone companies cannot finance the construction of adequate facilities through conventional private sources. Consequently, these companies are confronted with the dilemma of sacrificing the quality of their service or of jeopardizing the financial stability of their business. On the other hand, the needs of these companies are not so great as to warrant granting them the full Government subsidy of 2 percent REA loans.

Many of the companies in this middle group have borrowed large sums from the REA because they were unable, and in some cases unwilling, to obtain all of the funds they required from private sources. A large portion of these funds would undoubtedly have been borrowed from private sources if only that portion of their property for which the REA loan was obtained was required as collateral for that loan, rather than all of their property. The amounts Congress appropriates for 2 percent telephone loans could be much smaller if these companies were not, in effect, "locked in" to REA financing.

The ease with which companies in this middle group have been able to obtain 2 percent REA loans has enabled some of them to purchase and install modern telephone plant and equipment solely for the purpose of converting their companies into salable commodities in a "sellers market". Aside from the fact that the existing REA loans continued after the companies were sold, additional 2 percent loans were obtained by the acquiring companies.

The advantages of 2 percent debt money in the capitalization of a highly leveraged company are obvious. The amounts of loan funds Congress is asked to appropriate would be greatly lessened if all companies were required to make full use of their abilities to obtain private capital to meet the needs of their operations and of the operations of any companies they own.

The annual requirements for telephone loans could be further reduced if REA borrowers were not required, as conditions of receiving an REA loan, to provide facilities for higher grades of service than the standards established by the regulatory authorities in the various States—or, for that matter, a higher grade of service than the telephone subscribers want. It goes without saying that this results in higher rates than the economies of the areas can reasonably support. Some such companies find themselves required to borrow much more money than they need, and to install more facilities than necessary to meet their service requirements. Greater emphasis on meeting real telephone service requirements at the lowest practical cost would reduce the amount of REA loans required even by companies with a justifiable need for 2 percent money.

The elimination of this and the other shortcomings we have mentioned would substantially reduce the amounts that Congress is asked to appropriate for the REA telephone loan program. Correction of these faults in the telephone loan program would require changes in both the act and the administration of the act. It would be impractical in our estimation to attempt to make the necessary corrections by amending the act to prescribe the loan procedures in detail.

We believe that the needed corrections can best be made through passage of H.R. 12066 provided the following three basic considerations are incorporated in the bill: (1) to insure that the proposed rural telephone bank is oriented toward the segment of the telephone business it is designed to serve; (2) to insure that the telephone bank's loan policies and conditions will be established by people who have knowledge of the public purposes and obligations as well as the economics of the telephone business; and (3) to insure that the telephone bank will be independent of the need for Government funds at the earliest possible date.

To incorporate these three basic considerations, we urge the Committee to adopt certain specific changes in H.R. 12066. We firmly believe that the changes which we now recommend will clarify and facilitate the intent of the bill and overcome the weaknesses in the present telephone loan program:

1. Preamble, page 1: We believe there may be fewer telephone companies actually requiring financing under title II of the act than is indicated by loan requirement studies available to the committee. We suggest the Preamble be changed by substituting the word "some" for the word "many" in line 9.

2. Section 302(b), (1), page 4: We suggest that it is the intent of H.R. 12066 that the REA Administrator grant section 201 loans only when the applicant cannot reasonably afford to borrow money from the rural telephone bank or pay the going rate of interest on telephone bank loans, whichever is applicable. Therefore, we suggest the intent of this bill can be clarified in lines 13 and 14, by striking out all of the last phrase, "the amounts so" and ending with "until expended."; and substituting in its stead the phrase, "and no such loans shall be made if the applicant for a loan under Section 201 can qualify under the policies, terms, and conditions established for rural telephone bank loans by the telephone bank board."

3. Section 403(b), page 8: The full administrative costs of the bank's activities should be borne by the bank. This can be made clear in line 10, by striking out the last two words, "without cost", and in their stead inserting, "and the cost of such facilities and services shall be charged."; and in line 11, by striking out the words, "without charge to", and in their stead inserting, "shall be"; and in line 13, by striking out, "but", and inserting, "and", in its stead.

4. Section 405(b), page 10: We believe Congress should give the President the right to select telephone bank board members from the Treasury, Bureau of Budget, Comptroller General, and other governmental departments, as well as the Department of Agriculture, in the interest of obtaining the most qualified personnel to assist in establishing and managing the bank. This would be accomplished in lines 3, 4, and 8, by striking out, "Department of Agriculture", and substituting, "Federal Government".

5. Section 405(d), page 11: We believe that the bank board representation should be in proportion to the relative number of commercial-type and cooperative-type REA borrowers. At present there are three commercial-type borrowers for every one cooperative-type borrower. We suggest the bill recognize this differential in:

Line 5, by striking out, "three", and substituting, "two", in its stead;

Line 8, by striking out, "three", and substituting, "four", in its stead;

Line 17, by striking out "three", and substituting, "two", in its stead; and

Line 20, by striking out, "three", and substituting, "four", in its stead.

6. Section 406(c), page 14: Hopefully, the full \$300 million in class A stock will be subscribed by 1977, at which time, we believe, it is the intent of Congress to encourage the conversion of ownership, control, and operation of the rural telephone bank to the private sector of the economy. We recommend in:

Line 20, changing the date from "1982" to "1977";

Lines 24 and 25, and page 15, line 1, striking out "and after the amount of class A and B stock issued totals \$400,000,000".

7. Section 406(c), page 15: To emphasize the intent of Congress to make the rural telephone bank self-sustaining, we believe the wording should be changed in:

Lines 3, 4, and 5, by striking out the remaining portion of the sentence after the word "income" on line 3, and substituting therefor, "at a rate determined by the Secretary of the Treasury, to equal the average market yield on marketable obligations of the United States issued during the month of May preceding the fiscal year in which the class A stock was issued."

8. Section 407, page 17: Because the telephone bank debentures would not be guaranteed by the United States, in our opinion it would not be in the public interest, or consistent with the intent of Congress to make the bank-self-sustaining, to permit investment of fiduciary, trust, and public funds in such debentures. It is our opinion that the language should be changed in:

Lines 20, 21, 22, 23, and 24, by striking out the last sentence beginning on line 20 with the words "Telephone debentures" and ending with the words "officers thereof", on line 24.

9. Section 408(a), page 18: We do not believe that either the Secretary or the Administrator should be put in the position of being the sole judge in determining whether the proposed acquisition of other telephone lines, facilities, and systems by an REA borrower with REA money would result in improving the efficiency, effectiveness, or financial stability of the resultant combined telephone system. We are convinced that it is in the best interests of all concerned to give the telephone bank board a voice in matters of such significance in order to prepare for an orderly conversion of the telephone bank to private ownership, control, and management. Even though we believe that as a matter of general principle no "acquisitions" should be made with money provided by the Government, we recognize that some acquisitions may sufficiently involve the public interest to justify financing them with loans under section 201 or section 408. Therefore, we suggest that this provision be clarified in:

Line 18, by inserting between "the" and "Secretary", the phrase "Telephone Bank Board and the", so that this provision will read, "the Telephone Bank Board and the Secretary".

10. Section 408(b), (1), page 19: Technical and economic obsolescence are more pronounced now in the operation of telephone companies than in any other public utility industry. Despite this situation, REA loans today extend for 35 years, which is longer than the expected life of the property serving as collateral for the loans. If additional loans are made to finance replacement of obsolete equip-

ment before the original loans on such equipment are repaid, the total of the original and supplemental loans will exceed the value of the borrower's plant and property. This situation already exists with respect to many of the present REA borrower telephone companies. H.R. 12066 provides for extending loans for even longer than 35 years. Therefore, we suggest amending this section in: line 5, by changing "50" to "35".

11. Section 408(b), (2), page 19: Experience indicates that private capital has been used profitably to furnish telephone service meeting the standards of the regulatory bodies in the various States, and reflecting the grade and quality of service desired by the subscribers even though the average subscriber density may be as low as three per square mile. One such case is specifically cited in exhibit 1.

I would ask you to turn to the exhibit which is on the backside of the testimony. This exhibit is of our own Pioneer Telephone Co., in North Dakota. I would like to briefly go through some of the highlights in this exhibit.

Line 1, the number of exchanges, the number is 10.

Line 2, we show the total area served in square miles. In 1950, it was 1,031; by 1966, this had increased to 1,291, and that is the square miles served today.

Line 3, the average subscriber density per square mile. In 1950, it was 2.4; in 1966, 3.3.

Under "Operations results", I would just like to point out a few items that will emphasize several things. First, it will emphasize the need that existed in 1950 for our REA program.

Looking down to the bottom you will see the rate of return: In 1950, it was 2.66. The plant in service, at the very top, was \$388,959. Now, you will notice, going down to item 4, "Revenues" under "Operations results", the exchange revenue on a telephone basis per station was \$34.15, and toll revenue was \$6.27 per station, or \$40.59 total for the station.

Now, we move over, going along the top line, and you will notice that the investment increased from \$388,959 to \$983,517 in 1955; to \$1,282,789 in 1960, to \$1,789,319 in 1965, and at the end of 1966, it was \$1,908,356.

Going straight down under "1966", you will find that the total revenues per telephone in 1966 were \$25.62. The difference between \$6.27 and \$25.62 is a very important factor as to the difference between independent telephone operations in rural areas in 1950 and in 1966. This \$25.62 has made a great difference in our operations.

Now, to prove the point, look down to the bottom line and you will find that in 1955 we earned a rate of return on the rate base of 5.51, in 1960, the dial conversions were completed and we earned 7.49; 7.66 in 1965, and 7.85 in 1966.

Also, I would like to call your attention to the importance of a good corporate citizen like this, even though it is operated in a relatively marginal area with 3.3 subscribers per square mile.

Under "Operating expenses", item 5, note the item "(c) Taxes". The taxes paid by the operation of 4,238 main stations was \$95,330, or \$18.28 per station.

I offer that as proof that a great change has taken place in rural telephony between the years 1950 and 1966.

(Exhibit 1 submitted by Mr. Bollinger is as follows:)

EXHIBIT I.—PIONEER TELEPHONE CO., NORTH DAKOTA OPERATIONS—SELECTED OPERATING STATISTICS FOR YEAREND-1950, 1955, 1960, 1965, AND 1966

		1950		1955		1960		1965		1966	
		Total	Per station	Total	Per station	Total	Per station	Total	Per station	Total	Per station
IV. Operations results											
1. Number of exchanges											
II. Total area served in square miles:											
1950											
1966											
III. Average subscriber density per square mile:											
1950											
1966											
4. Revenues:											
(a) Exchange											
(b) Toll											
(c) Total											
5. Expenses and taxes:											
(a) Depreciation											
(b) Operating expenses											
(c) Taxes											
(d) Total operating expenses											
6. Net operating income											
7. Rate of return											

Source of information: North Dakota Public Service Commission annual reports for years ending Dec. 31, 1950, 1955, 1960, 1965, and 1966.

Mr. BOLLINGER. Returning now to my testimony, I will continue:

Therefore, we do not believe it is the intent of Congress to authorize use of section 201 loan funds by a telephone system serving an average subscriber density of up to 12 per square mile, which is our interpretation of the presently worded density criteria "of three per mile."

We are of the opinion that the intent can be clarified in: Line 9, by inserting "square" between "per" and "mile", and changing "shall" to "may". Line 9 will then read "of three or fewer per square mile may be made," and so forth.

12. Section 408(b), (3), page 19: If an REA borrower cannot afford to pay a rate of interest equal to the cost of money to the Government, the borrower should be covered under section 201 until the ability to pay such a rate is established. A number of the present REA borrowers have told us they can now afford to pay the conventional loan cost of money and would obtain such conventional financing if they were not impeded by the "first lien" requirements of the loan agreements and indentures required under the present act. We suggest the wording be amended in: Line 14, by striking out (i); and in lines 20 and 21, by striking out "or, (ii) 4 per centum per annum, whichever is lower."

13. Section 408(b), (3), page 20: We believe it was the intent to make the period during which intermediate or subsidized loans are made available the same as the 10-year minimum period during which the Government can subscribe up to the \$300 million maximum amount of class A stock. Therefore, the intermediate loan period should end at the same time the ownership, control, and operation of the telephone bank can begin to revert to the private sector by redemption of the class A stock. We believe that this intent can be expressed in:

Line 12, by changing "1982" to "1977."

14. Section 408(b), (3), page 20: We believe it is the intent of the proviso that the Secretary report to the President regarding the need to continue the intermediate loans at the end of the initial 5-year period of the rural telephone bank operations. We suggest this intent can be clarified in:

Line 17, by striking out the last word of the sentence, "thereafter" and inserting the phrase, "after the date of such report."

15. Section 408(b), (8), page 22: For reasons given earlier in connection with our recommended change in section 408(a) on page 18, concerning the inadvisability of sole approval authority resting with either the Secretary or the Administrator, we recommend that the language of 408(b), (8), on page 22 be clarified in:

Line 3, by deleting "Administrator" and substituting therefor "Secretary and the Telephone Bank Board."

16. Section 408(b), (8), page 22: We believe that H.R. 12066 is intended to require, in general, repayment of all obligations of the selling company to the REA or the telephone bank before acquisition of that company can take place. Therefore, we feel reference to holding companies only should be deleted to give more surveillance over such acquisitions to the Telephone Bank Board and the Secretary. The bill should, therefore, be clarified in:

Line 5, by striking out "to a holding company."

17. Section 408(c), page 22: For reasons given earlier in connection with our recommended change in section 408(b), (1), we recommend that section 408(c) be amended in:

Line 16, by changing "fifty" to "thirty-five."

This concludes our statement on H.R. 12066.

In addition to presenting these recommendations for your consideration, we sincerely hope that your committee will devote further study to the advisability of an "insured loan program" as a possible acceptable alternative to the establishment of a rural telephone bank.

Thank you.

The CHAIRMAN. Thank you very much.

Are there any questions of Mr. Bollinger or of any of his associates? Mr. Dole?

Mr. DOLE. First of all, I want to thank you, Mr. Bollinger, for an excellently prepared statement, and, secondly, I would like to discuss in more detail the first full paragraph on page 3 of your statement which starts with the words:

The ease with which companies in this middle group have been able to obtain 2 per cent REA loans has enabled some of them to purchase and install modern telephone plant and equipment solely for the purpose of converting their companies into salable commodities in a "seller's market".

Do you have any specific examples that might be helpful to the committee?

Mr. BOLLINGER. I would like to present some information from a bulletin, an institutional service report that makes reference to the problem that you raise. I would like to read from this investment bulletin. The company that they are referring to has different interests, among them telephone operation.

Referring now to the telephone division it states:

This is a highly leveraged operation, and Apache has been able to finance the expansion of the division without the help of equity capital. Of a net asset value on December 31, 1965, of \$16,000,000, \$10,200,000 was financed by the Rural Electrification Administration (REA) at 2 per cent, and \$4.4 million was financed primarily by the Kellogg Credit Corporation, a subsidiary of International Telephone and Telegraph; the remaining 9 per cent represented Apache's investment and minority interest.

I think the emphasis should be put on the fact that no effort was made to raise equity capital.

Mr. DOLE. The question I had in mind is in reference to your statement that borrowers may borrow money from the REA to improve their property so that it can be sold at a big profit. This disturbs me, and it did before this bill was in this committee.

Are there any specific examples where a borrower has borrowed money from the REA and then sold it at a large profit?

Mr. BOLLINGER. I do not have any specific examples here with me. We would rather not name names, but these facts are readily available in trade magazines. We could supply the committee evidence in this direction very easily.

Mr. DOLE. In the July issue of Forbes magazine, there is an article—and I hesitate naming names, but this is an article about Continental. I recognize there are complications here, and also recognize that some of the companies involved did not borrow money from the REA at 2 percent, but in this article on page 45 Mr. Wohlstetter states:

We have over \$100,000,000 of 2 per cent REA (Rural Electrification Administration) debt that we inherited from other companies. What's better, 6 percent on \$50 million or 2 percent on \$100,000,000? What does a debt equity ratio mean

in that context? But you have to weigh in balance the total cost of carrying your debt. That 60-40 ratio gives you a pretty good play in the first place.

And then the article continues on.

He is boasting about the debt-equity ratio. Frankly, I do not believe the purpose of the Telephone Act is to permit Continental, or any other company to pay high prices for a company financed by the REA. I understand you would correct this situation, and while it is not illegal, it is something that should not be permitted in my opinion. You would correct that by striking out on page 22, line 5, the words "to a holding company"; is that correct?

Mr. BOLLINGER. That is correct. We believe that it should be broadened to include everybody.

Mr. DOLE. What about an alternative, the words "to a holding company", leave it in line 5, and strike out the words "without approval of the Administrator" in line. In other words, make loans possible but not until all of the business debts have been repaid.

Mr. BOLLINGER. It would be a strong safeguard; it would be a strong safeguard.

Mr. DOLE. Would that satisfy the objection you have?

Mr. BOLLINGER. I think, largely it would. We would like to see this put in there, because the way it is presently drafted, as you pointed out, it is with reference to holding companies. We think that it would firm up the situation if we broadened this to include everybody.

Mr. DOLE. I doubt we have the right to prohibit the sale of property, but we can put in a condition precedent to require that all obligations must be paid before the sale is approved.

Mr. BOLLINGER. Yes, sir.

Mr. DOLE. Again, I would not suggest the committee to put such a restraint on all sales of property, but do believe this loophole could be closed by requiring all indebtedness to be repaid. I offered such an amendment earlier without success, but since then there has been further evidence that, perhaps, this is an area that needs closer scrutiny by our committee.

Mr. BOLLINGER. Yes, sir.

Mr. DOLE. Do you think that might serve the purpose?

Mr. BOLLINGER. I think that it would be most effective, very effective. I think it would help the industry, help the public interest.

Mr. DOLE. There is some thought in my area, at least by some companies, that there may be no small companies left. We have some responsibility to make certain money available at 2 percent but that it is not loaned for the purpose of sale or the rebuilding of a company for the purpose of resale. There is merit in small telephone exchanges, in Kansas, as well as in other places.

Mr. BOLLINGER. We have some small telephone companies up in my part of the country, in Minnesota especially. They are small, less than 2,000 telephones, that are being excellently managed and operated.

Mr. DOLE. You also point out in your statement that apparently when you borrow money from REA you give a mortgage on all of the property? Is that correct?

Mr. BOLLINGER. That is right; that is my understanding.

Mr. DOLE. Even though the loan may not be near the value of the property. You suggest as an alternative then, to enable the borrower to go somewhere, if it were not for the first lien.

Mr. BOLLINGER. It would be very helpful if that could be worked out.

Mr. DOLE. How would you accomplish this?

Mr. BOLLINGER. I do not have a suggestion to offer, sir. I was just suggesting that would be desirable. I hope that it can be done.

Mr. DOLE. I am not certain what would be involved; what relation that might have to the value of the property involved. I can see that you tie up the property if the Administrator had a first lien on everything—

Mr. BOLLINGER. I can give you an example: A very good friend of mine operates a telephone company CACEC—it was formerly a cooperative, but the directors and the stockholders changed it into a taxpaying corporation about 3 or 4 years ago. These people need capital and want to borrow, but they will not borrow any more at 2 percent. If this bank bill can be passed it will be just what this company needs. They are able to pay more. They will not borrow any more 2-percent money. They do need capital.

Mr. DOLE. Then, finally, on page 8 of your statement, item 11, you talk about making a change, and before the word "mile" to put the word "square". Perhaps if you would clarify that further, it would be helpful.

Mr. BOLLINGER. Again, I refer to my own experience. I cannot help but emphasize what we have really done. This is a case history of what can be done if you roll up your sleeves and go to work, and this, frankly, in 1950 was a prize candidate for a loan from REA. The evidence speaks for itself. But we decided it was our obligation to give it a try on a private enterprise basis. I will admit that along about 1955 we wondered whether we had really tackled more than we could bite off, but when we got to about 1956 or 1957, it became clear to us that our attempts were going to be rewarded—that we were going to be rewarded for what we had done, and the record as seen for 1960 proves that you can accomplish a great deal if you really roll up your sleeves and go to work.

I would like, also, as long as we are looking at that exhibit again, now to refer to item 2 under "Telephone Operation." It is the percent debt. I would like to emphasize to the members of the committee that in 1950, when we first started, we were struggling so hard, that the debt ratio, the amount of debt on this operation, was 41.9 percent; in 1955, it had risen to 55.6 percent; in 1960, to 43.5; and 1965, 50.4, and presently it is 50.8, at the end of 1966. So, we were maintaining a good debt ratio.

Mr. JONES of Missouri. Will you yield for a question?

Mr. DOLE. Yes, sir.

Mr. JONES of Missouri. You said a minute ago, if I did not misunderstand you, that this friend of yours did not want to borrow money at 2 percent; that he wanted to borrow money from a bank at a higher rate of interest.

Mr. BOLLINGER. He is one of these that I described as being locked in. It is necessary for him to come to the REA for further financing, under the present circumstances, but he does not feel right about borrowing the money from the Government, the REA, at 2 percent. He wants to pay more, and we think that perhaps this bank will solve this problem.

Mr. DOLE. Is he in good health? [Laughter.]

Mr. KLEPPE. This fellow is from North Dakota, I am sure. I am glad to see this report on someone in North Dakota, because this is my State. They do have a lot of feeling and an attitude out there that they should make things go if they can make them go—If you will yield, Mr. Dole?

Mr. DOLE. Yes.

Mr. KLEPPE. I do have a question about your density question in here. When you talk about square miles, how can you measure telephone lines on a square mile basis?

Mr. BOLLINGER. What we do is count up the square miles served and divide this into the number of main stations. Here we use main stations.

Mr. KLEPPE. The bill that we have before us contains "miles."

I was interested in this density provision that we have in here, which provides for three per mile, and when you say three per square mile, you are then, in effect, saying three-fourths of the bank subscribers per lineal mile; is that correct?

Mr. BOLLINGER. It could be. It is a varying thing. That is why I did not like the description of three per mile, because it is a mile of line. If there were lines all round the perimeter of this section it could amount to 12. I use that.

Mr. KLEPPE. I gathered that, from your statement.

Mr. BOLLINGER. But it would be real easy for your committee or the REA to administer the act if it were square miles, because we would just take the number of main stations and divide it by square miles, sir, it really only requires two factors before you count up the square miles and divide it into the subscribers, and you have got it. I think that this exhibit proves that something around three per square mile can be operated profitably.

Mr. KLEPPE. You certainly are to be commended for this operation, to say the least, because, like you say, I can see that the figures speak for themselves.

Let me ask you this: Is it not true that the expense you have shown on this exhibit here for the Pioneer Telephone Co. operations in North Dakota, is not necessarily applicable to the rest of the REA operations in North Dakota, that is, the telephone operations?

Mr. BOLLINGER. I would readily admit that. Going west from where we operate it gets more marginal all of the time.

Mr. KLEPPE. This is a point that I am making. The density here, of course, plays a very important part.

Mr. BOLLINGER. I am sure that the density of those operations west of us would not run more than two per square mile.

Mr. KLEPPE. It is less than that.

Mr. BOLLINGER. I am sure it is in some places, where it would be one or less than that.

Mr. KLEPPE. The reason I am studying this is because the need, from the standpoint of serving customers, is quite a bit greater in the western part of the State than it is in the eastern part of the State.

Mr. BOLLINGER. Yes, sir.

Mr. KLEPPE. Thank you. That is all.

Mr. DOLE. I have just one other question.

I think you have made it very clear that you do support the broad objectives of H.R. 12066; is that correct?

Mr. BOLLINGER. That is absolutely right. Very clearly, we really do.

Mr. DOLE. And the suggestions, or the amendments that you make, are made in that spirit, of improving the bill and not crippling the bill?

Mr. BOLLINGER. Definitely, very definitely. We are hopeful that these can be approved by your committee, worked into the bill. We think that we have a real solution to the industry problem.

Mr. DOLE. That is all. Thank you.

The CHAIRMAN. I do not understand what this argument is about. As I see it, you are discussing the rules of the REA which are not involved in this bill at all, because this bill simply sets up a bank that makes loans under the rules set out in this legislation.

Mr. BOLLINGER. Right.

The CHAIRMAN. And it does not change the rules under which the REA is operated.

Mr. BOLLINGER. Right.

The CHAIRMAN. We are criticizing the policy of the REA in requiring a lien on all of the properties of a borrower. As I understand it, this makes it more difficult for the borrower to get private money as has been stated. This is the same rule that you have in the Farmers Home and with all of these other credit institutions. When a man borrows from the Farmers Home, for example, he cannot borrow from the Farmers Home as long as he can borrow from someone else. If he can get conventional credit, he cannot borrow from the Farmers Home, and if he borrows from the Farmers Home and reaches the point where he can get credit from the bank, he can no longer borrow from Farmers Home. At that point Farmers Home will probably have a mortgage on his tractor. The bank making the new loan pays off the old loan and takes a mortgage. What prevents these people who have that good credit, what in the world keeps them from going out and making a conventional loan, if they want a conventional loan?

The REA does not refuse to take the money, does it?

Mr. BOLLINGER. I think that you have pinpointed the problem; I think that it ought to be studied in that light. I think that a solution could come from that.

The CHAIRMAN. I say that the REA has never been known to refuse to accept money. Have they?

Mr. BOLLINGER. No. These folks would not be in a position to pay off the loan. It is just that they should be free so that they can raise capital otherwise.

The CHAIRMAN. If they can get more capital, they can pay off. If you have a \$100,000 loan and you have \$200,000 worth of property, and if you can borrow another \$25,000, you can borrow \$125,000 as a first lien.

Mr. BOLLINGER. I think that there would be very, very few that would be strong enough financially to do that—a very few.

The CHAIRMAN. They do not have to be strong. If they are strong enough to get new and additional credit, they are strong enough to get it all from the bank.

Mr. BOLLINGER. Well, you are going farther than I would say is possible, but the philosophy that you are expressing is the philosophy that I think ought to be followed to the extent possible.

The CHAIRMAN. I am asking you this: Why can you not borrow right now?

You are complaining that it cannot be borrowed; that we are keeping them from financing with the banks; you are complaining of that.

Anybody who has enough equity to get a second lien \$25,000 credit with a \$100,000 first lien, can get \$125,000 first lien credit.

Mr. BOLLINGER. There might be a few that could do this, but you are asking a great deal of that borrower.

Mr. BELCHER. Would you yield?

The CHAIRMAN. Yes.

Mr. BELCHER. My understanding was that they are not willing to loan the \$25,000 on the second mortgage; they would be willing to loan it on the first mortgage. And you say that they would loan \$125,000 on a first mortgage.

The CHAIRMAN. They would. They would loan \$125,000 on the first mortgage, if they loan them \$25,000 on a second mortgage behind \$100,000 first lien.

Mr. BELCHER. They want it on the first lien.

The CHAIRMAN. That is not what he is complaining about. He is complaining that he already has this loan, and that is the reason that the man could not get it, though he has the credit to go out and get it, but the REA has all of his property mortgaged, and, therefore, he could not use the equities that he has accumulated to make a new loan.

All I am saying is this, and I will defer to my banker friend—I think he knows more about this than I do. I have never been a banker but I have been on the borrowing end, and I have been able to get a fellow make me a second-lien loan, but the same man would prefer to take a first-lien loan.

Mr. BOLLINGER. Bear in mind that the loan the man presently has is at 2 percent interest rate. When he converts that to private capital, the \$25,000, using your example—plus the \$100,000 that he has already borrowed—there is a great deal of change.

The CHAIRMAN. I understand full well why the man does not want to pay off the REA loan. I understand full well why he does not want to pay it off, but I do not understand this talk of this inability to get a private loan if he has security for it.

You have just told us how these people wanted to pay the higher interest rate.

Mr. BOLLINGER. Yes, sir.

The CHAIRMAN. And suggested the REA loan kept them from paying the higher interest rate. The REA never kept any man from paying a higher interest rate if he wanted to pay it. All he has to do is to get somebody to take that loan and pay the higher interest rate.

Mr. BOLLINGER. Yes, sir.

The CHAIRMAN. If he has the equity.

He is talking about where they have accumulated additional equity. He is talking about where they have built up additional equity. Of course, he could not go out and get a loan even at 12 percent if he does not have the equity, but if he has the equity he can get the loan at a higher interest rate.

Mr. MYERS?

Mr. MYERS. I think that what Mr. Bollinger is suggesting here is that the REA should relinquish their first lien in two ways: either take an equal amount, which is not in the best interest of the Federal Government's security, and then release part of the collateral so that

somebody else can make the loan. They do not want to give up 2 percent. That is the first thing. They want to keep their loan of \$25,000. But you would like to see the REA release enough security or collateral so that somebody else can come in and make some supplemental financing. Is that not what you are actually saying? This is the first thing.

Mr. BOLLINGER. Yes, sir.

Mr. MYERS. They want half a loaf. They each want to have their cake and eat it. This is true. They could give it up. I do not think that any banker would come in and make a second mortgage; I do not know of any bank that can make a second mortgage legally. They cannot come in and take a second mortgage with collateral that is already pledged to the REA.

What you are asking is that the REA relinquish part of the security.

Mr. BOLLINGER. That is what I am suggesting. I think it would be a great help. I am not certain that it can be done.

The CHAIRMAN. Let me ask you: Why should the REA reduce its security. You want the REA to carry it and you want the REA to make the low-interest-rate loans and take all of this risk, whereas we say to the one-gallus farmer down here in the country who has a loan with the Farmers Home Administration—we say to him, "Now, you can get credit from the bank and you pay us off and let the bank carry you." And the bank does in many instances when he gets in better shape. They take a lien on the same tractor that the Government had and pay off the Government. Why should not the telephone companies do as much as the poor one-gallus farmer does?

Mr. BOLLINGER. I think that it is a legitimate criticism, but I do know something about the ability of these companies to pay.

The CHAIRMAN. All right. Is it any better than that one-gallus farmer?

Mr. BOLLINGER. It is comparable.

The CHAIRMAN. All right. Why do you want better treatment than that which you extend to that farmer?

Mr. BOLLINGER. I subscribe fully to your criticism of my suggestion. I think it is all right, but I think that my suggestion would help this borrower finally to get into the position, as you say that he ought to get into right away, and I think that it would help him. Maybe he could gradually get over there if this would help him.

Let me give you an idea why some of the borrowers are in a little bit of a difficult strait: In 1964—this would be in 1965, I got from the North Dakota Public Service Commission some figures on three companies in North Dakota. These are all borrowers. Here is the percent of debt to net plant at the end of 1964, 128.6—debt to net plant, 115.8 percent, 103.2 percent, while my operation up there was 49 percent. Now, with the 49 percent debt ratio I would be free to do what you are suggesting, Congressman Poage, but when you get into such straits as the others were, no.

The CHAIRMAN. They would not be able to borrow from anybody else under those circumstances. There is no collateral. Obviously, there is no banker or any credit institution of any kind that will make such a loan. If you do not have any equity, you cannot expect to get a loan.

Mr. MYERS. How do you get that way?

I do not think that we are going far enough here, if we get into that shape.

Mr. BOLLINGER. These are from North Dakota sources.

Mr. KLEPPE. It is always possible to do this with Government funds.

Mr. MYERS. I do know that the Farmers Home Administration does do some of this. I do not know why they do it. Anytime that you borrow from two sources, there is a possibility of trouble. Neither side knows exactly what is happening. I do not think that it is really fair. I do not completely agree with your testimony here. I think that you should go one route or the other, preferably this financing that does not come from the Treasury, if they can do it. But the Farmers Home Administration does do some of this. They release collateral once in a while, and they do it in anticipation of their getting out themselves. They do not do it unless they see that in the very near future that they can get out. I must give them credit for that. They tell their borrowers not to borrow from the FHA if they can borrow from private sources. I do compliment them for that. Not everyone does this. The Farmers Home Administration, in my experience locally in Indiana, has done a pretty good job of doing this. And I think they do it, always in anticipation of getting out of it.

The CHAIRMAN. And they will probably finance others, that is, for a given period of time.

Mr. MYERS. It is always with a written agreement that both the FHA and the financing bank understand the arrangements.

Mr. DOLE. Will you yield?

Mr. MYERS. Certainly.

Mr. DOLE. I am not certain just what the value of the property might have been and what the loan might be. I do not see any reason that the security be 10 times the amount of the loan. I think that as long as the agency is protected it is all right when the mortgage is three times the amount of the loan, that is, the property value, and they are protected. They do this with a person or corporation in the private sector. There they have a first lien on it.

Mr. MYERS. If the debt ratio is over 100 percent, they should not. Equity is not there.

Mr. KLEPPE. Will you yield?

Mr. MYERS. I yield.

Mr. KLEPPE. If you are on the lender side of the loan, it does not make any difference what the collateral is if the borrower expects to pay it off. All of the collateral in the world does not make any difference, so long as he expects to pay it off. What we are talking about here is the possibility of allowing a borrower to go out and get additional funds if he already has an REA loan. This is what we are talking about here. And I think you indicated that it might, you thought, not be impossible but probably improbable. You think that is exactly where the difficulty is, because the borrower who has the 2-percent loan does not want to give it up and another lender is not going to come in and share that kind of an arrangement on a second-mortgage basis. This is not in the cards. I do not personally see how we can write this legislation, that is, the bill that we have under consideration.

I, personally, Mr. Chairman, do not see how we can incorporate such a facility in this bill.

Mr. BOLLINGER. This was merely a suggestion, you understand. It does not have anything to do with the bill itself. It is a suggestion on how we might improve the lot of some of these borrowers.

Mr. KLEPPE. I was just trying to draw this thing to a head, because I think we have kind of gotten off the line a little bit.

Mr. MYERS. I have one more question along the collateral end of it.

On page 8, you talk about lifetime equipment depreciation.

What is the lifetime of this equipment, the average of it, from your experience, the experience of the three of you?

Mr. FEGAN. I can give you an example, in my own company.

My father purchased the telephone company in 1910. In 1912, it was completely rebuilt. In 1929 it was completely rebuilt. In 1953, it was completely rebuilt.

Mr. MYERS. About 25 years?

Mr. FEGAN. Yes, sir.

Mr. MYERS. You are depreciating your Pioneer Co. at something around 3.75 percent per year. You do not depreciate it fast enough, do you?

Mr. BOLLINGER. We have increased it with the urging of the Commission. We have increased that just recently, with the urging of the Commission.

Mr. MYERS. Thank you.

The CHAIRMAN. Mr. Jones?

Mr. JONES of Missouri. My first experience with a telephone company loan was several years ago. I was rather amazed at the time, because the applicant for the loan was an individual. He owned the telephone company. He was expanding. And his difficulty was that he was seeking a loan—I forget the exact amount, but the REA people were proposing an increase in the amount of that loan. I had considerable trouble getting the REA to agree to lending him less money than they wanted to give him. Is that an unusual situation, or not?

Mr. BOLLINGER. I have been told of many instances just like that. We have never borrowed any money, in our own company, even though we have got 32 exchanges with fewer than 750 telephones, all of which would qualify for loans. We never borrowed any, so I have not had personal experience, but friends of mine have told me stories similar to this one you have just recounted.

Mr. JONES of Missouri. They finally made the loan for the amount that the man wanted, and since then he has made other loans.

What he was afraid of, or the thing that was disturbing him was that they were forcing this money on him faster than he could possibly use it; also, they were trying to encourage him to go into areas where he felt that there was not the possibility of earning a return on his money. We finally got that resolved, but it was with some difficulty that we got the REA to agree to this smaller loan. Since then he has made, I think, two or three other loans and has had a very satisfactory operation.

I just wondered if it was typical.

Mr. BOLLINGER. Typical in my State.

Mr. JONES of Missouri. That is all.

Thank you.

The CHAIRMAN. Mr. Wampler?

Mr. WAMPLER. Mr. Bollinger, I want to commend you on your statement this morning, and I also want to generally associate myself with the remarks of my colleague from Kansas, Mr. Dole.

I think that every member of this committee is genuinely concerned in seeing that rural America has modern and adequate telephone service.

I have been disturbed for some time about the alleged use of Government subsidies for the purpose of speculating in the telephone business. It certainly is my present intention to support the legislation before us, provided that we can add some amendments.

I want to commend you on the amendments that you have proposed to this committee for its consideration. I think that many of them are very fine. I think we should have legislation that would close these loopholes. If we make additional financing available, or make financing easier for the telephone cooperatives, there may have to be some limitations. This is really one of the problems of rural America today, as I see it, in having adequate telephone service.

Mr. BOLLINGER. Definitely so.

Mr. WAMPLER. Thank you. That is all.

The CHAIRMAN. Mr. Mayne?

Mr. MAYNE. Would you please identify the investment bulletin which you referred to? You did not tell us the name or issue of it.

Mr. BOLLINGER. It was issued by Piper, Jaffray & Hopwood, dated July 11, 1966.

Mr. MAYNE. Is that a regular investment bulletin that is sent out to all of their customers?

Mr. BOLLINGER. No. It is a confidential bulletin.

Mr. MAYNE. It is a confidential bulletin, and we would not then be able to verify it through any other source?

Mr. BOLLINGER. I can give you a copy of it.

Mr. MAYNE. I think that since you are quoting something, we should have access to it, or that we should have it. It should be a part of the record. I am a little suspicious of somebody who says, "And I quote," and then never reveals the source of the quotation. That would seem to me not to be very good practice.

Mr. BOLLINGER. I will be glad to introduce this as an exhibit, if you wish.

The CHAIRMAN. I would suggest that that be put in the files of the committee.

That will be done.

Mr. MAYNE. That will be satisfactory.

(The document referred to will be found in the files of the committee.)

The CHAIRMAN. Are there any further questions?

Mr. Miller?

Mr. MILLER. It seems to me that, in the statement made by Mr. Bollinger a few minutes ago, he had some information but was unable to clarify it 100 percent, and I can understand why. A company would not be able to pay off the REA in order to take a loan from private enterprise. It seems to me that companies working with a debt limitation to plant investment somewhere above the 50 percent, but less than 70 percent, could not afford to pay off a large REA loan that they are now paying 2 percent on. They could not pick up all of the money at the money-market price today, because of the profit that they are making. So the REA would be locking these people in and forcing them to go back to the REA for an additional loan. It appears that we are locking in some of these and should give

further consideration to Mr. Bollinger's problems, and, in some way, clear the air in that area.

But I also have a question, if I may, Mr. Chairman.

I have had information conveyed to me that many of the rural telephone companies still have eight-party lines and that many more applications are in today, dollar-volume-wise, than what is available under the 2-percent operation that the REA has today. I understand that this is the reason for wanting an additional telephone bank, because then there would be additional funds available. This information has been conveyed to me that many of the applications are asking for money to reduce the eight-party circuits down to single-party circuits. This would undoubtedly require additional lines and other control equipment. This seems to be the plan to reduce from eight- to one-party systems. We do not even have that in all of our municipalities today. Have you found that this is the intent, to reduce it all down now from eight- to one-party lines?

Mr. BOLLINGER. There is a good deal of activity in that direction in Minnesota, to go from eight- to one-party lines.

We are not considering it in our own company. We are offering one-party service to those who wish to pay the additional charge for it, but we are planning to upgrade from eight- to four-party lines. We presently have that program in effect.

Incidentally, we have started in North Dakota with that most marginal operation of ours.

When you go to the one-party line, you are obsoleting a very large percentage of your telephone property. And many of these properties that will be involved with this one-party service with REA loans have been built in the last 10 years. And most all of the outside plants of the rural telephone systems will be entirely obsoleted, because they will be replaced. This is what brings on that high debt ratio that I talked about and the danger of excessive debt money.

I would just like to give you an idea. This, again, refers to the State of North Dakota. Here, we operate in 10 towns, and in those towns 10.2 percent of the businessmen have two-party service. This is their own choice. They can have one-party service. The one-party rate is \$8.50, and the two-party rate is \$7.50. Of the residence subscribers, 42.8 percent choose one-party service; 1.92 percent, two-party service; 55.3 choose four-party service. One-party service is available to all of them at \$5, and four-party service at \$3.75.

It is our company's policy to respond to the wishes, the needs of the public. This is the way we hope to keep our company in tune with the times, to supply service on that basis.

Mr. MILLER. My intention was to try to find out if the reason for additional funds is to try to bring all lines and switch-gear equipment down to a single-party system.

Mr. BOLLINGER. It simply has to be a very large percentage of it, of the increased need, because, you see, quite generally throughout the United States conversion has been made to the dial service of an eight- or ten-party basis, so that this additional need of capital has got to be associated with the program you have described.

Mr. BARNHART. If I may add here: Quite a few State commissions do not encourage us to do this, to go to the one-party system, because it does not give the subscribers a choice of rates. If they want to pay a

lower rate, they cannot do so. A great many of the commissions oppose the single-party system.

Mr. MILLER. Thank you. That is all.

The CHAIRMAN. Mr. Price?

Mr. PRICE. I would like to ask Mr. Bollinger one question:

On page 11 of your testimony, in the last paragraph, you say:

In addition to presenting these recommendations for your consideration, we sincerely hope that your Committee will devote further study to the advisability of an "insured loan program" as a possible acceptable alternative to the establishment of a rural telephone bank.

Do you think that the insured loan approach in the bill that we have before us is the best for the country, in the financial condition we are in today?

Which program would actually solve the problem that is before us in financing the telephone business in your opinion, which approach do you think would be better?

Mr. BOLLINGER. To answer your question broadly either would help the situation or the problem. It is certain that the bank would do so. If the amendments are not acceptable, then we would suggest that the insured-loan program be considered. We sincerely hope that the amendments we have offered are acceptable and that the bill would be adopted. We think that this bill would do the job if it is very carefully administered.

Mr. PRICE. Do you think that the insured loan program, if it were adopted, would give you the money needed?

Mr. BOLLINGER. It would not give all of the money that has been applied for. Certainly, the program would be delayed. We will get to those things someday. Our company intends to wait for developments of the art to get to the one-party rural telephone service. We definitely plan on providing all one-party rural service in our company someday. So, we will delay that investment. We know it will be less if we wait for the development that we know is coming. So, I think that the insured-loan program would do a reasonably good job. My own feeling is that it would not be quite as good as the bank.

Mr. PRICE. Thank you.

That is all.

Mr. BARNHART. Could I say a word here?

The CHAIRMAN. All right, go ahead.

Mr. BARNHART. I have in mind a case in North Carolina, about an order issued by the North Carolina Utilities Commission on a matter of a loan, which tells, in a few words, what sometimes happens. This is relative to the application of the Eastern Rowan Telephone Co., Inc., for the establishment of reasonable and just rates, and the commission found and issued this order—this is just a brief summary that I made of it, which I would like to read:

1. The company had an outstanding balance owed to REA at 2 percent interest of \$624,000 and had pending an application for an additional loan of \$467,000. Its equity capital consisted of \$92,408, or an 11 percent equity ratio. At the same time, the company held as corporate assets investments in the common capital stock of various corporations with no relationship to its telephone operations at original cost of \$89,792. While the company was enjoying 2 percent loans from REA, an amount almost equivalent to its total equity investment had been withdrawn from company operations and invested in outside activities.

2. Even though an amount almost equal to the equity capital had been withdrawn and diverted to nontelephone investments, the equity capital of the corporation enjoyed earnings during the test year (1961) of more than 20 percent.

I would like to make reference to the fact that the General Accounting Office has made investigations of REA borrowings, and the committee might wish to seek out information from it concerning some of the cases available that will give you examples of loans that have been made.

The CHAIRMAN. Mr. Teague?

Mr. TEAGUE of California. Mr. Bollinger, I thank you for having given us a very constructive statement and suggestions. I think they deserve the full consideration of this committee. I do not have any questions.

Personally, I have a closed mind on this subject. I am not convinced that there is any need at all for a telephone bank. It seems to me that the money can be obtained through the bank for cooperatives or through commercial sources.

Nevertheless, I do thank you for your contribution today.

The CHAIRMAN. Are there any further questions?

Mr. Zwach?

Mr. ZWACH. Just one brief question.

I will say, Mr. Bollinger, that I am happy to have a Minnesotan here displaying some good astute management. You said a number of times that you believed in small independent operations, and that Minnesota has a lot of them. I see in your testimony that you say and you have a good reputation in our State, but you say that you will shortly become a subsidiary of United Utilities, Inc. This is the opposite of a small independent operation. Is this for personal reasons or for business reasons? Would you mind answering that question?

Mr. BOLLINGER. I will answer that. Our company has two quite large substantial stockholders. They have become elderly and have wanted to get their estates in shape for retirement. In our case, it was for personal reasons.

Mr. ZWACH. For personal reasons?

Mr. BOLLINGER. Yes, sir.

Mr. ZWACH. Thank you. That is all.

The CHAIRMAN. If there are no further questions, we are very much obliged to you, Mr. Bollinger and your associates. We appreciate your attendance here today.

The document which you referred to concerning the North Carolina case will be made a part of the record at this point.

(The document referred to follows:)

STATE OF NORTH CAROLINA, UTILITIES COMMISSION, RALEIGH

Docket No. P-62, Sub 13

Before the N.C. Utilities Commission In the Matter of Application of Eastern Rowan Telephone Company, Inc., for the establishment of reasonable and just rates.

ORDER DENYING INCREASE AND DISMISSING ACTION

Heard in: Raleigh, North Carolina, on June 14, 1962.

Before: Chairman Harry T. Westcott, and Commissioners Sam O. Worthington, Clarence H. Noah, Thomas R. Eller, Jr. and R. Brookes Peters.

APPEARANCES

For the Applicant: Nelson Woodson, Woodson & Woodson, Attorneys at Law, P.O. Box 144, Salisbury, North Carolina.

James L. Woodson, Woodson & Woodson, Attorneys at Law, P.O. Box 144, Salisbury, North Carolina.

For the Commission's Staff: Charles W. Barbee, Jr., Assistant Attorney General, N.C. Utilities Commission, Raleigh, North Carolina.

Worthington, Commissioner: By application filed with the North Carolina Utilities Commission (Commission) on March 26, 1962, Eastern Rowan Telephone Company, Inc. (Company), seeks to increase its present rates and charges in accordance with schedule attached to the application sufficient to produce approximately \$13,538.40 additional gross revenue annually. The application was scheduled for hearing, and the Company was required to publish notice in the local newspaper setting forth the place and time for hearing and showing the comparison of the existing rates with those proposed as such increase relates to each type of service. No formal protest was filed with the Commission. Correspondence was had with certain individuals and organizations expressing dissatisfaction at the proposed increase in rates. The Mayor of the Town of Rockwell, accompanied by two other citizens, appeared at the hearing held in the Hearing Room of the Commission, Library Building, Raleigh, North Carolina, on June 14, 1962, and was permitted to participate and offer what objection they had. The Company was present through its officers and counsel.

Testimony through witnesses for the applicant indicates that the Company acquired the properties of the Rowan Telephone Company in 1949 which was then serving about 400 subscribers. In October, 1952, it installed a new dial exchange on U.S. Highway 52 between Granite Quarry and Rockwell in the eastern part of Rowan County with service to 1,000 subscribers. In order to finance construction of this plant it borrowed \$343,000 from Rural Electrification Administration. The demand for telephone service increased to the extent that 1,408 subscribers were being served by December 31, 1953. It was necessary to expand facilities, and in order to do so additional funds were borrowed from Rural Electrification Administration exceeding in total amount more than \$800,000, of which it now owes approximately \$624,000.

The Company now serves the municipalities of Faith, Granite Quarry, Rockwell and Gold Hill, together with the surrounding territory to the extent of about 38 square miles, serving approximately 2,000 subscribers. It now has pending an application to Rural Electrification Administration for an additional loan of \$467,000 with which to further expand and improve its facilities. Extended area service is available to Salisbury, an exchange in the Southern Bell territory, with approximately 17,000 subscribers. The average gross cost per main station of the Company is \$367. The Company has no held orders nor any pending requests for upgrade in service.

Gross operating revenues as per Company books for the calendar year 1961, test period used by the Commission's Accounting Staff for its report, were \$138,261.84, adjusted to a total of \$138,843.84. The proposed increase in rates is calculated to produce additional gross revenue of \$13,538.40. Net operating revenue for return for the calendar year of 1961 was \$23,478.58. Dividend income from total investment in common stock of other companies in amount of \$89,792, was \$3,535. Other income (interest of \$986) produced a total of \$28,000 in income available for fixed charges. Average fixed charges were \$12,368. Actual fixed charges paid were \$11,856. Dividends totalling \$3,000 were paid during the period. After payment of fixed charges and dividends \$13,144 was available for surplus. Earnings on average common equity were 20.99 percent. Under exactly the same operating experience the proposed increase in rates would have resulted in common equity earnings of 29 percent and \$19,312 available for surplus.

Testimony of witnesses for the Company indicates additional operating expense in the amount of \$1,200 for loss in mileage charge due to the elimination from its tariff of mileage charge on multi-party service; \$2,500 expense for pension plan being inaugurated for five full-time employees and two-part time employees of the Company; and \$1,000 to provide wage increase for employees for total additional expense not included in the 1961 operating experience of \$4,700. If this additional expense had been incurred in 1961, present rates and charges would still have produced \$10,051 for surplus and common equity earnings of 16.97 percent on average common equity of \$76,928. The \$3,000 in dividends equates to a 5 percent dividend on par value of the 600 shares of common stock of the Company of the par value of \$100. If the dividends had been 10 percent instead of 5 there would still have been available for surplus \$7,051 with the additional expense and \$10,144 under 1961 actual operations. These determinations are a result of an investigation and report by the Accounting Staff of the Commission. Officers of the Company, as witnesses, agreed to the correctness of these figures and that they represent Company operations.

The management of the Company has invested \$89,792 of Company funds in stocks of other companies. Par value of the common stock of the Company is \$60,000. Actual earned surplus of the Company as of December 31, 1961, was \$32,408.09. Thus, the investment in stocks of other companies approximates the par value of the common stock, plus earned surplus. The Company proposes to use funds available from approved Rural Electrification Administration loan of \$467,000 in the next five years to eliminate any lower grade service than that of four-party. It anticipates considerable additional investment in plant in order to afford its customers a higher grade of service.

The proposed increase in rates would increase one-party residence from \$5.10 to \$6.50, two-party residence from \$4.25 to \$5.10, four-party residence from \$3.60 to \$3.80 monthly and multi-party residence from \$3.60 to \$3.80 with mileage charge eliminated. One-party business would be increased from \$9.80 to \$11.80, two-party business from \$7.80 to \$9.80, four-party business from \$6.60 to \$8.60 and multi-party from \$5.50 to \$7.50 monthly. Average telephone plant in service during the test period, including material and supplies, plus cash working capital, as shown by the Staff's report, was \$572,662.54. As of the end of the period the gross plant in service was \$832,159. End of the period net plant, plus material and supplies of \$5,342, was \$591,490. The debt ratio of the Company is approximately 89 per cent while equity is about 11 per cent.

The protestants offered the Mayor of Rockwell and one other subscriber as witnesses. The Mayor presented a petition signed by a number of people in which they suggest that telephone rates are high enough. They offered no expert witness nor did they particularly complain about any service being rendered. They just think that their present rates are as high as they ought to be.

The report of the Staff on the operations of the Company for the calendar year of 1961 was offered evidence in and for all practical purposes accepted as an accurate statement of Company operations during the period.

FINDINGS OF FACT

Considering all of the testimony and all of the exhibits offered by all parties to this matter in the light most favorable to the Company justifies the following finding of fact:

The Company has not justified its suggested increase in its rates and charges, has not shown such proposed rates and charges to be just and reasonable, and its application should, therefore, be denied.

CONCLUSIONS

In 1957 or early 1958 the Commission determined and fixed just and reasonable rates and charges for this Company to apply in the operation of its telephone system. It is apparent now that under those rates and charges the Company did not realize substantial net earnings in 1958 or 1959. However, it is apparent that in 1960 appreciable net earnings were realized. These net earnings increased for the year 1961. Evidence offered by the Company indicates no reason as to why net earnings should not continue to be available and even increase under present rates and charges. While the evidence indicates that the Company is eliminating mileage charges on multi-party service and desires to provide a pension plan for employees and finds it necessary to increase employees' wages, all in a total amount of some \$4,700 annually, it does not appear that this amount of additional operating expense will seriously impair the net earnings of the Company.

When a public utility seeks to have its rates and charges increased it is faced with the burden of showing that its present rates and charges are unjust and unreasonable and that an increase in rates and charges is justified to provide just and reasonable rates for the service being rendered. Usually rate increases are requested by a utility when there is no available net earnings or net earnings are dangerously decreasing. In this instance the situation is unusual in that the request for an increase comes at the time the Company is enjoying its first net earning experience.

In the determination of just and reasonable rates it is necessary to provide rates that will give the Company a fair rate of return on the fair value of its property used and useful in rendering service. As the fair value of the property is a judgment figure so is the denominated fair rate of return a judgment determination. A rate of return of 6 per cent may be found necessary to provide just and reasonable rates in one instance while it may be necessary to use a lower or higher rate of return to provide just and reasonable rates in other instances.

This Company has \$60,000 in common stock and approximately \$32,000 in earned surplus. The rest of its investment and capital is borrowed at 2 per cent. Its fixed charges are, therefore, reasonably low. The amount of common equity is comparatively small. The debt ratio is 89 percent while common equity is only 11 per cent. Its earnings on average common equity for the calendar year 1961 were more than 20 percent. If the proposed increase in rates had been in effect during the period, earnings on average common equity would have been approximately 30 per cent. Had the additional \$4,700 in operating expense as suggested by the Company occurred in 1961 earnings on average common equity would still have been more than 16 per cent. The Company could have paid its interest requirements, a 10 percent dividend on its common stock and added to surplus \$7,051. By every test the present rates and charges of the Company are just and reasonable and provide for the Company adequate revenue and a fair rate of return on its investment.

The Company has invested approximately \$90,000 of Company funds in the common stock of other companies. This amount approximates the \$60,000 par value of the Company's common stock and its earned surplus of \$32,000. It is unusual for a public utility to invest company funds in the common stock of other companies. Rather, the practice is to invest these funds in plant instead of borrowing money. The Commission does not look with favor upon this method of investment. However, the investment having been made and dividends having been received they are being added to net income and treated as income of the Company for rate-making purposes just as operating income.

In 1961 the Company as such incurred no Federal income tax liability for that the four stockholders elected to include in their gross income the amount each would have received as a dividend if the Company had distributed pro rata to its stockholders an amount of money equal to its undistributed taxable income for the year. While this method meets the requirements of Section 1372(A) of the Internal Revenue Code the Commission does not look with favor on this practice. It understands that the Company has already made arrangements to discontinue this practice and will in the future file income tax returns for the Company in the regular manner.

The Company having failed to establish the justness and reasonableness of the proposed rates the application will be denied and the action dismissed.

ORDER

It is, therefore, ordered that the application of Eastern Rowan Telephone Company, Inc., to increase its rates and charges for telephone service be, and the same is hereby, denied and this action be, and the same is hereby, dismissed.

Issued by order of the Commission.

This the 3rd day of July, 1962.

[SEAL] NORTH CAROLINA UTILITIES COMMISSION,
By KATHERINE M. PEELE,

Assistant Chief Clerk.

The CHAIRMAN. I have a letter addressed to me as chairman of this committee, dated August 17, 1967, from the Morrison Telephone Co., signed by Mr. L. N. Ewers, general manager, and he requests that it be made a part of the record.

Without objection, it will be made a part of the record at this point.
(The letter dated August 17, 1967, follows:)

MORRISON TELEPHONE Co.,
Morrison, Ill., August 17, 1967.

Congressman W. R. POAGE,
Chairman, Committee on Agriculture,
House Office Building,
Washington, D.C.

DEAR CONGRESSMAN POAGE: Thank you for acknowledging my telegram of August 5 expressing my opposition to the telephone section of the REA Bank Bill.

I understand hearings have been scheduled for August 23 and 24 relative to the above Bill. My specific objections to this legislation are:

1. I do not believe that the broadening of federal financing of rural telephone companies is necessary. The rural telephone situation has progressed

from the period which federal funds were needed to provide and extend service, and I believe that any necessary extension of service can be adequately taken care of through the existing REA program.

2. I believe that any broadening of federal financing of rural telephone companies would only promote programs beyond the intent of the original legislation.

3. That with the creation of a rural telephone bank, the discrimination against conventionally financed companies could continue and that the cost of capital to REA borrowers would continue to be less than the cost of capital to a privately financed company.

4. I believe the REA program, if continued, should be retained as it is presently constituted, however, the act should be amended to permit the granting of loans at rates comparable to the cost of money to the government.

5. Also that an alternate proposal should be considered to provide for federally insuring conventional loans in place of REA loans.

Again thank you for taking the time to answer my telegram and offering me the opportunity to express my objections to this legislation.

Sincerely yours,

L. N. EWERS, *General Manager.*

THE CHAIRMAN. If there are no further questions, we have completed the list of witnesses for today. The Chair will excuse our visitors. We will take up some things in executive session, about our work for next week.

Thank you, gentlemen.

We will meet at 10 o'clock tomorrow morning.

(Whereupon, at 11:30 a.m., a recess was taken until 10 a.m., Thursday, August 24, 1967.)

RURAL TELEPHONE SUPPLEMENTAL FINANCING

THURSDAY, AUGUST 24, 1967

HOUSE OF REPRESENTATIVES,
COMMITTEE ON AGRICULTURE,
Washington, D.C.

The committee met, pursuant to recess, at 10 a.m., in room 1301, Longworth House Office Building, Washington, D.C., Hon. W. R. Poage (chairman) presiding.

Present: Representatives Poage, Gathings, McMillan, Abernethy, Jones of Missouri, O'Neal, Foley, de la Garza, Vigorito, Jones of North Carolina, Dow, Nichols, Belcher, Teague of California, Dole, Hansen, Wampler, Miller, Burke, Mathias, Mayne, Zwach, Kleppe, Price, and Myers.

Also present: Christine S. Gallagher, clerk; Hyde H. Murray, assistant counsel; and Francis LeMay, consultant.

The CHAIRMAN. The committee will please come to order.

I understand that Mr. Charles F. Avila, president of the Edison Electric Institute, desires to file a statement. Without objection, it will be made a part of the record at this point.

(The prepared statement of Charles F. Avila follows:)

STATEMENT OF CHARLES F. AVILA, PRESIDENT, EDISON ELECTRIC INSTITUTE

The Committee having specifically reserved time for electric utility companies, Edison Electric Institute is submitting this statement for the record concerning H.R. 12066, a bill to establish a Federal Telephone Bank. The Institute recognizes that this legislation relates only to the REA telephone program—a program in which we have relatively little direct interest, and we are not purporting to speak for the telephone industry. The views contained in this statement are offered primarily because we believe that the establishment of a telephone bank or any other bank by legislation containing some of the provisions in this bill might at some future date be used as a pattern for establishing an electric bank.

Witnesses for the Edison Electric Institute testified in March, 1967, before this Committee that an insured loan program would be a superior solution for future financing of the REA electric program. Details of the insured loan solution are contained in bi-partisan legislation introduced by six members of Congress, including three distinguished members of this Committee—Representatives McMillan, Teague, and Goodling. We suggest now that an insured loan program for REA telephone borrowers would also be more efficient and much less costly for the nation's taxpayers than the bank approach set forth in H.R. 12066.

Although Edison Electric Institute does not believe that a bank is the best way to provide supplementary financing for the telephone program, if, however, the establishment of any bank to make loans for telephone operations is to be considered by the Committee, we submit several improvements should be made. For example, such a bank should reimburse the Federal Government for the services of all U.S. Department of Agriculture personnel, regardless of whether they are full-time or part-time employees of the bank. The return to the Government on Class A stock should be no less than the cost of money to the U.S. Treasury, rather than only 2%. The Government's investment should be repaid

on a regular repayment schedule and completely retired within a reasonable period. Social Security and other Federal trust funds should not be used to purchase bank debentures. The operations of the bank should be subject to adequate Congressional supervision and control. The maximum loan period should not exceed the depreciable life of the equipment or thirty-five years, whichever occurs first. The bank should not be turned over to borrower control until *all* Government capital has been retired. The 2% program should be revised to increase the rate of interest to correspond to the ability of each borrower to pay.

These points correspond to six of the nine points made in the "Additional Opposing Views" by four members of this Committee at pages 26 and 27 of House Report No. 459 on H.R. 10190. They would seem to be applicable to H.R. 12066 as well as to H.R. 10190.

In addition to the above points, the loan authority of the bank should be identical to that under the 2% program. The language concerning use of bank funds for expansion and acquisition purposes should be deleted. Bank loans should be made at a single rate of interest reflecting bank costs, including costs of administration and a reserve for losses. The subsidized intermediate loan program should be eliminated.

The last two points are made because this bill differs from the electric provisions in H.R. 10190. The Committee deleted use of electric bank funds for acquisitions, and the intermediate loan program. In our opinion, similar provisions should be made to any telephone program.

In summary, the Edison Electric Institute recommends the bill (H.R. 12066) not be approved by the Committee for three basic reasons: (1) it would serve as an unfortunate precedent for an electric bank in the future; (2) it could be used as a vehicle for adding the electric bank provisions at some point in the legislative process; and (3) other more reasonable alternative methods of providing financing for the REA telephone program have not been explored.

If the Committee, however, desires to consider the bank approach further, it is recommended that improvements along the lines of the suggestions made in this statement be incorporated in order to assure that the bank would operate on a self-sustaining basis, under appropriate Congressional controls, and for proper purposes.

The CHAIRMAN. We will also make a part of the record at this point a statement by the Honorable Alvin E. O'Konski, together with a statement from the American Farm Bureau Federation.

(The statements follow:)

STATEMENT OF HON. ALVIN E. O'KONSKI, A REPRESENTATIVE IN CONGRESS
FROM THE STATE OF WISCONSIN

Mr. Chairman. I appreciate the opportunity to present testimony in support of H.R. 12066, the legislation to provide for additional sources of financing for the rural telephone systems.

If we are to reverse the trend of outmigration from our farms to crowded cities with their slums and ghettos, we must provide for a dynamic Rural America. The rural telephone program, initiated in 1949, is *essential* to the development and revitalization of Rural America—to make it an attractive and prosperous place for new industries and business and the families which go with them. It is just not reasonable to expect that industry and people in this modern day and age will either settle or stay in communities where they cannot enjoy quality telephone service. And when farms prosper, all America prospers.

I am proud that my home state of Wisconsin has been one of the pioneers in the rural telephone program, with the first REA telephone loan in the State going to a 10th District borrower, the Cream Alley Telephone Company at Hawkins, Wisconsin, in October, 1950. Statewide there are now more than 123,000 farm families who have modern telephone service over 24,000 miles of line. The success of the program is clearly shown in the 10th District where REA has approved loans to twenty telephone systems to enable these borrowers to provide new or improved service to nearly 54,000 subscribers over almost 11,000 miles of line.

The average rural subscriber on an REA financed system is making three times as many calls as he did when he first obtained dial service. Likewise, the demand for single-party service continues to increase. There still remains the unfinished job of reaching the estimated 20 per cent of the rural establishments

which do not have telephone service and to modernize those which are using outmoded, inadequate and multi-party telephone lines.

It is imperative that we update the phone system for Rural America. It is estimated that REA telephone borrowers who received loans of \$1.3 billion since the beginning of the telephone program will need more than twice this amount in the next fifteen years to meet the demands of modern communications service in their areas. In Wisconsin there is a backlog of about \$20 million in loan applications. The average subscriber density for all REA telephone borrowers is 3.7 per mile, compared with 16 telephone subscribers per mile for the independent industry generally and an estimated 40 subscribers per mile for Bell System companies. Annual revenues average about \$400 per mile for REA borrowers, compared with \$2,538 per mile for the independent industry. H.R. 12066 will give the flexible financing needed through the Rural Telephone Bank for funds from the private money market.

As one of the early sponsors of legislation to provide supplemental financing for both the rural electric cooperative systems and the rural telephone systems, I respectively urge this Committee to take favorable action on H.R. 12066. By enacting this legislation, we can assure continued progress for Rural America in meeting its quality telephone needs for now and the future.

STATEMENT OF JOHN C. LYNN, LEGISLATIVE DIRECTOR, THE AMERICAN
FARM BUREAU FEDERATION

We appreciate the opportunity to again present the views of the American Farm Bureau Federation with regard to supplemental financing for the rural telephone program. On April 4 of this year we presented in detail our recommendations with regard to the provisions of H.R. 1400, dealing with the "telephone bank."

Farm Bureau has a long record in support of rural electric and telephone programs. As early as 1944 our delegate body recommended that rural electric cooperatives move toward less dependence on the federal government for financing. We worked for the enactment of the rural telephone legislation in 1949. This program has meant a great deal to rural America.

We are disappointed that certain segments of the rural electric cooperatives and the electric industry succeeded in persuading the Rules Committee to table H.R. 10190, which provided supplemental financing for rural electrical and telephone cooperatives through the establishment of an electric bank and a telephone bank. We would prefer to see supplemental financing provided for both these programs in the same legislation.

Recognizing that many farmers and ranchers throughout America are dependent on the rural telephone program, we support the enactment of H.R. 12066 providing for supplemental financing for the rural telephone program.

We hope that in considering this separate legislation for the telephone program, the Committee will continue to keep firmly in mind the needs of the rural electric cooperatives for supplemental financing and that some sound method will be developed to meet the pressing needs of the rural electric cooperatives.

We shall continue to work toward this objective.

The CHAIRMAN. Is there anyone else who cares to submit anything in behalf of the electric cooperatives?

There is no one. We will now pass then to the telephone part. On the list of witnesses I have before me, Mr. David C. Fullarton, executive manager of the National Telephone Cooperative Association is the first on the list. He is accompanied by B. Maynard Christenson, who is president of the Dakota Cooperative Telephone Co. of Volin, S. Dak., and Robert E. Jamison, who is with the Horry Telephone Cooperative of Conway, S.C.

We will be glad to hear from you gentlemen now.

STATEMENT OF DAVID C. FULLARTON, EXECUTIVE MANAGER, NATIONAL TELEPHONE COOPERATIVE ASSOCIATION, WASHINGTON, D.C.; ACCOMPANIED BY B. MAYNARD CHRISTENSON AND ROBERT E. JAMISON

Mr. FULLARTON. Thank you, Mr. Chairman and gentlemen. My name is David C. Fullarton. I am executive manager of the National Telephone Cooperative Association. With me today are Mr. B. Maynard Christenson of Volin, S. Dak., president of the association, and Mr. Robert E. Jamison of Conway, S.C., vice president of the association.

We have no prepared statement to present, having appeared before this committee several times previously this year to support supplemental financing for REA telephone borrowers. We supported them and we fully support H.R. 12066 now. We noted with extreme interest the testimony of yesterday's witnesses and were pleased that they supported telephone supplemental financing, and a telephone bank to provide additional financial needs.

However, as you are probably aware, many of those represented here yesterday are not directly involved in the REA telephone program. I am grateful for their support, but I fear they misunderstand the ramifications of some of the amendments to H.R. 12066 that they propose. For this reason, and in collaboration with the National REA Telephone Association, the organization representing the commercial REA borrowers and ably represented here today by Mr. A. Harold Peterson, the National Telephone Cooperative Association has prepared an analysis of these proposed amendments and their effect on the objectives of the telephone program. And I would request that this jointly prepared analysis be made a part of the record at this point.

The CHAIRMAN. Without objection, it will be made a part of the record.

(The document entitled "Analysis of Amendments," follows:)

ANALYSIS OF AMENDMENTS OFFERED BY H. R. BOLLINGER TO H.R. 12066 (THE TELEPHONE SUPPLEMENTAL BILL), PREPARED BY NATIONAL REA TELEPHONE ASSOCIATION AND NATIONAL TELEPHONE COOPERATIVE ASSOCIATION

In testimony presented before the House Agriculture Committee on August 23, 1967, Mr. H. R. Bollinger offered seventeen amendments to H.R. 12066. The following analysis is presented in the order that the proposed amendments were offered by Mr. Bollinger in his prepared statement.

1. Requires that the wording of the preamble reflect that "some" rather than "many" systems require 2% financing.

Comment: Although this amendment is not substantive the word "many" appears to be a more accurate description of the situation according to all currently available studies.

2. Deletes provision for carry-over of unobligated telephone loan funds.

Comment: This serves no useful purpose since the estimated carry-over of funds is taken into account in establishing the loan fund level for the succeeding fiscal year. This amendment might encourage acceleration of loan approvals before the end of each fiscal year to avoid lapse of authority. This is not sound administrative practice.

This amendment also prohibits 2% loans to applicants who "can qualify under the policies, terms, and conditions established" for bank loans by the bank board of directors.

Comment: It is contemplated that 2% loans would not be made to applicants where the REA feasibility study indicates that a higher "bank" rate could be

absorbed while still meeting program objectives. This determination should be made first, rather than in compliance with telephone bank loan policy, terms and conditions. Further, this amendment conflicts with the requirements of section 408(b)(2) that loans to applicants meeting the subscriber density criteria of 3 or fewer per mile, be made at 2% unless the applicant elects a bank loan.

3. Requires the bank to be charged and recover from borrowers the costs of REA facilities or services of employees partially or jointly used by the telephone bank.

Comment: The Bill now provides for such utilization without charge to or recovery by the bank until conversion of the bank to borrower ownership and control. This is intended to soften the impact of administrative expense during the transitional period and would enhance the ability of rural telephone systems to utilize bank financing, and enable more systems to move more quickly to bank financing.

4. Authorizes Presidential appointment of Federal members of the bank board from the Federal Government generally instead of restriction appointment to Department of Agriculture employees.

Comment: Section 403 (a) provides that the bank shall be an agency of the United States, subject to the supervision and direction of the Secretary of Agriculture. It is only logical therefore that the Federal board members come from the Department of Agriculture. The expertise of the Treasury Department is available, and in fact mandatory, under the provisions of section 403(c) of the Bill.

5. Requires that two instead of three bank directors be named from cooperative-type entities, and four rather than three from commercial-type entities.

Comment: The Bill provides for equal board representation for the two classifications of borrowers, thus assuring that neither will dominate or control. The effect of this provision is that all borrowers must work together toward achievement of program objectives, and it assures that the people of rural America will continue to be the beneficiaries of the program.

6. Requires retirement of Class A stock to commence as soon as practicable after June 30, 1977 rather than 1982, and deletes the provision that such retirement commence after the total of Class A and B stock reaches \$400 million.

Comment: The existing provision in the Bill contemplates the accumulation of \$100 million in Class B stock subscriptions and their retention as part of the equity capital structure of the bank. The amendment would in effect require full and virtually immediate use of the proceeds of Class B stock and to this extent diminishes the bank's equity capital. This will adversely affect the bank's credit and its ability to market its debentures. Advancing the date for retirement of Class A stock will have the same effect.

7. Substitutes a return on Class A stock based on the average market yield on marketable obligations of the United States issued during the month of May in the preceding fiscal year for the present 2% return on Class A stock.

Comment: The effect of this amendment would be to approximately double the cost to the bank of the Class A equity funds invested by the Government. It would substantially reduce the volume of intermediate loans and limit them to not more than the amount of the annual Class A stock subscription of \$30 million. The 2% rate of return permits a blending of Class A funds with funds realized from the sale of debentures and thereby enables a larger volume of intermediate loans. Reducing the bank's capability to make intermediate loans limits the number of borrowers and dollar volume of loans which could be handled by the bank and would tend to hamper the orderly transition from the basic 2% financing to the intermediate step of the credit ladder provided in the Bill.

8. Deletes the provision making the bank's debentures lawful investments of certain funds under the authority and control of the United States.

Comment: This would appear to be an unnecessary restraint upon the salability of bank debentures and would deprive the bank of part of the market for its debentures. Initially, this market could be very important for the telephone bank.

9. Requires approval of the Telephone Bank Board as well as the Secretary for acquisitions financed by the bank.

Comment: Section 408 (a) of the Bill already provides that in the case of acquisition loans the Governor of the telephone bank is authorized to make loans in accord with policies approved by the bank board of directors and subject to the approval of the Secretary.

10. Reduces maximum loan period from 50 to 35 years.

Comment: This would have the effect of substantially increasing debt service requirements, that is the amount of principal and interest payable periodically during the life of the loan with a resultant drastic increase in subscriber rates. Equipment replacement costs are normally met out of depreciation reserves. The maximum 50 year term is considered by REA to be economically sound. Reducing the term would retard the transition from basic REA 2% financing to bank financing.

11. Requires basic 2% financing for systems with average subscriber density of three or fewer per square mile, instead of three or fewer per mile.

Comment: It is the practice of the telephone industry to define density in terms of subscribers per route mile of line. Defining it otherwise divorces it from the cost of providing service and makes it unusable for setting criteria.

12. Removes the 4% ceiling on the intermediate loan program and requires such loans to carry a rate based on the average market yield during May in the preceding fiscal year on outstanding marketable obligations of the United States with comparable maturities.

Comment: *Treasury Bulletin* for July 1967, reports (Table 1, p. 69) an average market yield of 4.76% on long-term Treasury bonds, in May 1967. With the 4% ceiling removed, this would presumably be the interest rate on intermediate loans made during fiscal year 1968. Since the rate could fluctuate annually this would introduce an element of uncertainty for those bank borrowers who most need certainty in their capital costs at least until they develop the financial strength to utilize market rate loans. An increase in the intermediate loan rate would restrict the number of borrowers who could progress to bank financing from the basis 2% financing.

13. Terminates authority to make intermediate loans on June 30, 1967 rather than 1982.

Comment: The 15 year period for intermediate loan financing provided in the Bill is reasonable and prudent. Eliminating the intermediate loan step of the credit ladder after 10 years could retard transition of some borrowers from basic REA 2% financing to bank financing.

14. Clarifying change in requirement of report by Secretary of Agriculture on intermediate loan program.

Comment: None; Does not change substance.

15. Requires approval of Secretary of Agriculture and the Telephone Bank Board, in place of the Administrator, for sale of borrower's property, rights, or controlling interest.

Comment: None.

16. Requires approval of all such sales (see 15 above) rather than only those to a holding company.

Comment: None.

17. Limits adjustment of payment schedules so as not to extend beyond 35 years, instead of 50 years.

Comment: See comment on 10 above.

H.R. 12066 is identical to the telephone provisions of H.R. 10190 which after extensive hearings and consideration was approved and voted out by this Committee on May 24, 1967. The National REA Telephone Association and the National Telephone Cooperative Association believe that H.R. 12066 in its present form is an appropriate and suitable means of providing supplemental financing to the nations rural telephone systems. We therefore respectfully urge early passage of H.R. 12066 in its present form. All witnesses who have appeared before this Committee in reference to telephone supplemental financing, have recognized the need for it, the desirability of continuing the 2% program, and have supported the concept of a telephone bank.

Mr. FULLARTON. I would reiterate that this is a joint analysis by Mr. Peterson's group which represents both the commercial REA borrowers and our own association which represents the cooperative borrowers.

I will be very brief. First, I would like to comment on some of the amendments proposed by yesterday's witnesses.

There are two of them.

The first is representation of telephone borrowers on the Telephone Bank Board of Directors. I believe the witnesses yesterday were in-

interested in some type of arithmetic ratio. We believe that H.R. 12066, which provides for equal representation of the two classifications of borrowers, is the proper approach. Equal representation will reduce conflict, assure cooperation, and go a long way toward assuring the objectives of this legislation are met and that the people of rural America will benefit, not some segment of the industry. We respectfully urge the committee to provide for borrower representation on the Telephone Bank Board as it is already specified in H.R. 12066.

I would also direct your attention for a moment to the proposal of yesterday's witnesses on "holding companies" and "acquisitions." I would be the last person to recommend that speculation be allowed in a program with which the Federal Government is connected. I am concerned, however, lest the committee restrict acquisitions by other than holding companies, for it is often only by acquisition or merger that service can be extended to the unserved areas of the country. This is important in extending area coverage to all of rural America. I believe that the restrictions on acquisition already in H.R. 12066 are sufficient to protect the Government's interest and allow REA telephone program objectives to be met.

Finally, there were three points raised in the questioning of yesterday's witnesses that I believe need clarification.

The first, Mr. Barnhardt referred to a company in North Carolina with some \$87,000 in high-return investments and a considerable amount of REA 2-percent money. He stated, I believe, that this was brought up as an example of the uses made of REA loan funds. I would only point out to the committee that REA loan funds cannot be used for investments of that nature. Telephone loans can only be used for telephones, cable, central office equipment, and the like that are actually installed to bring telephone service to our rural people.

Second, Mr. Bollinger made the statement that some companies find themselves required to borrow more money than they need and to install more facilities than necessary to meet the service requirements. I think that this leaves a misleading impression and I would just briefly state the situation to you. When a borrower files an application he files it in terms of what he believes to be good business practice and in terms of his own objectives, and the objectives of the program. However, the REA technical staff and the loan review people must abide, of course, by the provisions of the 1949 amendment to the act, and these provisions include the very important one, among various other faults, that in some cases REA is required, under the charges of that 1949 amendment, perhaps, to broaden the scope of the loan application, so that the area coverage concept is carried out. I believe that that is an important enough point that it should be elaborated on here.

The other statement that Mr. Bollinger made, I believe, was that the REA borrowers were required, as conditions of receiving an REA loan, to provide facilities for higher grade service than the standards established by the regulatory authorities or that the telephone subscribers actually wanted.

At the outset of the program REA, as a matter of policy, confined its financing virtually to the matter of completing modern dial service. This was to insure against technological obsolescence and to give

the rural subscribers service as closely as feasible to that received by the urban population. And eight-party service was the standard, and with the advent of newer techniques and materials, increasing urban demands for upgraded service, there has been developed a standard whereby there are fewer parties on the line, and today four-party service is in vogue, and upgrading beyond this is occurring when there is a subscriber demand. The REA encourages upgrading and to bring more telephone service to the rural areas.

Experience demonstrates that the practice has been sound and generally accepted by the borrowers who have, on the whole, dedicated themselves to meet the subscribers' demands for the best grade of service technically and economically available.

Mr. Chairman, we appreciate again the opportunity to appear before this committee. We are fully in support of H.R. 12066 and we will be happy to answer any questions or to make any further comments that the committee desires.

The CHAIRMAN. Are there any questions? Mr. Jones.

Mr. JONES of Missouri. I am sorry that I got here late and did not hear all of your testimony. You made a statement about a question I raised yesterday, about the REA telephone people insisting that some of the applications be raised as to the amount of money involved. Do you agree that that is done?

Mr. FULLARTON. Yes, Mr. Jones, I agreed with your answer yesterday when you stated that you had this problem, that you had been acquainted with it, and that further loans were subsequently made by the borrower. My point as you were walking in was that in some cases because the REA is obligated under the 1949 telephone amendment to provide area coverage, so far as it is feasible, that on occasion borrowers would submit loan applications that would not be in agreement with its basic area coverage concept of the act, and for this reason the REA sometimes was forced to increase the size, so that area coverage would be carried out.

Mr. JONES of Missouri. Do you not think that the operator of the telephone system who has been a man of experience of many years, would know more about what would be an operation that would permit him to pay off this loan than someone sitting up here in Washington?

Mr. FULLARTON. Yes, sir; I believe, generally, that the people in this business are competent to do that, but I am not sure that the Congress interpreted the 1949 act in that fashion.

The CHAIRMAN. Will you yield to me?

Mr. JONES of Missouri. Yes.

The CHAIRMAN. I would like to comment on that. The law plainly states that the Administrator cannot make these loans unless the applicant agrees to provide area coverage, and that if a man brings in an application to serve only a part of an area, as many companies very naturally do, that the REA Administrator has no right to make him a loan, unless he is willing to service these thinner areas, and that is the whole thing about this rural telephone service, and the basis on which it was felt it was justified in using public funds to make these loans—it was to get to areas that could not be justified by the profits from the service, that is, the profits that could be made out of these areas. Certainly, the REA Administrator would be

violating the existing law if he made a loan that did not carry out the 1949 amendment. And this is not to say that the applicant is doing anything wrong if he wants to serve only a part of the people, but the program contemplates serving all of the people. That, obviously, costs more money. In many cases, it is not a profitable business, certainly not as profitable as serving those on the main highway. It is the same thing that we have in other fields. There are always those who will be willing to serve the more profitable areas. But the purpose of this whole program is to serve the people where it was not so profitable. This bank bill has nothing in the world to do with that requirement of the Administrator because it is in the law now—it will remain there whether we pass this bank bill or whether we do not pass this bank bill. That phase of the thing is not touched by the legislation under consideration here. That is a basic part of the existing law and has been ever since we have had a telephone bill.

Mr. JONES of Missouri. I do not want to get into an argument with the chairman about this thing, but I was just calling your attention to the fact of the situation that I brought up that with a little persuasion the administrator who made the loan did reduce the amount of the loan. I do not think that he violated the law. I think that he was finally convinced that the operator of the telephone company had a valid reason why he did not want to get himself up over his head in a loan that he might not be able to pay off. I commended him for it.

The CHAIRMAN. I think that he is to be commended, but I do not see how this affects this bill one way or the other, because this bill does not change that portion of the existing law one way or the other. Certainly, the administrator should always be available for discussion and should be available to reason and should be available to hear all of the facts, and to make a decision. I am not suggesting that he violate the law, either. I am not suggesting that anything was wrong in talking about it, but that is the present law. And we will not change it by passing this bill, and neither will we change it if we do not pass this bill.

Mr. JONES of Missouri. Mr. Chairman, the thing that I am trying to do is to point out that because of the experience I have had, not only with the REA, but with other Government agencies, I know that there is an inclination on the part of the bureaucrats to exercise the maximum amount of authority. And I would just like to throw in a few things every once in a while to put a little brakes on it, to try to slow them down, to get somebody to watch them. And I am going to raise a little Cain on occasion. And if they go beyond what I think is a reasonable application of the law, I will do so. That is all I am trying to bring out here. If it has any effect, good. If it does not, I have not wasted much time. Again, that is all I am trying to do.

The CHAIRMAN. Are there any further questions of Mr. Fullarton? If not, we are very much obliged to you and your associates.

Mr. FULLARTON. Thank you.

The CHAIRMAN. I understand Mr. Mathias wants to introduce our next witness. I do not know what the situation is.

Mr. MATHIAS. I appreciate this opportunity, Mr. Chairman, to introduce Mr. Lucier, who is president of the Continental Telephone Corp., of St. Louis, Mo. His company does provide a great deal of service to my district in California. So I would like to have this oppor-

tunity to introduce Mr. Lucier at this time. I believe that he is going to file a statement. He can say that for himself, however. Thank you, Mr. Chairman.

The CHAIRMAN. We are glad to have you here, Mr. Lucier, and we will be glad to hear from you now.

**STATEMENT OF PHILIP J. LUCIER, PRESIDENT, CONTINENTAL
TELEPHONE CORP., ST. LOUIS, MO.**

Mr. LUCIER. Mr. Chairman and members of the committee, in view of the testimony that was given yesterday on the part of the witnesses who supported the bill, I am not going to file a statement today, but I am available for any questions that you might want to ask.

The CHAIRMAN. Are there any questions? Mr. Teague of California.

Mr. TEAGUE of California. You say that you do support the bill, if I understand it right.

Mr. LUCIER. Yes, sir.

Mr. TEAGUE of California. I have just one question then. You, undoubtedly, know that we have a Federal deficit of, approximately, \$30 billion?

Mr. LUCIER. Yes.

Mr. TEAGUE of California. Am I correct in assuming that you are one of those persons who has no objection to paying additional Federal income taxes?

Mr. LUCIER. No, sir; that is not right—no more than anyone else.

Mr. TEAGUE of California. Do you think that the Congress would be making a mistake to raise the Federal income tax or to add a surtax?

Mr. LUCIER. I am not qualified to pass on that.

Mr. TEAGUE of California. All right. I think that we cannot go much further than to make this observation—that \$30 million or \$20 million for rat control is not very much—that is not very much, I repeat, but in some ways these bills have to be paid. If we embark on these new programs, in my opinion, the Congress has no way to go except to raise the income tax.

Mr. LUCIER. Mr. Teague, may I make this comment about this bill?

Mr. TEAGUE of California. Yes.

Mr. LUCIER. It does seem to me that it is a step and perhaps a long step toward getting the Government out of the telephone loan business. It may take 20 years to do it, but it is a constructive step in that respect. So that, at least, we are tending toward the direction of devising a mechanism for, eventually, the Government getting out of this business and not to make loans.

Mr. TEAGUE of California. I am sure that you must believe that or you would not be supporting the bill. Personally, I think that we will continue with the 2-percent loan and then have this additional subsidy on top of the present program. That is my opinion.

Thank you. That is all, Mr. Chairman.

The CHAIRMAN. Mr. Dole.

Mr. DOLE. Yesterday I made reference to an article that appeared in Forbes magazine. You probably read the article?

Mr. LUCIER. Yes, sir.

Mr. DOLE. This was by Mr. Wohlstetter, who stated, "We have over \$100 million of 2 percent REA debt that we inherited from other companies."

You are familiar with that statement?

Mr. LUCIER. Yes.

Mr. DOLE. How many of your companies were REA borrowers?

Mr. LUCIER. I cannot give you the exact number. We have some 24 or 25 REA financed companies. It might be appropriate to give you a couple of short statistics. As of June 30, our consolidated debt position to the companies which we own, which had borrowed from the REA, was about \$132 million.

Of that amount about \$2,500,000, or some 1.5 percent was applied for subsequent to ownership by Continental. Something less than that, about \$1,500,000 has actually been drawn down. So that, so far as Continental is concerned, they have not subsequent to our ownership been a borrower except in well, less than 1½ percent of the total amount. As a general policy once a company which has borrowed from the REA is owned by Continental we do not continue to borrow from the REA. There have been three exceptions. One in northern California, up in the mountains which Mr. Mathias will be familiar with, one in West Virginia, and one in the Appalachian section of North Carolina. The total amount of these applications is about \$2,500,000, \$1 million in California was applied for in April of 1964, if I recall correctly, and we never received the money.

Mr. DOLE. Would you have purchased these companies under any other circumstances if they had not been financed by 2-percent money?

Mr. LUCIER. Mr. Dole, the fact that they have 2-percent money has nothing to do with the purchase.

Mr. DOLE. You would not care then if we closed that loophole?

Mr. LUCIER. I do not know what kind of loophole you are talking about.

Mr. DOLE. To change the law so that if an REA borrower sells to a holding company or to anyone else, that then the loan to the REA is immediately due and payable.

Mr. LUCIER. I will phrase my answer to the question in the form of a question: Why should the purchaser of an REA company be treated any differently than in the purchase of any other company? That will be against the public interest, in any respect. As a practical matter, when we get to the State regulatory basis, I would suspect that, except in rare instances and in special circumstances, I do not believe there is a regulatory body in this country that will allow the substitution of 6-percent money for 2-percent money when the results would, ordinarily, be a substantial increase in the rates of the companies, including, for instance, General Telephone that has purchased REA financed companies and have continued with the financing, but they have not paid them off. You can say that it is because of economic infeasibility or regulatory disapproval, but the 2-percent money per se has nothing to do with the purchase or the subsequent operation of the property.

Mr. DOLE. That is compulsory, too, but Mr. Wohlstetter stated, "What's better, 6 percent on \$50 million or 2 percent on \$100 million?" And you say it does not make any difference?

Mr. LUCIER. No, sir, he is talking about a mathematical fact. I might, also, add that most of those things are quite out of context. It is true that once the debt is there, that it is a lesser interest payment.

Mr. DOLE. It does make a difference then?

Mr. LUCIER. In the matter of the purchase, no, sir. Under regulations based on the cost of money, the cost of the telephone service, that is a part of the cost of doing business, and it does make for lower telephone rates.

Mr. DOLE. You can afford to pay more for that property then?

Mr. LUCIER. That is not so, because you are looking, primarily, to the return on your equity. And that is not related to the cost of the interest, because you know you are only allowed a lesser rate of return when there is 2-percent money on that portion of your total capitalization. It just does not have anything to do with it. If this were so, we would continue to borrow 2-percent money.

Mr. DOLE. Thank you. That is all.

Mr. LUCIER. If I may add this, strictly speaking, on the basis of the borrower records, these other people are opposed to further REA money, then if they look at our record, they ought to recommend that all of the REA borrowers sell out to Continental, because this would be, in effect, the end of the 2-percent money program. This is what experience has shown.

Mr. KLEPPE. Will you yield?

Mr. DOLE. Yes.

Mr. KLEPPE. Mr. Lucier, you indicated that it makes no difference in the purchase price, the fact that these loans do exist?

Mr. LUCIER. No, sir. I mean, yes, I made that statement.

Mr. KLEPPE. Yes. You made that statement.

Mr. LUCIER. Yes.

Mr. KLEPPE. You, also, indicated that there are many jurisdictions with lower rates because of the 2 percent interest rate.

Mr. LUCIER. There are advantages to the subscribers, too.

Mr. KLEPPE. And to the subscribers?

Mr. LUCIER. Yes, sir.

Mr. KLEPPE. You indicated that it makes no differences in the purchase of the company. Am I correct in saying that from your standpoint as a purchaser it would make no substantial difference, but it does make a difference to the seller, to the extent that you are buying a piece of property that has a known opportunity for a rate of return on the investment, based on a 2-percent loan, and the interest accruing thereon, and with that loan rate higher you would have to pay a higher price for that business or to charge higher rates; is that correct, or is it not?

Mr. LUCIER. The second part is correct, that is, the rates to the subscriber would be higher if the same amount of money had been borrowed at 6 percent, let us say, rather than 2 percent, but so far as the return on the equity, the ownership, the fact that the money rate on the loan portion, that has no material bearing.

Mr. KLEPPE. That is what I understand is the reason why you say that the 2 percent makes no difference, from your standpoint as a purchaser.

Mr. LUCIER. And I do not see how from the standpoint of the seller as a seller that it does.

Mr. KLEPPE. What you are saying then is that the only advantage involved is to the subscriber?

Mr. LUCIER. Yes, sir. There is this additional advantage, and, again, this is not related to the cost of the money. The money is available or has been—I am talking historically. These small companies have not

had any other source of money at any rate, and this is the real advantage. And in a great many instances, certainly, most of the instances so far as the private borrowers are concerned, availability is the important thing. This is why, generally, they support this bank bill at higher interest rates.

Mr. KLEPPE. What Mr. Dole and I are trying to get at, I am sure, is that there is a difference between the going bank rates, if this were passed, let us say that it would be 6 percent versus the 2 percent, that somebody has to be getting the benefit of it, and what you are saying is that the somebody is the subscriber.

Mr. LUCIER. Yes, sir.

Mr. KLEPPE. It is not the purchaser—it is not the seller?

Mr. LUCIER. The seller only in the sense that he had the funds available to him where he might not have had any funds available to him, but that is not related to the interest rate.

Mr. KLEPPE. All right. Thank you. That is all.

Mr. MYERS. If you will yield?

Mr. DOLE. Yes.

Mr. MYERS. Mr. Lucier, you have been talking about these companies. How do you keep them within your corporation, Continental—how are they held, are they holding companies, do you keep them as subsidiaries, or how?

Mr. LUCIER. The companies we purchase are subsidiaries of Continental, which is a holding company.

Mr. MYERS. Then you operate them as separate corporations?

Mr. LUCIER. Yes, sir. Many of them, for instance, the majority—I think we have purchased five or six small Georgia companies, small separate corporations, all of which were financed by the REA. In that instance, in Georgia, it was partly for our benefit in consolidating those into one corporation—that was to our advantage. For instance, the REA rightfully required a separate certificate from a CPA at the end of each year. That would cost about \$2,000 for the certificate. When we consolidated them we only had to have one certificate, instead of six certificates. It is true in that instance, and it is generally true that the Georgia Service Commission, I should say, was insistent that they be consolidated. We now have one larger, better company, with a lot of economies, a lot of efficiencies, a better coordinated company, certainly, better cash flow benefits. So we have one company in Georgia where there were six individually owned companies. These have all been consolidated into one company. So that now we have but the one Georgia subsidiary and for a moment in time we had six.

Mr. MYERS. Then the REA loan was refinanced into one loan?

Mr. LUCIER. Yes, sir. They were just simply consolidated, no terms changed.

Mr. MYERS. The loan was not rewritten?

Mr. LUCIER. I am sorry, I cannot answer that question. I do not know whether there was.

Mr. MYERS. Something was entered into?

Mr. LUCIER. Yes, sir.

Mr. MYERS. How do you happen to acquire all of these companies? Do you have people looking for them, or do the companies come to you?

Mr. LUCIER. Both ways, sir. All of the companies in the United States are listed in several directories. Everybody has knowledge of every company.

Mr. MYERS. Then some approach you and you approach some of the companies that you purchase?

Mr. LUCIER. Yes, sir.

Mr. MYERS. Do you have the figures of how many companies you have purchased in the last 5 years?

Mr. LUCIER. Roughly, 350.

Mr. MYERS. How many of those had REA loans?

Mr. LUCIER. About one half or a little less—45 percent of our total telephones in service are financed by the REA.

Mr. MYERS. You spoke a moment ago about the rate of return on the investment.

Mr. LUCIER. Yes, sir.

Mr. MYERS. When you go out to purchase a company, about how many times annual earnings do you pay for the company? Do you have those figures?

Mr. LUCIER. Sir, that would vary in the 350 instances.

Mr. MYERS. Give me a couple of extremes.

Mr. LUCIER. Some of the companies that were purchased had a loss. If this were true, how many times losses would we be paying? In a loss company, there would, obviously, be opportunities there in the way of increased service; and, therefore, increased revenues that the local company had not been able to have foreseen or chosen to take advantage of. We look to the future and not to the past. I would say that, by and large, and, historically, when we are talking about a small company, the lower the earnings the higher we would pay in terms of historical earnings. But the least that we would pay would be in terms of their foreseeable earnings in the near term future.

Mr. MYERS. That does not answer my question exactly, does it?

Mr. LUCIER. I do not know how else to answer it.

Mr. MYERS. You do not know how many times you might buy a bankrupt company then for some reason?

Mr. LUCIER. What I am saying is that if it had a loss—and there have been some that were in a loss position—if you paid anything for it, how many times earnings is this? If the company is extremely well run, has taken advantage of all of its opportunities, then the price in relation to its earnings would be lower, perhaps 10, 15, perhaps 20 times earnings.

Mr. MYERS. Do you have any figures at all as to what you have been paying for these companies?

Mr. LUCIER. Well, sir, we have historical records, but most of them—99 percent of them—have been acquired for stock, so that you are not paying any cash at all. And the times earnings factor happens to be what the stock market happens to be at the time. All listed telephone companies, generally, are at lower levels than they were, say 6 months ago. If we concluded a transaction 6 months ago, taking the Continental price at \$33, now it is \$28, as against \$33 when we signed the agreement, and then concluded the transaction now, what did we pay for it? The stock went down 10 percent or so, which is generally true of all telephone companies. So that when you give them stock, all you are saying to the individual is, "You can have, roughly, the same

multiple in times earnings as we enjoy in the stock market." And these small telephone companies say, "My stock may not be a listed security, but why should my stock be worth any less than your stock which has a known multiple?" And, generally speaking, all listed telephone securities have had generally high multiples for the last four years.

Mr. MYERS. When you buy a company, you are interested in that?

Mr. LUCIER. That is right. That is why we relate their income to our stock, that the number of shares that we give, not in terms of what our shares are worth.

Mr. MYERS. You would know something about the annual income, I think.

Mr. LUCIER. What their income can be, yes—not what it has been.

Mr. MYERS. You know what it has been.

Mr. LUCIER. That is not the only thing that we know at all. We know very well what it can be.

Mr. MYERS. Then the interest rate you are paying for it does have something to do with it. You say that you are anticipating. And the only way to anticipate is to know what the expenditures will be. And one is overhead. Another is interest paid on the money.

Mr. LUCIER. Well, the rate of return under regulations is by and large based on the cost of the money. For instance, you may be allowed 3 or 4 percent return if you are financed by the REA and 6 or 7 or 7.5 if you are not. But it all comes down to the return on your equity which is substantially the same, which will be 10 to 15 percent. We turn on equity. So under regulations, if you get a lower interest rate, if you have to pay a lower interest rate, it does not flow to the stockholders—it flows to the subscribers.

Mr. MYERS. I have been in the banking business for a few years. We always look at the earnings. That is one way you establish what something is worth. I do not know anything about the telephone business and I still do not.

Mr. LUCIER. This is not only true of ourselves, but of others. We make a judgment as to what the future returns can be—not what it has been historically. Small companies, for instance, if they are family owned corporations, they may conceivably have no earnings at all. They take it all out in salaries. If the owners are retiring—and, again, in a small company it may go from zero earnings to 10 or 15 per cent earnings, simply by the change of one thing. So that we apply what we know about the business. We estimate the economies and the savings that can follow and determine what this company can earn in the future. Obviously, for the commercially financed companies, United Utilities has, for instance, paid 40 times earnings—they are not buying it on its historic basis, but on the future.

Mr. MYERS. That is how you really make your money, by consolidation into a larger operation?

Mr. LUCIER. It is one of the elements, yes, sir.

Mr. MYERS. Then finances also might be beneficial?

Mr. LUCIER. The availability of funds.

Mr. MYERS. Refinancing, yes.

Thank you, that is all.

The CHAIRMAN. Mr. Zwach?

Mr. ZWACH. Lucier is French?

Mr. LUCIER. French Canadian.

Mr. ZWACH. How much of the REA 2-percent money do you have within your company?

Mr. LUCIER. \$132 million.

Mr. ZWACH. What is the amount?

Mr. LUCIER. \$132 million. I can give you the figure as of June 30. It is \$132 million out of, roughly, \$360 million, sir.

Mr. ZWACH. About one-third?

Mr. LUCIER. Yes, sir.

Mr. ZWACH. So that your blend interest rate has been reduced to the extent that 2-percent money is lower money than the money borrowed on the market?

Mr. LUCIER. Yes, sir.

Mr. ZWACH. I think the committee is interested in this to learn to what extent you serve urban centers. What part of your service is urban centers, and big centers?

Mr. LUCIER. Well, I do not know exactly what your definition of "urban centers" is.

Mr. ZWACH. Let us say municipalities, towns, cities.

Mr. LUCIER. Relatively few of our total exchanges exceed 5,000 telephones. Perhaps, roughly, we would be serving about 1,500 towns or have that many exchanges. I would say probably less than 25 of them would exceed 5,000 telephones in any one exchange.

Mr. ZWACH. What is the biggest exchange?

Mr. LUCIER. Probably De Kalb or Sycamore, Ill.

Mr. ZWACH. How big a community is that in population?

Mr. LUCIER. The population would be roughly 25,000 to 35,000.

Mr. ZWACH. How many of your companies in these areas have 2-percent money?

Mr. LUCIER. Well, in our larger exchanges we do not have any REA financing. It depends on the circumstances, but by and large—

Mr. ZWACH. You perhaps have an overall interest plan?

Mr. LUCIER. No, sir, no, sir. Each one of these are separate companies, separate areas, and only on a combined balance sheet would there be any blending. Each company, from the standpoint of regulation and earnings, has to stand on its own.

Mr. ZWACH. Except that you would have an advantage over other companies that perhaps pay 5 percent for all of their borrowings?

Mr. LUCIER. We do not have any advantage in Continental. We have purchased companies that have lower interest rates.

Mr. ZWACH. You mean that rate regulatory groups give the rate reduction to the customer?

Mr. LUCIER. Yes, sir. That is true.

Mr. ZWACH. Which helps you to pick up new growth?

Mr. LUCIER. By and large, because of the thinness of the areas where the REA financing has been used, the actual dollars are about the same. What you are saying is that it would have cost those customers a lot more had they not had available to them through the REA the 2-percent money.

Mr. ZWACH. I should say to you that I am on a farm. I have this telephone service. I also have the REA electric service. It is in our interest to see that all have this service. In the overall picture I would like to know how you might have an advantage over other companies because of this low interest rate.

Mr. LUCIER. It is very difficult to make a generality, because the areas served are different. For instance, we are converting some 15 exchanges this year to 100 percent single-party service. All of these are areas that are strictly rural areas. And yet we are not using in those companies—and it is partly coincidence—any REA funds.

Mr. ZWACH. Are you doing that because of the regulatory requirement or REA requirements? Or are you doing that on your own?

Mr. LUCIER. It has nothing to do with the REA. We are doing it because the more service we sell—and there is a demand for the service—the more revenue we get, and the more money we make.

Mr. ZWACH. And the 2-percent money makes it easier for you to do this?

Mr. LUCIER. Well, in this instance that I am talking about we have no 2-percent money. This is strictly conventional financing in those exchanges that we are converting to single-party service.

In the area of what we are talking about, remember that nine out of 10 of all of the companies sold are sold in the competitive atmosphere. We do not wander in, unfortunately for us, and buy a company without the owner's soliciting and seeking out other bids. Certainly, in the total number of telephone companies that we have purchased, I am sure that there are some exceptions where we have not had competitive bidding, but every time we buy a telephone company somebody else is also trying to buy it.

Mr. ZWACH. Somebody wants to sell, too.

Mr. LUCIER. Somebody wants to sell. A great number of people want to buy.

Mr. ZWACH. You do not think that this 2-percent setup gives you an undue advantage that you have for the one-third?

Mr. LUCIER. Two percent is there already. Any advantage or no advantage exists. And anyone bidding on the property has the same set of circumstances to bid on it. It happens that we bought mostly small companies, because we were small. We only started 6 years ago, and we cannot go out and buy something 10 times as big as we are. So we kind of made a specialty of small companies, because we were small. In spite of that, we have competition from other holding companies and other local companies and will continue to have competition, but it is a part of the game, and many companies that we bought did not have REA financing that were small companies. Anybody who owns a small company and wants to sell it is going to have a lot of people knocking at his door, whether or not he has REA financing. It is just not otherwise. We bought small companies because we were small.

Mr. ZWACH. Thank you, Mr. Lucier.

That is all, Mr. Chairman.

The CHAIRMAN. Mr. Jones?

Mr. JONES of Missouri. I have two questions. One, after you buy these companies have you ever had any REA loans made to Continental or to the companies that you buy?

Mr. LUCIER. Three, sir, which total about \$2.5 million, out of, roughly, \$132 million. That is not wholly correct, because we actually have not received the funds on one of those three loans that we made. That is 1.5 percent of the total money outstanding owed to the Government by the subsidiaries of Continental which were applied for after we

owned the companies. We have provided \$26.5 million, some-odd, to the REA financed companies, from conventional loan sources after we owned them.

Mr. JONES of Missouri. Is it the policy or the custom or the operational procedure, I guess, that the more customers you have in one exchange the higher the rate is going to be for that exchange—is that true?

Mr. LUCIER. That is not a policy, sir. Again, the rates are set on the investment. And by and large the telephone business is the kind of business where the more telephones you have in a give area, it does not necessarily mean that the rates will be lower—it is quite the contrary.

Mr. JONES of Missouri. That is just the contrary to the electrical concept.

Mr. LUCIER. Yes, sir; it is quite different.

Mr. JONES of Missouri. It is just the opposite?

Mr. LUCIER. By and large the more—

Mr. JONES of Missouri. What I am trying to get at is as to this case down in Georgia where you took six companies over and consolidated them—what was the increase in the rates per subscriber afterwards?

Mr. LUCIER. None, sir—no increase.

Mr. JONES of Missouri. That is not in conformity with what you said happens. If you had six small companies and you put them into one large company, then it would seem to me that the rates would have gone up.

Mr. LUCIER. No, sir. What I was talking about is concentration in a given area. Now, again, it is hard to make a generality. A large metropolitan area will have many technical complications that cost, a very high investment, and by and large will have higher rates. Part of the reason, however, is because the service is worth more.

Now you get into a very thin area, such as in western North Carolina, for instance, or in Kansas, where Mr. Dole is from, where the rates will be fairly high because of extreme density, but some place in between, by and large, in the high density areas, the metropolitan area will call for a high investment and there are other exchanges where you have very scattered, sparse areas that will take a high investment per telephone, too.

In the middle it is different.

Mr. JONES of Missouri. Of course, when you go from eight-party-line service to one-party-line service, you naturally will charge for that.

Mr. LUCIER. Yes, sir; that is true.

Mr. JONES of Missouri. You said a minute ago that when you increased the number of subscribers that you could expect the rates to go up. I am not criticizing you for doing that. I was trying to find out what happened in Georgia where you purchased six companies and put them into one company. That was evidently an unusual circumstance. And you did not increase the rates there.

Mr. LUCIER. No, sir. That was not an unusual circumstance. The act of putting the companies together made possible certain economies. It meant one thing, that we would make somewhat more money within the regulated process allowable. It also means very likely that that company will not get a rate increase as soon as if they were six separate companies. There are wages, all kinds of things that change all of the time—material costs go up. In any given circumstance, a company may or may not need a rate increase over some period of time, but

the fact of the consolidation in that instance makes for economies. The number of subscribers in the company has not so much bearing, as in the problem that you are talking about, as does the concentration. You cannot move the subscribers together. In other words, the company may have many subscribers, but if they are not in the right areas concentrated, then it costs more.

Mr. JONES of Missouri. I think that you did not get my point. In my home county the telephone companies always want to make it so that you can call more towns. And every time you can call more towns without it being long-distance, the rates go up.

Mr. LUCIER. Your local rates go up.

Mr. JONES of Missouri. Your basic rates for that telephone go up.

Mr. LUCIER. Yes, sir.

Mr. JONES of Missouri. Although 90 percent of the people living in that small town do not need that extra service, but it is forced upon them, so that is what I am trying to get at. When you do combine and consolidate, as in the case of the six companies, you continue to operate them as separate entities, although they were grouped together in the financial statement as one company.

Mr. LUCIER. Yes, sir.

Mr. JONES of Missouri. That is all. Thank you.

The CHAIRMAN. Mr. Wampler?

Mr. WAMPLER. You testified that Continental Telephone Corp. is a holding company?

Mr. LUCIER. Yes, sir.

Mr. WAMPLER. What investments do you have other than telephone companies?

Mr. LUCIER. We own a manufacturing company—technically two of them—one very small. We also have a CATV property. We own a leasing company. I think that about summarizes it.

Mr. WAMPLER. Were you present at the hearing yesterday?

Mr. LUCIER. No, sir; I was not.

Mr. WAMPLER. Have you had an opportunity to analyze and study the amendments that were offered by Mr. Bollinger?

Mr. LUCIER. Yes, sir.

Mr. WAMPLER. Do you find yourself in opposition or in agreement with them?

Mr. LUCIER. Generally, in agreement. I concur in their findings; that is, of the USITA.

Mr. WAMPLER. Let me ask you this question. Would your company generally pay more for a telephone property that has the 2-percent REA loan than one that has conventional financing?

Mr. LUCIER. No, sir; it will not.

Mr. WAMPLER. It will not.

Mr. LUCIER. No, sir; it will not.

Mr. WAMPLER. There are some of us on the committee who feel that there is a loophole in the law as to a property that has a 2-percent REA loan. Is it not a fact that the seller of the property can benefit substantially where there is 2-percent money?

Mr. LUCIER. No, sir; I do not believe that he does, so far as the value of his property is concerned. I think that there is a general misunderstanding as to this so-called loophole, because a group of individuals who are stockholders have elected under the laws of the

United States, and with the encouragement of the telephone associations—in view of the fact that he has no other choice as the availability of money—to pursue or to borrow under this act. And under the proposed act where he should not be denied what any other stockholder of any other company who has other resources available to him can do, which is about the increased value of his common stock or his equity—the fact that he borrowed 2 percent money does not get him as a holder or as an owner any particular advantage. The advantage through regulation is passed on to the subscriber.

The talk about denying him what everyone else in the business has got is no reason to deny him that—it is not a loophole. I do not understand it as a loophole. It has no direct bearing on his ability to sell.

Mr. WAMPLER. Since you feel it is not a loophole, then you have no objection if we tighten the language in this respect?

Mr. LUCIER. I do not know, I would want to see the language. The language that is in the proposed bill is not objectionable to Continental. I understand that it is not objectionable, generally speaking, to the USITA and it was not objectionable to the people who were here yesterday.

Mr. WAMPLER. Let me clear up the record. I do not feel that this proposed amendment is directed to Continental or to anyone else in particular.

Mr. LUCIER. I will have to disagree with you. I believe that it must be called the Continental amendment. [Laughter.]

Mr. WAMPLER. Do you support the Continental amendment then?

Mr. LUCIER. I do not think that it will accomplish what they think they are going to accomplish.

Mr. WAMPLER. I can only speak for myself. Let me say that my concern is in seeing the rural areas of America have the telephone service they are entitled to. We do not want to see the taxpayers' money used unwisely, or to unjustly enrich those who sell and those who purchase.

Mr. LUCIER. I do not know of anyone who disagrees with you. Both general purposes are worthy objectives. So long as this bill is in substantially the same form as it is today, these objectives will be accomplished. There is general agreement on them.

I think there is considerable misunderstanding—and I do not want to take any more of the committee's time about the function of holding companies in the telephone business in that they may or may not relate to the historical borrowings of the individual subsidiaries.

Mr. WAMPLER. Thank you. That is all.

The CHAIRMAN. Mr. de la Garza?

Mr. DE LA GARZA. I do not want to ask a question, Mr. Chairman. I wanted to say to the witness that, apparently, that he does seem to have an enterprising company that has been quite successful. I think that we should commend him. We need more of that type of enterprise in this country where we get somebody to do something for himself.

Mr. LUCIER. I might add that I do not know whether you are aware of the fact, but we have a plant in your district that is very successful. [Laughter.]

The CHAIRMAN. Are there any further questions? Does anybody else have any questions that they want to ask?

Mr. Dow?

Mr. Dow. Just one quick question.

Mr. Lucier, generally, in the States of the United States do the regulatory commissions limit or control the rate of return or the earnings of such companies as telephone companies?

Mr. LUCIER. Sir, in 49 of the 50 States, Texas excluded, there are regulatory commissions which regulate the telephone companies, all of them, in relation to rates. And most of them in relation to financing. We are not operating in a vacuum in any respect.

All of these loans that the REA makes, or a substantial portion of all the loans made by the REA, must be reviewed and approved by regulatory bodies. All, or virtually all, acquisitions by us or anyone else, generally, are under some regulatory procedure, either in the State or in the Federal Communications Commission or both.

There is no mystery here. All matters that relate to the telephone business are matters of public record.

Mr. Dow. What proportion, actually, limit earnings of the companies—what proportion of the States do?

Mr. LUCIER. Forty-nine out of the fifty, sir. In Texas, the regulation is on a local, or city, level. Their purpose is, also, to limit it. This is, really, the function of the commissions. They have other functions, like insuring good service but primarily it is to limit the rate of return.

Mr. Dow. Suppose that you made a very skillful purchase and you succeeded in obtaining a company that on balance returned you an interest rate of 20 percent—how would the regulatory commission in most of the States regard the rates in a company of that sort?

Mr. LUCIER. I presume that you are talking about—well, 20 percent on a rate base—and there would be one obvious answer, that the rates would be reduced. Generally speaking, an allowed rate of return, depending on the cost of the money, varies from 3 to 7 percent.

Mr. Dow. Have any of the commissions ever required you to reduce rates?

Mr. LUCIER. Yes, sir.

Mr. Dow. Thank you, Mr. Chairman. That is all.

The CHAIRMAN. Mr. O'Neal.

Mr. O'NEAL. I do have one question. I am interested in companies that you acquired in Georgia. Are they all in the same section of the State? Would you identify them?

Mr. LUCIER. Mr. O'Neal, I think this is down in your territory. Generally, it is on an arc, running from Statesboro, Savannah, in that area, down around through the southeast, to Donaldsonville.

Mr. O'NEAL. They are scattered all across the State?

Mr. LUCIER. That is right.

Mr. O'NEAL. They are not in one area?

Mr. LUCIER. Not all of them, but there are several of them which are grouped together.

Mr. O'NEAL. Could you name any of the others?

Mr. LUCIER. Yes, sir. The towns, sir?

Mr. O'NEAL. Yes.

Mr. LUCIER. Well, there is Claxton, Homerville—one of the areas up around Statesboro—down in your territory, sir.

Mr. O'NEAL. Some of them are 250 miles apart.

Mr. LUCIER. From one extreme to the other extreme.

Mr. O'NEAL. From Statesboro—

Mr. LUCIER. No two that are that far apart.

So that there are two extremes, but they are scattered all the way in between. I would suspect 35 to 40 miles. The group over near your territory, sir, would be the farthest removed from the balance of them. Incidentally, in our office in Georgia, they also are charged with the operation of a company in north Florida, right across the line from that part.

Mr. O'NEAL. Thank you, sir. That is all, Mr. Chairman.

The CHAIRMAN. Mr. Jones.

Mr. JONES of North Carolina. Those you purchased in the State of Georgia, none were subsequently financed with REA money, prior to your purchase, were they?

Mr. LUCIER. Actually, we feel heir to that group. Another holding company purchased those companies and we, through a merger with another holding company, came into possession of the stock of those companies. All of them had been financed by the REA prior to our acquiring them. Subsequent thereto, none of them had borrowed or made new applications for loans from the REA.

Mr. JONES of North Carolina. That is all. Thank you.

The CHAIRMAN. If there are no further questions, we are very much obliged to you, Mr. Lucier. We appreciate your attendance here.

Our next witness is Adm. William C. Mott, executive vice president of the United States Independent Telephone Association, who is accompanied by Hugh Wilbourn, president of the Allied Telephone Co., of Little Rock, Ark.; Harold Payne, chairman of the REA Borrowers Committee and president of the Telephone Utilities of Pennsylvania, Export, Pa.; William Kingman, president of the Chenango-Unadilla Telephone Co., Norwich, N.Y.; and Bill Baine, president of the Mid-Texas Telephone Co., San Antonio, Tex.

We welcome you here, gentlemen. We will be glad to hear from you now.

STATEMENT OF ADM. WILLIAM C. MOTT, EXECUTIVE VICE PRESIDENT, UNITED STATES INDEPENDENT TELEPHONE ASSOCIATION; ACCOMPANIED BY HUGH WILBOURN, PRESIDENT, ALLIED TELEPHONE CO., LITTLE ROCK, ARK.; HAROLD PAYNE, CHAIRMAN, REA BORROWERS COMMITTEE, AND PRESIDENT, TELEPHONE UTILITIES OF PENNSYLVANIA, EXPORT, PA.; WILLIAM KINGMAN, PRESIDENT, CHENANGO-UNADILLA TELEPHONE CO., NORWICH, N.Y.; AND BILL BAINE, PRESIDENT, MID-TEXAS TELEPHONE CO., SAN ANTONIO, TEX.

Mr. MOTT. Mr. Chairman and members of the committee, in previous testimony before this committee we made the point that our industry, like all industries affected by this bill, was not unanimous in its viewpoint on all provisions of the REA bank bill.

The last time I testified, I pointed this lack of unanimity out. I think that yesterday's testimony was an example which demonstrates to the committee that there has been and is some difference of opinion with respect to particular provisions of any bill which treats of an REA

bank with intermediate financing. However, it seemed to me or, at least, it was my impression of yesterday's testimony, that all parties concerned have come into agreement with the broad objectives of H.R. 12066 and what this committee is trying to accomplish by coming out with an REA bank bill with intermediate financing.

We have a policy directive in our association, the United States Independent Telephone Association, which gives authority to the REA Borrowers Committee, which is chaired by Mr. Payne to my left, and we have a quorum of that committee present here in the hearing room today, in coordination with the chairman of the legislative committee, Mr. Kingman, to go into the various bills and the amendments and pick and choose among them in the interests of the REA borrower companies and in the interests of the Independent Telephone.

So after the amendments were submitted by Mr. Bollinger yesterday, this group, the REA Borrowers Committee and the chairman of the legislative committee went over the amendments in detail and insofar as time permitted—and we did not have much time. We have submitted to the committee, and you have it before you, the comments of this group on these amendments. It is not my purpose to go into detail or to testify in detail, Mr. Chairman.

We have submitted the statement to the committee. We would prefer to rest there, unless there are questions that you would like to ask of any of our people.

THE CHAIRMAN. Your statement will be made a part of the record at this point.

(The complete prepared statement of the United States Independent Telephone Association follows:)

STATEMENT OF THE UNITED STATES INDEPENDENT TELEPHONE ASSOCIATION

The United States Independent Telephone Association like any other trade association must follow the current policy directives of its Board of Directors. As explained to the committee in our last appearance before it on March 23, 1967, our Board of Directors resolved at its meeting in April, 1966—again in October, 1966—and finally in April, 1967, that it supported “legislation which will provide supplemental financing for REA telephone companies in the form of intermediate financing and a telephone bank.”

The committee may recall that we stated at our last appearance that the Independent telephone industry was not completely unanimous in its thinking with respect to all of the provisions of the bill (H.R. 1400) then under consideration (record, page 343). The committee has in its files certain telegrams and letters which would at the time they were sent give the indication that some of our members were opposed to a bank bill, and specifically H.R. 12066, in any form.

However, yesterday happily it developed that there now seems to be no dissent from our Board of Directors objective and directive to “support legislation which will provide supplemental financing for REA telephone companies in the form of intermediate financing and a telephone bank.” I refer to the statement of Mr. Harold Bollinger on his behalf and on behalf of some eleven other Independent telephone companies in which he assured you, Mr. Chairman, that he was in favor of the broad objectives of H.R. 12066, which objectives we believe include supplemental financing through intermediate financing and a telephone bank.

The committee heard testimony from Mr. Bollinger and others yesterday which proposed certain specific amendments to H.R. 12066 which would in the witness's words “clarify and facilitate the intent of the bill and overcome the weaknesses in the present telephone loan program.” Most of these amendments have been the subject of discussion before the committee in one form or another on many previous occasions and perhaps no further words from the United States Independent Telephone Association on the subject are needed. However, the views of the Association, in accordance with its policy directives, are submitted here-

with for use by the committee in considering its action on the proposed amendments.

For the record we should state that our Board of Directors has by resolution directed our REA Borrowers Committee in coordination with the Chairman of our Committee on Legislation to pick and choose where differences appear in various bills and to support those features which, in the opinion of the committee, are in the best interests of the REA borrower companies and Independent telephony.

The chairman will appreciate that the REA Borrowers Committee and the Chairman of our Committee on Legislation have had very little time—in fact less than twenty-four hours—to consider all of the amendments proposed by Mr. Bollinger. However, they have caucused and have the following comments to make on the proposed amendments as they understand them.

Amendment No. 1, p. 1, line 9—changing the word “many” to the word “some”.

Comment: The committee accepts this amendment on the ground that getting help to the needy companies is what is important and not their numbers.

Amendment No. 2, p. 4, lines 12, 13 and 14, after the word “act;” insert the words “and no such loans shall be made if the applicant for a loan under Section 201 can qualify under the policies, terms, and conditions established for Rural Telephone Bank loans by the Telephone Bank Board.”

Comment: Our committee has no objection to the insertion since it believes that with present budgetary pressures the REA Administrator would administer the loan program in the suggested manner anyway. There would be little enough money in the direct loan program to satisfy those who need 2% money and certainly anyone who could qualify for either the intermediate rate or the full bank rate ought not to be allowed to tap the 2% fund.

While the committee agrees to the addition of the proposed language after the “:” at the end of line 12, it believes it should be followed by a “;” and the clause in lines 13 and 14 left in the bill. It can see no reason for striking this language and indeed can find none given in the testimony which advocates the excision. It believes sound fiscal administration demands the retention of lines 13 and 14.

Amendment No. 3, p. 8, lines 10 through 13.

Comment: Here it is proposed that costs of all labor (full or part-time) and all “facilities” shall be charged to the administrative cost of the bank. It is very difficult to comment objectively on such a proposal until it is priced out. Certain it is that charging “all” costs instead of just the salary of full-time employees and the administrative expenses of the bank would increase the interest rate which would have to be charged to the customers of this fledgling institution. If the interest rate is driven up so high that customers cannot avail themselves of the bank then a useless entity has been created and the broad objectives of supplemental financing through the use of a bank has been frustrated—broad objectives which the witnesses yesterday stated they supported.

It is the feeling of the REA Borrowers Committee of the USITA and the Chairman of its Committee on Legislation that during the early years of this bank when it is trying to fulfill the needs of borrowers at rates of interest they can afford, that the administrative costs and salary costs to the bank should be left in the bill as is. There is going to come a time when the bank passes to private hands when *all* expenses including the salaries of everyone concerned as well as the facilities and services will have to be assumed by the bank.

Amendment No. 4, p. 10, lines 3, 4 and 8.

Comment: We have no objection to the substitution of the words “federal government” for “Department of Agriculture”. They give the President a wider choice but don’t restrict him in any way.

Amendment No. 5, p. 11, lines 5, 8, 17 and 20.

Comment: This amendment relates to the relative number of commercial type REA borrowers to cooperative type REA borrowers on the bank board. The USITA has heretofore testified that it believes no fixed percentage should be set in the bill but only the best men from the industry selected. However, we would have no objection if it is the wisdom of the House Agriculture Committee to set the relationship in accordance with the actual percentage breakdown of the industry.

Amendment No. 6, p. 14, lines 20, 24 and 25 and p. 15, lines 1 and 2.

Comment: In this amendment it is proposed to advance the date after which Class A stock shall be redeemed and retired by the Telephone Bank as soon as practicable—by five years, i.e., from June 30, 1982 to June 30, 1977. We do not

believe that it would be possible to reach the full \$300 million capitalization by the earlier date for the simple reason that the \$30 million a year authorized to be expended for Class A stock must come out of repayments—the principal amount of which would probably not exceed \$20 million a year at the beginning. In other words, the repayments of which the Class A stock must be bought will be insufficient. While we have no objection to advancing the date per se so long as discretion is left to the Telephone Bank Board that early retirement would or would not impair the operations of the Telephone Bank we feel that the mandatory provision in lines 23-25 on page 14 and lines 1 and 2 on page 15 for retirement of Class A stock is impractical, if not impossible, of attainment. Therefore we feel that the date 1982 should be left as is and that the proposed deletion in lines 24 and 25, page 14 and lines 1 and 2, page 15 should not be made.

Amendment No. 7, p. 15, lines 3, 4 and 5.

Comment: The purpose of this amendment is to increase the return on Class A stock from 2% per annum to cost of money to the government. This is another amendment which would increase the cost of money to the bank and thus increase the interest rate which must be charged to prospective borrowers. The effect of charging higher than 2% on Class A stock would be to so affect the "mix" that it is doubtful that an intermediate fund charging cost of money to the government could be established in effective amounts. If the interest rate of the bank is pegged so high that the borrowers cannot use it then the objectives of H.R. 12066 are defeated.

Amendment No. 8, p. 17, lines 20, 21, 22, 23 and 24.

Comment: This amendment would delete language making the telephone debentures lawful investments for fiduciary trusts and public funds under the control of the United States. As we understand the language now in the bill it is not so much for the purpose of qualifying government trust funds for investments as it is to introduce often used words of art to qualify private funds, i.e., certain insurance companies and trust funds, for purchase of the debentures.

Kuhn-Loeb and Company and the Trust Department of Riggs National Bank—the banker for USITA—advised us of the effect of excising this language on the marketability of the debentures. The opinion of both institutions was that it would limit the number of private investors who would be able to purchase the debentures and thus drive up the price at which they could be sold. This in turn would drive up the interest rate the bank would have to charge.

Amendment No. 9, p. 18, line 18.

Comment: We have no objection to requiring approval by the Telephone Bank Board as well as the Secretary on loans for acquisitions.

Amendment No. 10, p. 19, line 5 would change the period for amortization of the bank loans from a maximum of fifty years to a maximum of thirty-five years.

Comment: Economic feasibility studies in consideration of telephone bank loans or indeed any kind of REA loans normally take into consideration the fact that the average service life of the facilities may be less than a fifty year term or even less than a thirty-five year term. A loan has not been approved in the past and would not be approved in the future unless these studies indicated that the proposed system could be expected to obtain sufficient revenues to meet all normal operating expenses, including maintenance of the system, make interest and principal payments on the loan, and provide funds required to finance replacement of plant components as their useful service life expired. Thus the service life of the components of the physical property and amortization period of the loans are unrelated in terms of loan security. It is our belief that the period of fifty years for a bank loan at a rate of interest substantially higher than 2% has as its objective the provision of an amortization period which will allow repayment of the loan and still leave enough money for needed maintenance and additions. This simply follows the pattern of conventional loans to public utilities.

Amendment No. 11, p. 19, line 9.

Comment: This amendment would substitute a new and untried measurement of subscriber density from "three or fewer per linear mile" to "three or fewer per square mile". All utilities base their costs on a measurement of linear miles and therefore the density has to be measured in the same way.

We have no objection to the substitution of the word "may" for the word "shall" because we think the Administrator should have discretion as to any loan he makes regardless of density.

Amendment No. 12, p. 19, lines 14, 20 and 21.

Comment: This amendment would eliminate the alternative rate of interest for the intermediate fund, i.e., cost of money to the government or 4% whichever is lower. The Board of Directors of USITA voted at its most recent meeting in

April, 1967 that the bill's supplemental financing provisions should call for a rate of interest at least equal to the cost of money to the Government. Therefore we concur in the proposed deletion in amendment No. 12.

Amendment No. 13, p. 20, line 12.

Comment: For reasons given with respect to Amendment No. 6, we feel that the date 1982 should be left as is.

Amendment No. 14, p. 20, line 17.

Comment: We have no objection to the substitution of the words "after the date of such report" in line 17 for the word "thereafter".

Amendment No. 15, p. 22, line 3.

Comment: This amendment would substitute the Secretary of Agriculture and the Telephone Bank Board for the Administrator in granting discretion to approve sales of a borrower's property.

We have no objection to the thought involved since we believe the Secretary is the alter ego of the Administrator and can be substituted for him at any time and we don't have any objection to the Telephone Bank Board having the power over Section 408 loans but we think the power should be given in the alternative instead of the conjunctive. The Secretary has power over Section 201 loans but not at all times over 408 loans. The Telephone Bank Board never has any authority over Section 201 loans. Therefore we think the language should read "without approval of the Secretary of Agriculture with respect to Section 201 loans or the Telephone Bank Board with respect to Section 408 loans."

Amendment No. 16, p. 22, line 5.

Comment: This would eliminate the words "to a holding company" and thus broaden the class of vendees who would be restricted by the language of the subsection. We have no objection to this change.

Amendment No. 17, p. 22, line 16.

Comment: This amendment would substitute thirty-five for fifty years and for reasons given earlier in connection with Amendment No. 6 we believe this to be unworkable.

Mr. Chairman, this completes our statement on the amendments to H.R. 12066 proposed by Mr. Bollinger et al. We appreciate the opportunity you have given us to comment.

The CHAIRMAN. Are there any questions?

Mr. TEAGUE of California. I have not had a chance to analyze in detail your statement regarding the amendments presented by Mr. Bollinger. It would appear hurriedly that your association agrees with some of his suggestions.

Mr. MOTT. Yes, sir.

Mr. TEAGUE of California. Particularly, those that I considered at first glance to be minor, and you disagreed with some that are more major in character; is this a fair statement?

Mr. MOTT. It is difficult to generalize, sir, but we feel that some of these amendments—and when I say, "we feel," I mean the gentlemen who are charged with the responsibility in passing on these amendments, feel that some of them would tend to drive the interest rates so high that you would create a very nice paper entity which would not be used.

Mr. TEAGUE of California. Therein lies your principal difference with Mr. Bollinger?

Mr. MOTT. That is correct. By the way, one of the amendments which was suggested we think is technically defective.

Mr. TEAGUE of California. I am trying to get into those matters. Unless the chairman wants to go into that; otherwise, I do not want to go into them now, however. I do not want to go through them item by item.

You have stated that there must be some differences of opinion within the USITA, because Mr. Bollinger testified on behalf of his company and other companies, which I am informed represent about

50 to 70 percent of the rural telephones in the country, that is, some 11 other companies?

Is that correct?

Mr. MOTT. I would not say 50 percent of the rural telephones, but they might add up to 50 percent or better of the independent system.

Mr. TEAGUE of California. Yes?

Mr. MOTT. However, I do not think that there is any basic difference any longer, if I understand Mr. Bollinger's statement, on the basic objectives of the bill.

Mr. TEAGUE of California. I think we are agreed on that.

Mr. MOTT. Yes, sir; we are agreed.

Mr. TEAGUE of California. In this connection, I have one more question, Mr. Chairman. Mr. Payne, I have here what purports to be a letter signed by you as chairman of the REA Borrowers Committee to President Johnson in June of 1965. The purpose of the letter was to support the repeal of the excise tax, but this statement also appears:

Mr. President, two percent money for telephone loans, definitely, is necessary in many instances if the intent of Congress is to be carried out.

And then you go on to say:—

However, there are instances, especially, when supplemental loans are required for updating and expanding additional facilities where the borrowers could afford to pay a rate somewhat higher, including, in some cases, interest rates comparable to the cost of money to the United States Government.

Is that still your opinion?

Mr. PAYNE. Yes, sir.

(The letter referred to above follows:)

JUNE 1, 1965.

The PRESIDENT,
The White House,
Washington, D.C.

DEAR MR. PRESIDENT: I am addressing this communication to you because of your strong support and interest in the rural people of our great country. Nowhere has this been better exemplified than in your courageous recommendation to repeal the excise tax on telephone service—an onerous tax which bears so heavily on country people.

The 1949 Telephone Amendment to the Rural Electrification Act has provided over 800 telephone companies the necessary long term monies, under a very favorable lending program, to carry out the intent of Congress to bring telephone service to rural people. The result of the passage of this amendment has enabled these companies to bring to some two million rural families (some for the first time) the blessings, economic and personal, of telephone communications heretofore enjoyed only by city people. While great strides have been made there is still a need in some rural areas to continue the kind of loans and assistance contemplated by Congress in the Telephone Lending Amendment.

This brings me to the purpose of this communication authorized by the Board of Directors of the United States Independent Telephone Association.

Mr. President, two percent (2%) money for further telephone loans is absolutely necessary in many instances if the intent of Congress is to be carried out. *However, there are instances, especially when supplemental loans are required for upgrading and expanding existing facilities, where the borrower could afford to pay a rate somewhat higher—including, in some cases, an interest rate comparable to the cost of money to the United States Government.*

The terms of the Rural Electrification Act, however, are such that the Rural Electrification Administrator has absolutely no discretion as to the interest rate charged when making a loan. He has been put in a legislative straight jacket—he must lend money at two percent (2%) and at no other rate.

Our national telephone association, through its board of directors, feels that considerable criticism of the Independent telephone industry and of the Administration could be alleviated by a change in the law whereunder the Ad-

ministrator of the Rural Electrification Act would be given discretion to apply a rate of interest compatible with the cost of money to the government in all cases except where the higher interest rate would adversely affect the feasibility of the project for which the loan is needed. The exercise of this discretion should in no wise interfere with the basic objective and intent of Congress as expressed in the original Rural Electrification Act nor would it permit the lending of money at less than two percent (2%).

We realize, Mr. President, that exercising this discretion would add a burden on the REA Administrator, but it is a burden shouldered by many administrators of federal agencies and one which we think could be borne with credit to all. As the same time, it would allow you to effect an economy in government which we note with approbation is an aim of your administration. We feel that a borrower who can afford to pay the cost of money to his government to bring a service to rural America should not be prohibited from doing so by the Act.

May we suggest that you refer this subject to the appropriate agency for study and recommendations. We would be pleased to encourage the support of our members for proposed legislation which could accomplish the twin objectives of economy in the administration of the REA program and the meeting of the expanding needs of rural telephone users.

Sincerely yours,

HAROLD G. PAYNE,
Chairman, REA Borrowers Committee.

JUNE 17, 1965.

MR. HAROLD G. PAYNE,
Chairman, REA Borrowers Committee,
U.S. Independent Telephone Association,
Washington, D.C.

DEAR MR. PAYNE: President Johnson has asked me to thank you for your letter of June 1, regarding the REA telephone loan program. He also wants you to know that he appreciates your Association's support of his recommendations for repeal of the excise tax on telephone service.

I can assure you that your thoughtful views and the proposal to provide for modification of the REA telephone loan program will be given careful consideration as the Administration reviews and formulates its budgetary and legislative proposals.

Sincerely,

PAUL M. POPPLE,
Assistant to the President.

MR. TEAGUE of California. Thank you, sir. I do have one more question, I find, Mr. Chairman.

Admiral Mott, as you probably know, I have not been convinced that there is any need for the Federal Government to get into the electric or telephone bank operations. In our minority views that were filed, there were three main reasons set forth—very distinct ones—which I will read to you, if I may, and ask you for your comments.

I at least want to have them in the record. I do not expect you to agree with them.

We objected to the electric and the telephone bank, No. 1, because of the onus of paying the subsidy on Government funds loaned to present REA borrowers and the telephone bank at 2 percent per year.

We also objected to the very real risk of never seeing \$300 million of Government funds returned to the U.S. Treasury because of loans running as long as 50 years and repayment of principal being deferred at the option of the electric bank board.

We also object to the provisions for the indefensible transfer of control of \$300 million of taxpayers' funds to non-governmental hands at the time of the bank's conversion to borrower control, without any assurance at the time or any guarantee at all that the Federal obligation would have been entirely repaid.

In other words, in this case, the subsidy would be a gift, possibly a gift, you might say, of this amount to privately owned financial institutions of Government money.

These were our objections and still are mine.

If you do want to comment on those, I would like such comment as you wish to make.

Mr. MOTT. Mr. Teague, first of all, the letter to the President of the United States, to which you referred a moment ago, was an effort on the part of the U.S. Independent Telephone Association to bring to the attention of the Chief Executive in as forceful language as we could that there were weaknesses in the REA borrowing system. Incidentally, it was sent just after he had come out with a statement giving all of the savings that he had made in Government and we thought it appropriate to go to the President of the United States and point out to him that in our judgment he had an economically unconscionable situation on his hands, because there were borrowers, and there are borrowers, who are perfectly able to pay more than 2-percent money. There are those who are able to pay the full cost of the money to the Government, and there are those who are able to pay what the full commercial bank rates would be under H.R. 12066.

We said, in effect, "Mr. President, under the present law, if a borrower were to go down to the REA and say, 'Look, you have got me strapped in, because you own a first mortgage on my property and I cannot go to a commercial house to borrow money, but I have proposed; my telephone company is doing very well, and I have got money falling out of all my pockets, and I want to pay my Government what it costs my Government to borrow money, and they would say in horror, 'I am sorry, that law does not permit that. If you want to borrow any more money from us, it has to be at 2 percent.'"

We proposed to the President, with the full approval of our board of directors, that he ought to change that law and that he ought to introduce a needs test into the law whereunder a borrower would pay what he could afford to pay between 2 percent and the cost of money to the Government to eliminate a situation we considered to be economically unconscionable.

I do not know all of the processes that go on in making up the President's mind as to what kind of legislation the President is going to sponsor, but I do know from conversations we have had with certain staff members that he was somewhat stunned by the fact that this situation existed and determined to do something about it.

I now get into a little guessing game which you probably know as much or more about as I do, but I understand that the President rejected—or the White House, or the Bureau of the Budget rejected—the proposal that we had made to him, because he wanted to wean these people away from Government financing—he did not wish, I judge, to have to continue to come up to Congress year after year and justify appropriations in his budget which would go on, let us say, forever, and have no termination, and he did not want, presumably, the Administrator of the REA to be put on the spot as to who would be entitled to what loan, and at what percentage of interest.

In other words, a sliding scale of interest in accordance with need puts the Administrator in a terrible spot. So the Bureau of the Budget, presumably in consultation with the chairman of your committee,

decided that one way to lead these people on the path to economic independence was to have a bank bill which would wean them away as rapidly as possible—as rapidly as they were able to pay—from the 2-percent money to a higher rate of interest and, eventually, away from the Government altogether.

Mr. ABERNETHY. Will you yield there? That is, for one question?

Mr. TEAGUE of California. Yes.

Mr. ABERNETHY. Does not this bill do exactly what you have presumed that the President was trying to get away from, that is, to make a determination as to who would get the cheap money and those who would get the higher interest money? That one group would continue to get money directly from the Government, from the REA, from the Telephone Division, and that the other group would get it from the telephone bank, at REA rates? It does exactly that, does it not?

Mr. MOTT. It does it in somewhat a different fashion. It has an ending down the road to get it thoroughly out of the Government's hands which other programs do not have.

Mr. ABERNETHY. It does not get it out of the Government's hands, because it still leaves some of them eligible to borrow directly from the REA.

Mr. MOTT. Well, that is true, sir. I am speaking about the bank with which this bill is concerned. The last time I testified before this committee I gave my own view of how this would happen, and I think that it is, probably, fairly accurate. If a man came in to borrow directly from the REA after this bank bill went into effect, he would have to—as they say in the law—show cause why he could not go to the bank. He would have to go to the REA Administrator and show that he was so poor that he could not possibly serve his area under the mandate of the original REA Act unless he was given the 2-percent loan.

Now, of course, there would be a lot of factors coming in to keep direct loans at a minimum. Not only would borrowers have to show a need for direct 2-percent loans, but the Appropriations Committee would have to be convinced and the Congress convinced every year that this need was there. And I would think that all of the pressures would be to reduce direct loans to a minimum and keep reducing them as people qualified to go to the bank. When the prospective borrower was told, "No, there is no money for you here in REA, you go to the bank," I would think that under the terms of this bill he would have to show cause why he should not pay the full bank rate before he could qualify for the intermediate rate. At least, this is my interpretation of what would happen.

And so, I think that our objective is to wean these people away from the 2-percent money by a device, a bill, a bank of this type. That is our objective, or one of our objectives.

Mr. TEAGUE of California. That is all. Thank you.

The CHAIRMAN. Are there any further questions?

Mr. Dole.

Mr. DOLE. There are many different telephone associations in the country. Mr. Lucier mentioned earlier that he was in accord with your statement.

Mr. MOTT. Mr. Lucier is a member of our REA Borrowers Committee, which under our policy directive have the duty of commenting on the issues before this committee.

Mr. DOLE. I make specific reference to amendment 18, about line 9 of the statement, where you indicate that you have no objection to the suggested amendment to eliminate the words, "a holding company." How do you view that amendment? Do you note any objection to it?

Mr. MOTT. We think that it is rather unfair to single out holding companies to which this restriction should be applied and to allow a company which is not a holding company to escape. I think that this amendment broadens the impact.

Mr. DOLE. This requires the approval of the bank. He indicated that.

Mr. MOTT. Yes, sir.

Mr. DOLE. It does not punish a holding company. It brings everybody under the tent.

Mr. MOTT. This is the amendment, I believe, Mr. Dole, which we think is technically deficient because yesterday it was proposed to substitute for the Administrator the words, "Secretary of Agriculture, and the Telephone Bank Board."

We have no objection to substituting the Secretary for the Administrator because they are alter egos anyway; nor do we have any objection to the telephone bank board acting on section 408 loans, but to put the amendment in the conjunctive, instead of the alternative, would have the telephone bank board operating on section 201 loans, which is no concern of theirs.

They are loans made under the original act. So it is our proposal in our statement, which does not violate the thought, as we understand it, of Mr. Bollinger and his associates, that this wording should be changed to read, "Without approval of the Secretary of Agriculture, with respect to section 201 loans, or the telephone bank board with respect to section 408 loans."

Mr. DOLE. That is as to No. 15. I was directing my attention to No. 16. They are all in the same section.

Mr. MOTT. We think it is a healthy change to eliminate the words "a holding company."

Mr. DOLE. I suggested yesterday, and I have no real basis for this suggestion, that perhaps an alternative would be on line 3, page 22, to simply eliminate the words, "without approval of the Administrator," so that it would read, "Notwithstanding the provision of the law, no borrower shall sell or dispose of his property until all indebtedness shall be paid."

Mr. MOTT. Mr. Dole, I heard your suggestion yesterday. I feel that you cannot avoid death and taxes, whether you are selling a company, such as Mr. Bollinger's or any other—you may remember yesterday he was asked why his company was sold—and his answer, really, was "death and taxes." You have death and taxes in REA companies, too. And if you were to circumscribe or to limit the class of persons to whom or the manner in which those people can sell their property, we might have put an end to all REA borrowings pretty quickly.

Perhaps, Mr. Wilbourn would like to comment on that. We were talking about this last night without really having it before us. He is president of the Allied Telephone Co., of Little Rock, Ark.

The CHAIRMAN. We will be glad to hear from you.

Mr. WILBOURN. I am in the group that is working on these amendments. If that clause were there, I would not want the money—I would not borrow the money. I would just get out of business, simply because it would restrict me in the operation of my business and, particularly, in my personal affairs as a stockholder in the company.

Mr. DOLE. I am not putting anything in—I am taking something out.

Mr. WILBOURN. I know. But you are taking out, or, by taking out, you are putting in. You are making it so an REA borrower, as I understood what you said yesterday, could not sell.

Mr. DOLE. The purchaser must pay the indebtedness first.

Mr. WILBOURN. He has to pay it off. If he has to pay it off, where is he going to get this money?

Mr. DOLE. From the bank, I presume.

Mr. WILBOURN. Do you think that a borrower would do this?

Mr. DOLE. I heard this morning that it does not make any difference—I am wondering about that.

Mr. WILBOURN. Now, then, you are back to the Public Service Commission. A borrower has to go to the Public Service Commission and ask them to support a loan at 6.5 percent, perhaps, which would automatically raise all the rates of that telephone company.

I think that this has no—well, I think that the statement that you made yesterday would kill the REA bank bill. I would not borrow the money. I would not borrow the money to sell my plant—I would not do that. And I borrowed it in good faith some 12 years ago.

Mr. DOLE. You would have no concern about this then?

Mr. WILBOURN. Yes, I would; I would. Because I do not want any restriction on my company.

The CHAIRMAN. Would you yield there?

Mr. DOLE. Yes.

The CHAIRMAN. I do not know a thing about the telephone business, Mr. Wilbourn, but I own a farm. The Federal land bank has a loan on it and has for quite some years. Would this not have the same effect on the telephone company that it had on my farm? I can sell that farm any day that I can find a buyer, and he can take up the Federal land bank note, carry it, or pay it off according to the terms—whatever he likes, but he does not have to dig up all the cash to do so.

Mr. WILBOURN. Sure.

The CHAIRMAN. I know that I can sell that place much more readily with that Federal bank loan on it than I could if a purchaser had to pay that Federal land bank note off. But he does not have to pay it off—anybody can buy that farm if it is all right with me. And then he has to pay whatever I am obligated to pay to the Federal land bank, but he does not have to pay it all in order to buy it.

Mr. WILBOURN. That is quite correct.

The CHAIRMAN. That is not exactly the situation here that Mr. Dole is proposing. And would not that cut your market down because it would affect the purchases?

Mr. DOLE. You have the 2-percent money.

Mr. MYERS. Are we financing for sale or for operation?

The CHAIRMAN. I want to answer that question.

Mr. MYERS. I am trying to get an answer.

The CHAIRMAN. You asked in your question, "Mr. Chairman." I will answer it.

Mr. MYERS. I have not asked a question yet.

The CHAIRMAN. You asked me a question now that I want to answer.

Mr. MYERS. You answer my question, then.

The CHAIRMAN. I want to answer it. We are making these loans to provide telephone service in the rural areas where service would not be provided if we did not make the loan. We are not making the loan to help the Bell Telephone Co. or the Continental, or to help United Telephone Co., or any other telephone company. We are not making loans to help them. We are making loans to provide telephone service. They are to provide these services. They are to provide the service that has not been provided before.

What difference does it make to the Government who holds the title to the property and the rate of interest? Their concern is that the service be provided and continued. If you make it impossible to sell property or if you reduce the value of the property at sale, I do not think that you would make any profit on it—it is less likely that the rural area will ever be served.

I do not think that it is our business to try to say who is going to operate this some 100 years from now or 10 years from now. Our business is to try to see where we can make these loans so that we will provide the service to the people who need the service. And we do not make any distinction in the REA law as to who gives that service, whether it is the Bell Telephone Co., because they have the same right, under the law—under the REA law—that these gentlemen have, if they will accept the obligation to provide the service—if they will, they can get the money at 2 percent. I do not see that it makes any difference in the world as to who provides the service.

We are not sitting here trying to reform the business world so that nobody can make a profit. I am for making a profit. I do not think that there should be any law against making a profit. But I am interested in getting these telephone companies into the rural areas. I do not care who owns the lines, so long as they do go on giving service, so long as the REA has this loan outstanding, that it continues the service, or it can foreclose the loan.

And what difference does it make? If you get it so that the REA cannot assure these people service, the minute that they pay off, that the REA loses any power of control to insure the continuance of adequate service, when, so long as they have the loan on there they can assure that, they can foreclose when the service goes down, when they do not have the kind of service that they have contracted for.

The REA can have a great deal to do with whether the United States or anyone else gives good service or not.

It seems to me that we probably have a stake in seeing that these holding companies retain REA loans.

Mr. MYERS. You can sell your farm with an FHA loan on it, you said.

The CHAIRMAN. I said a Federal loan bank.

Mr. MYERS. It makes no difference. If you have a 90-percent loan, it makes no difference, the borrower is not concerned—it is the financing itself. Why does the Federal loan bank, any more than anyone else, any more than the commercial banks down there, have that—you do not mean that.

The CHAIRMAN. I did not mean that it makes any difference between the Federal land bank or anybody else's loan, but the loan does not have to be paid off for me to sell my equity.

Mr. MYERS. Just the fact that there is a loan on it.

The CHAIRMAN. The fact a loan is there often helps sell it.

Mr. MYERS. Mr. Lucier said that it made no difference—they bought these companies, I believe this was his statement, because of the consolidation—it was beneficial to everyone. Why would it be beneficial, when they put two or three companies together and operated them—they separated the loans—they kept it separate, so that it was a cheaper operation.

Why can they not put the financing together and have one financing in every instance?

The CHAIRMAN. Just because it is difficult to refinance. As a banker, do you not find that you turn down a lot of security that somebody else has already financed?

Mr. MYERS. Yes, we certainly do. And the reason why, the Treasury of the United States is a big factor—we are talking about that—we are establishing a new bank, and we are trying to get one that will make good loans, I hope. This is a very costly thing. That is what we are talking about.

The CHAIRMAN. What you are talking about is not the bank. What you are talking about is the requirement that these people have to repay the REA loans, the administrative loans. You are not talking about the bank at all.

This conversation has been about administrative loans, and what you have been talking about is requiring the payment of the administrative loans. The bank is not going to be making 2-percent loans. You are talking about administrative loans, but you are not talking about bank loans. It has nothing to do with the bank at all.

You are talking about the basic principle of REA; at least, the telephone section as it has existed since 1949, and you are seeking to change the existing telephone law as it now exists, and you are not talking about having to pay off the bank loans; you are talking about paying the administrative loans.

The Administrator is the only one that makes any 2-percent loans. This bank does not make any. You are not talking about bank loans.

Mr. MYERS. I think that the discussion here has had a bank loan in it.

The CHAIRMAN. We are talking about two things. There is no such thing as 2-percent loans from this bank.

Mr. MYERS. No. I have made thousands of loans the last few years, and we make a real estate mortgage that you are speaking about, this is true. But on personal loans, personal collateral, chattel collateral, most of them are payable—

The CHAIRMAN. They are real estate loans. The lien that the REA has to take is on all of the property—it is the real property—it is recorded in the county records.

Mr. MYERS. It is chattel—not real estate.

The CHAIRMAN. It is real estate.

Mr. MYERS. Also, largely chattel.

The CHAIRMAN. They can own some chattel, but it is real estate.

Mr. MYERS. The statement—I will go back to my original statement—nobody could object to the fact that it would have to be paid

if they sold their property, on the chattel part of the property, or even the real property, and it is a capital even though they expect to pay it back. I would not take it. If I sold it—it might be to the same borrower, to renegotiate the loan—then that is it.

The CHAIRMAN. I think you have a perfect right to ask that, the bank. From the standpoint of the Government, in extending coverage, it is for the purpose of extending service, not for the purpose of giving the business to some particular telephone company.

Mr. MYERS. That is right; I agree with that.

Mr. DOLE. I do not want to disrupt service or kill the bill.

Mr. MOTT. I wonder if I could add something to the discussion in the conversation here? I have heard quite a few statements about the REA borrowers who allegedly borrow money solely for the purpose of increasing the value of their property, and then selling their property at a handsome profit.

I have only been associated with the telephone business about 31½ years, but I have observed that most of these companies, which are sold whether they are commercial companies with not a dime of REA money involved, or whether they are REA companies, are sold because of death, taxes, and family problems. You could give examples of both kinds, and Mr. Bollinger gave one yesterday—in the case of his own company.

It went because, primarily, two major stockholders desired, as I understood him, to sell because they were growing older and they wanted to liquidate their estate. That is the precise reason most companies are sold. I have heard the statement made that people borrow REA money just for the purpose of building up their telephone properties and then selling them at a handsome profit. When a prospective borrower goes into the REA he first has to convince the REA that he is borrowing this money to bring the kind of service envisaged to the people of a particular area, and then he has to go before a State regulatory body and make the same statement.

So everybody would really have to be a crystal ball gazer to say that people borrow money solely in order to improve their property and to sell it at a profit. Furthermore such motivation would bring borrowers pretty close to perjury.

Mr. DOLE. He might well do that. On the other hand, somebody can sell it off at a bigger profit. But if someone offers me a double value for my property, although I might have very good intentions beforehand, it would be very legal and proper to make that profit.

Mr. MOTT. This is equally true, Mr. Dole, of both types of companies.

Mr. DOLE. In the past year, maybe you two know—how many purchases have your companies made—do you have any idea?

Mr. MOTT. Well, they go on all of the time. I would hazard a rough guess that the number of independent companies in the last year have, perhaps, been reduced from 2,300 to 2,200.

Mr. DOLE. How many of those have been REA-financed—what percent?

Mr. MOTT. If you are talking on the basis of station count, a very, very small percentage of them, because you would have big acquisitions like the Hawaiian Telephone Co. by General, the Northern Ohio Telephone by General, the Jamestown by Mid-Continent.

Large acquisitions are so overwhelming by comparison that the number of stations of REA-financed acquisitions would be relatively very small. I would have to look at the record, but I could provide you with this information, Mr. Dole.

Mr. DOLE. We could have GAO make a review of the sales and make a report as to whether or not they feel that this is a proper use of the 2-percent money. That is my only point.

Thank you.

The CHAIRMAN. Mr. Belcher.

Mr. BELCHER. Let me see if I can get this clear in my mind.

Let us say that company "A," an independent telephone company, can qualify for 2-percent money for a loan. My understanding is that the reason that company "A" can qualify for the 2-percent money is because they are going to operate in the territory in which the 2-percent money is justified. Is that not correct?

Company "A" cannot get it because they have a lot of assets, or they have no assets. They get it because company "A" is going to serve a territory where 2-percent money is justified.

Mr. MOTT. Yes, sir.

Mr. BELCHER. Now, we will say that company "A" puts the loan through. Now, why is company "B" going to buy company "A"? Because of that loan, because company "B" could, if they decided to, qualify on the same basis, could they not—as company "A"? Company "B"—could buy company "A" before company "A" got the loan.

Mr. MOTT. Yes, sir.

Mr. BELCHER. They could go right ahead and they would have the same qualifications for the same territory—it would be in the same condition if 2-percent money was justifiable for company "A", it would be justifiable for company "B", would it not?

Mr. MOTT. Yes, sir.

Mr. BELCHER. Why would company "B" give a big premium to company "A," because they got the loan that company "B" could get after they bought it?

Mr. MOTT. I do not know that they would. I will let Mr. Lucier answer. I would not think that company "B" would be financially well managed and smart if they gave a big premium to company "A." I will let Mr. Lucier answer that, because he has had a lot more experience with it than I have had.

Mr. LUCIER. This is my point: the fact of the 2-percent money does not change the sales price.

Mr. BELCHER. And it does not change the conditions of the territory in which either company would serve, either before the sale or after the sale.

Mr. LUCIER. This is correct.

Mr. BELCHER. If the territory could qualify a company for 2-percent money, they could turn it over to company "B," and they could go right into the same spot and qualify for the 2-percent loan money, could they not?

Mr. LUCIER. Yes.

Mr. BELCHER. Whether it was Continental or General Motors.

Mr. LUCIER. Yes, sir.

Mr. BELCHER. And you do not take into consideration the assets of the company when you are getting the loan—you take into considera-

tion the conditions that exist in this territory that the company is going to serve, is that not right?

Mr. LUCIER. You are right, sir.

Mr. BELCHER. I am not going to vote for 2-percent money to give it as a charitable proposition. My reason for supporting the REA, either the electric or the telephone program, is to bring a service to the people who would otherwise not be serviced by private enterprise.

Mr. LUCIER. This is correct.

Mr. BELCHER. This is my only reason for doing it. As I say, I agree with the chairman, and we do not always agree [laughter] not even when we have hearings—but I do agree with him, that the materiality of the proposition is, do the people get the service—are they going to get it from company “B” or company “A”? If they are justified in getting it from company “A,” they are justified in getting it from company “B,” whether company “A” is almost broke or company “B” has a billion dollars. That is my feeling about it.

Mr. DOLE. Why not have one big company own all of them? It would not make any difference to you.

Mr. BELCHER. So far as the REA service is concerned, I would not care if one company owned every single one in the United States, if they would put service into a particular area.

Mr. DOLE. I asked one company about that.

Mr. BELCHER. Are you interested in the company, or are you interested in the people out there in getting service?

Mr. DOLE. I am interested in private companies, independent companies, staying in business.

Mr. BELCHER. I cannot understand why 2-percent loans would force the company to sell, or to prevent it from selling. They do not have to sell. There is no compulsion for a company that has a 2-percent loan to sell, is there?

Mr. DOLE. At a big profit, yes.

Mr. BELCHER. You are a better Houdini than I am, as to where the big profit is.

Mr. MYERS. If you will yield; one more thing.

Mr. BELCHER. Yes.

Mr. MYERS. This is the difference in the testimony of the witnesses, and this would be true ordinarily, but every time there is one more telephone at the top of Pikes Peak, you are increasing the telephone range of the people in New York City, and so you have expanded their calling distance. And you may have it all around a desert out here.

Mr. BELCHER. “A” company, when it sells, owns the telephones, do they not, and the telephones are in existence—they go to company “B.” It is then the same company.

Mr. MYERS. Then you have a blend, do you not?

Mr. BELCHER. If you go into a little area and get all of the lines, you can call New York City—you may call two or three different companies to get there, but my understanding is that the thing that makes a telephone business is because a telephone is in existence and not who owns the telephone.

Mr. MYERS. I think you can make that statement in general. I do not think that the intent of Mr. Bell or anyone else is to make the general observation. When they testified this morning, it was not a happenstance that they kept it separate—they did it for a benefit to

themselves. If they put them together, they would have to put all of their companies together, and most of them would have to reduce their individual telephone rates. They could operate a bigger company with a bigger profit individually by keeping themselves as a holding company, and if they put them both together, they could not charge as high rates.

Mr. BELCHER. All I know about telephones is that at one time, for about 4 months, I worked for the Southwestern Bell Telephone Co. as a student. I do know something about regulatory bodies. I know something about corporation commissions, so far as Oklahoma is concerned. I may be completely wrong.

Mr. MOTT. You are not.

Mr. BELCHER. I cannot understand why, in the far-out areas of the country, it makes any difference whether they get it from company "A" or from company "B." If the territory justifies the 2-percent money, it ought to justify it for company "A" as well as for company "B."

The CHAIRMAN. We still have to hear from Mr. Peterson.

We are very much obliged to you for your appearance here today, Admiral Mott.

Mr. MOTT. Thank you.

The CHAIRMAN. We will now be glad to hear from you, Mr. Peterson. Mr. Peterson is executive director and counsel of the National REA Telephone Association of Chisago City, Minn.

STATEMENT OF A. HAROLD PETERSON, EXECUTIVE DIRECTOR AND COUNSEL, NATIONAL REA TELEPHONE ASSOCIATION, CHISAGO CITY, MINN.

Mr. PETERSON. Thank you, Mr. Chairman and members of the committee. I know that the time is running short for the hearing this morning.

I merely want to reiterate one or two points which I hope that the committee will bear in mind, in considering the need for this type of bill.

These points have not been mentioned this morning, much of the time being taken up with these other matters that you have discussed and have asked questions about.

I do want to reiterate the primary reason why there is an REA telephone bank being discussed. It is simply this: 2 or 3 years ago, it became quite apparent that the amount of money that would be needed for the REA telephone loan program was going to greatly exceed that which had been appropriated in past years.

To give you some idea of what that relationship is, in terms of what has happened over the last several years, I just want to recite a few brief figures.

In 1963, the amount of unapproved loan applications on hand in the REA at the end of the fiscal year was \$58.3 million. In 1964, this amount had increased to \$84.7 million. In 1965, it was \$122.2 million. In 1966, it was \$197.1 million. And on June 30, at the end of this fiscal year 1967, the fiscal year just ended, the total amount of unapproved telephone loan applications on hand in the REA amounted to \$251,971,000.

During the last 3 years the amount of the appropriations for this program have been increased. For instance, in 1965, it was \$70 million; in 1966, it was \$97 million; and in the year just ended, it was \$117 million.

The point that I am making is that in spite of the increased annual appropriations, the amount of unapproved loan applications on hand at the end of the fiscal year is being compounded as each year passes with nothing being done about it, except the increases in the appropriations process, which I have just detailed.

What do you do about a situation like this?

Two years ago this month, I had a conference with the Director of the Bureau of the Budget and outlined these same facts, as they existed at that time. He said to me, "Mr. Peterson, I appreciate the problem that faces the telephone borrowers, but," he said, "one thing that you ought to keep in mind is this, that the Federal budget process is now reaching the point where we simply cannot meet this kind of total need purely out of annual appropriations, and I think that your people ought to investigate the possibility of supplemental financing of another nature."

Gentlemen of the committee, this is precisely the reason why H.R. 12066 is now before you.

The need for this money to meet the problem of capital financing for REA telephone borrowers is very grave. The amount of money that will be needed in the next 16 years of this program will be double that of the past 16 years.

This is in consonance with what is happening in the entire industry. Let us reflect just for a moment on the financial ability of these REA companies. In spite of the discussion which has transpired here this morning in terms of holding companies, stocks, buying and selling, the stark fact remains that today, considering all of the REA telephone borrowers there is only 2 percent of them who have a net worth as a percentage of total assets of over 40 percent.

What chance have they ever got to go to a bank or any kind of lending institution and getting money? They are facing the same kind of financial vacuum that existed in 1949 when the REA telephone amendment was passed.

I should like to recite one more figure: 37½ percent of all of the REA telephone borrower companies have less than 1,000 subscribers. In terms of density—and I think that I presented these figures to the committee before—the Bell System enjoys over 40 subscribers per mile of line.

The independent industry, including General, United, Continental, and all of the rest of them, as well as the REA telephone borrowers, enjoy a density of 16 customers per mile. But when we get down to the REA telephone companies, we get a figure of 3.7 subscribers per mile of line. This is precisely the reason why this program came into being in the first place, because it was in these thin areas that the Congress of the United States decided that telephone service ought to be made available, and they have made it possible with this program.

In terms of miles of line, the Bell System enjoys revenues of over \$10,000 per mile of line. The independent industry, as a whole, enjoys approximately \$2,500 per mile of line in revenues. And the REA borrowers, less than \$500 per mile of line in revenue.

Gentlemen, in considering how to meet the needs, we would merely like to reiterate once more that in discussing H.R. 12066 in executive session, we respectfully ask that you keep in mind three basic objectives:

No. 1. There ought to be adequate debt capital to meet the needs at usable interest rates.

No. 2. There ought to be built-in incentives in the bill, so that eventually the bank will come into the ownership of the companies themselves.

And, lastly, there ought to be sufficient latitude to permit the telephone companies to meet their industry responsibilities as the years go by.

I think with that I shall close my statement; I shall be very happy to answer any questions that you may have.

The CHAIRMAN. Thank you, Mr. Peterson.

Are there any questions of Mr. Peterson?

Mr. Myers.

Mr. MYERS. You meant to say that the companies would own the bank, rather than the bank own the companies?

Mr. PETERSON. That is right.

Mr. MYERS. I believe that I understood you to say that the banks should own the companies.

Mr. PETERSON. No; I did not mean that.

Mr. MYERS. Thank you. That is all.

The CHAIRMAN. Mr. Wampler.

Mr. WAMPLER. As I read the bill, in trying to interpret it, the criteria that the bank board will use in deciding who would be eligible for the 2-percent loans and who would be eligible for the going rate of interest loans, is not very clearly spelled out, is it?

Mr. PETERSON. That is true.

Mr. WAMPLER. Let me ask you this hypothetical question: Assuming that company "A" has a 2-percent REA loan, and they decide to sell to company "B," and company "A" has grown—circumstances have changed, it is now able to pay more than 2 percent for money, what would be wrong with requiring, upon the sale of all of the REA financed companies, that the loan then be immediately due and payable, and to make them reapply, and let them pay the going rate of interest?

Mr. PETERSON. In answering your question, I would agree with the statement made here this morning, that if such an amendment was put into the bill I think that it would restrict the future loans, just as Mr. Wilbourn has indicated. I would agree with his statement.

Mr. WAMPLER. What would limit them?

Mr. PETERSON. I think that it would impair the sale of the company at some date, for whatever reason, contemplation of death being the predominant reason in a family owned company.

Mr. WAMPLER. Of course, if you are able to pay the prevailing rate of interest, you ought to be paying it. I understand that is one of the objectives behind the bill, is it not?

Mr. PETERSON. Yes.

Mr. WAMPLER. Would this not make available more 2-percent money for the companies that need it, where it is not available? It would require some to pay off and go to the bank and pay the prevailing rate of interest.

Mr. PETERSON. Well, maybe I misunderstood your question. If an amendment were put in this bill which would provide that a company, if sold, that the entire debt must be repaid?

Mr. WAMPLER. Yes. They can go to the bank and pay the prevailing rate of interest, or receive a continuation of the 2-percent loan if they cannot afford the prevailing rate of interest.

Mr. PETERSON. If you have such an amendment, again, I reiterate what other witnesses have already indicated, that it would, I think, necessarily restrict future loans. I do not think that they would be coming in for future loans.

Mr. WAMPLER. If they are able to pay the prevailing rate, they should not be coming in for 2-percent loans, should they?

Mr. PETERSON. Yes; that is true.

Mr. WAMPLER. Thank you.

The CHAIRMAN. Mr. Dole.

Mr. DOLE. You are not suggesting that all telephone companies would be eligible for 2-percent money if we passed the bank bill?

Mr. PETERSON. I would think that any company, regardless of size, would be eligible for 2-percent money if they agreed to go into an unserved territory and provide telephone service not presently there, which was the case in 1949, and which provided that the Bell System or anyone else could go into the territories and obtain the 2-percent money to do that.

They did not choose to do so, however. To me, it is a plain question of economics. It costs money to bring the service out there, when you have the kind of density in those REA areas of 3.7, compared to over 40 for the Bell System. It is a question of what the subscriber will ultimately have to pay for his service and what you pay for interest rates affects the subscriber.

The CHAIRMAN. Will you yield?

Mr. DOLE. Yes.

The CHAIRMAN. Under the present law, the Bell Telephone Co. has the same right to borrow 2-percent money that the smallest telephone company in the United States has. I think that they are good loans. I am for them. We did not pass that law for the purpose of helping the Bell System, nor helping Mr. Bain's system. We passed that law for the purpose of helping the rural people to get telephone service, regardless of who brought it to them.

Mr. PETERSON. That is right.

The CHAIRMAN. I do not think that we ought to say that nobody should make a profit out of the telephone business or any other business. That you are evil, or some such thing, if you make a profit. I do not think that. I hope that everyone does make a profit in business. But I am interested in seeing these people get telephone service.

And if you make it so that the man who serves the rural areas cannot sell out readily, there will be less incentive to serve the thin areas. And it is getting thinner all of the time in some areas.

Mr. MYERS. I would like to make one statement. I am very sure that I am very much in agreement with that. I voted for it the last time, and I hope to vote for it again. What most of our concern is about, and the thing that interests me, and I have asked this a half a dozen times, and nobody has told me? Mr. Poage, and several others, have said that they did not want to go back into the rural areas to build these telephone services.

Mr. PETERSON. Yes, that is correct.

Mr. MYERS. Why should they be so interested to purchase them, now? When they are the same areas—why are they interested in buying the companies when we get them financed?

Mr. O'NEAL. It may be that some of them have grown. For instance, in connection with the telephone companies mentioned before in my State, I do not know how large these companies were at the time that they got the 2-percent money, but in one instance, it is a town of about 16,000 people now.

Mr. MYERS. Okay, then. It is a new area, is it not? And we have voted several times in this committee to get increased yearly reviews of appropriations. That is all we are suggesting. I do not know how I will vote on this. I have not made up my mind.

Mr. O'NEAL. If you will yield further, I think that we are confusing the liquidity of the company with the need and the density of the community in population. If we are going to have any restrictions, I think that they should be directed at the needs and the density of the community, rather than to the liquidity of the companies.

Mr. MYERS. This is a new area. I am not sure whether this is right or not. That is why we are having hearings to decide whether it is the right way. And a review would not hurt anything. Even after the original law was passed, for some reason, as has been said here, the company that did not originally build there, has a new look in the area—they are interested now. They may be interested in paying a better rate.

Who is paying for this money? The subscribers are paying for it in the form of taxes.

Mr. O'NEAL. I am sure that the telephone company in Statesboro was eligible, for still they have loans.

Mr. MYERS. They should go back to the bank.

Mr. O'NEAL. They may be owned by a mixed company.

Mr. MYERS. They would still be eligible to go into the bank.

Mr. O'NEAL. I do not know that they would. I think they have grown out of it.

Mr. MYERS. I am not saying that this is right. This is a possibility.

Mr. DOLE. Would you yield?

Mr. PETERSON. I was going to make one additional statement concerning the question, "Why are the other companies so anxious to buy?" I am not so sure that it is a case of the companies being anxious to buy, as much as it is that certain conditions, which are inherent in the commercial companies in the REA program have changed. Admiral Mott alluded to them. Many of these companies are owned by families. Many of these companies were started at the turn of the century.

Mr. Baine here, for instance, is serving down in Texas. He is the third generation operating a telephone company started by his grandfather. There does come a time when the family considerations come into play such as estate planning, and I think this is one of the conditions which is precipitating what is happening in the selling of companies—not the question of somebody trying to gobble them up.

Mr. MYERS. As Mr. Poage and Mr. Belcher both said, they would both be eligible—they would be eligible for REA loans.

Mr. DOLE. Would you yield?

Mr. MYERS. Yes.

Mr. DOLE. As I understand it, everybody in America seems eligible for 2-percent money, with this bill. If this is so, I do not think the bill would be a good thing.

Mr. MYERS. I have nothing further.

Thank you.

The CHAIRMAN. If there are no further questions, we are very much obliged to you, Mr. Peterson.

(The following letters, telegram, and statement were also submitted to the committee:)

GULF STATES-UNITED TELEPHONE CO.,

Tyler, Tex., August 11, 1967.

HON. W. R. POAGE,
U.S. House of Representatives,
Washington, D.C.

DEAR CONGRESSMAN POAGE: We certainly appreciate receiving your letter of August 8, 1967, in response to our wire in which we expressed opposition to the proposed "rural telephone bank."

Your courtesy in inviting us to express our reasons for opposing this legislation is also sincerely appreciated. We welcome the opportunity to give you our reasons which are basically as follows:

The REA telephone loan program has been abused. The 2% interest rate intended as a subsidy to insure small telephone companies capital to provide efficient telephone service continues in effect. Yet, these small companies that have borrowed large sums under the present loan program have been acquired by telephone holding companies. As a matter of fact, additional loans have been made to such small companies even after their acquisition by a holding company which has ready access to conventional capital markets. Any supplemental or successor telephone loan program should insure against similar uses.

Undoubtedly there are a few situations which still exist where a small rural telephone company will need help in the form of a government subsidy to assist them in providing modern, efficient telephone service. In these cases, the help should be readily available. We believe that the REA telephone loan program, in its present form, is adequate to provide this needed help. There is a serious question about the interest on such loans to small telephone companies. This rate of interest should be at least equal to the cost of money to the government.

REA telephone loans or "rural telephone bank loans" should not be made available to telephone companies which have access to conventional capital markets for the funds they need, either individually or through a corporate parent company. Eligibility for either initial or supplemental loans, whether from the REA or a rural telephone bank, should be made only after a showing that funds from conventional sources cannot be obtained on reasonable terms.

Further, when a small telephone company which holds an outstanding REA loan is acquired by a larger company or by a telephone holding company, the REA loan agreement and mortgage indenture should be properly amended as necessary to make it possible and practicable to meet any requirements for additional capital through the insurance of conventional forms of equity or debt security.

These basic facts are respectfully submitted for the committee's consideration.

Sincerely,

ROLLA L. JOHNSON, *President.*

LINCOLN, NEBR., *August 14, 1967.*

HON. W. R. POAGE,
Chairman of House Agriculture Committee,
U.S. House of Representatives,
Washington, D.C.:

We strongly object to H.R. 12066, the telephone bank bill, and to any similar-purpose legislation. Rural telephone, as I am sure you realize, has made substantial progress in recent years. Any remaining meritorious situations can adequately be dealt with under the same REA program, which made it possible for our organization, through subsidiaries, to provide service in certain uneconomic and sparsely settled areas in Virginia and Florida.

Without mitigating the foregoing, a few of our more important objections to the provisions of H.R. 12066 are:

The authority of the Banks' Board of Directors is much too far reaching—(1) as to the extent of its operations; (2) as to the amounts and purposes of loans; (3) as to the aggregate amount of loans that can be authorized during any one fiscal year; (4) as to the policies and standards imposed upon borrowers which ought to be consistent with the requirements of the regulatory authority having jurisdiction within the particular State; and (5) as to the costs of operating the bank, which ought to be at least self-sustaining.

As I am sure you know even better than we do—our country and each of us as taxpayers now are facing tremendous and constantly increasing costs at home and abroad. All facts considered, we regard it as vital that if a telephone bank bill is to be enacted, then it should provide for the interest rates charged on loans made thereunder to equal not less than the Government's then current average cost of money; and should not be discriminatory against comparable size companies which solve their own financing problems.

We respectfully urge that H.R. 12066 should not be reported out by your committee. If notwithstanding our urging, this bill is to be reported out, then in the interest of the public generally and not just the temporary beneficiaries thereof, we plead that it should first be amended to specifically include provisions for, or for the Congress to retain, reasonable and effective controls over each of the matters referred to herein.

Respectfully,

TORAL DUCKETT,
Executive Vice President,
Central Telephone Co. and Affiliates.

CITIZENS TELEPHONE CO.,
Brevard, N.C., August 22, 1967.

HON. W. R. POAGE,
House Agriculture Committee,
House Office Building,
Washington, D.C.

DEAR SIR: The House Agriculture Committee has under consideration a bill to establish an REA Telephone Bank (HR 12066) which we feel is vital to the continued existence of the small independent telephone companies.

The General Telephone Company, United Utilities and several of the large holding companies have voiced opposition to this bill for the reason, I believe, that the Bank will make funds available and stymie these companies in their program of gobbling up the small Independents who are unable to obtain adequate financing from private sources. In addition to their buying up the small Independents, these giants have acquired manufacturers and suppliers of telephone equipment and at present the Stromberg-Carlson Division of General Dynamics is the only American manufacturer of dial switching equipment which they have not yet been able to acquire. If they are allowed to continue in this practice it will make the small Independents more vulnerable to acquisition by the "big" of the industry.

We strongly urge you to lend your support and influence in getting HR 12066 passed by the House and Senate at an early date.

We further request that you take a look at the practice of the large Independents acquiring manufacturers and suppliers of equipment to see if the anti-trust laws are being violated.

We will appreciate any help you can give us in this manner.

Very truly yours,

CITIZENS TELEPHONE CO.,
C. W. PICKELSIMER, JR.

STATEMENT OF NATIONAL ASSOCIATION OF MANUFACTURERS

This statement is filed on behalf of the National Association of Manufacturers, a voluntary association of business enterprises, large and small, located in every State.

We appreciate this opportunity to express our views on H.R. 12066, which would establish a new government corporation to be known as the Rural Telephone Bank.

On April 4, 1967, we filed with the Committee on Agriculture a statement on H.R. 1400, a bill to establish both a Rural Electric Bank and a Rural Telephone Bank. That bill did not reach the House floor. Although our previous statement dealt only with the Rural Electric Bank provisions of H.R. 1400, we wish to

incorporate it by reference into this record because we believe the reasons why a Rural Electric Bank is unnecessary and undesirable are equally applicable to the proposed Rural Telephone Bank.

We wish to state again our policy position on "Federal Business-Type Activities" as it deals with Federal lending activities:

"Substantive legislation for Federal business-type activities involving credit should provide that interest rates and maturities be based on market realities, except where a subsidy is expressly specified and measured. All such Federal lending programs, including those which are self-supporting, should be reviewed periodically with a view to discontinuing the activities when possible. Any lending operations caused by circumstances which are no longer present should be discontinued as soon as possible without causing sudden or undue hardship to those sectors of the economy which have become dependent on this form of governmental support. Necessary lending operations of the government should be so conducted as to avoid confusion of the activity and its purposes with political motives and purposes."

We believe that H.R. 12066 does not incorporate any effective steps in the direction of terminating Federal lending in the telephone field, but moves in the direction of further massive Federal involvement by institutionalizing the activity.

The bill would authorize the appropriation of \$30 million per year for a total of \$300 million. The Rural Telephone Bank corporation would issue Class A stock to the United States in exchange for this money. Class A stock would be entitled to a return, payable from income, at the rate of 2% per year.

The bill provides that "such Class A stock shall be redeemed and retired by the telephone bank as soon as practicable after June 30, 1982, but not to the extent that the Telephone Bank Board determines that such retirement will impair the operations of the telephone bank; . . ." Thus, elimination of Federal involvement would not even begin until June 30, 1982. In the meantime, the present Rural Electrification Administration program of 2% loans to rural telephone systems would continue.

In summary, the bill would authorize the commitment of \$300 million of government funds at a time when fiscal restraint is imperative. It would expand rather than constrict Federal activities in this field, and would postpone lessening of Federal involvement to a date far in the future.

For these reasons, we strongly urge the Committee not to report H.R. 12066.

The CHAIRMAN. That completes our witness list. Is there anybody else here who wants to be heard?

If not, that will close the public hearings.

The committee will meet in executive session the 19th of September.

(Whereupon, at 12:10 p.m., the committee adjourned, to meet in executive session on September 19, 1967.)



incorporate it by reference into this record because we believe the reasons why a Rural Telephone Bank is unnecessary and undesirable are equally applicable to the proposed Rural Telephone Bank.

We wish to state again our policy position on Federal business-type activities:

As it deals with Federal lending activities involving credit, substantial legislation for Federal business-type activities involving credit should provide that interest rates and maturities be based on market realities, even where a subsidy is expressly specified and measured. All such Federal lending programs, including those which are self-supporting, should be reviewed periodically with a view to discontinuing the activities where possible. Any Federal operation caused by circumstances which are no longer present should be discontinued as soon as possible without causing undue hardship to those sectors of the economy which have become dependent on this form of Government support. Necessary lending operations of the Government should be so conducted as to avoid confusion of the activity and its purposes with political motives and purposes.

We believe that H.R. 1206 does not incorporate any effective steps in the direction of terminating Federal lending in the telephone field, but moves in the direction of further massive Federal investment by institutionalizing the activity.

The bill would authorize the appropriation of \$30 million per year for a total of \$300 million. The Rural Telephone Bank corporation would issue Class A stock to the United States in exchange for this money. Class A stock would be entitled to a return payable from income at the rate of 2% per year.

The bill provides that such Class A stock shall be redeemed and retired by the telephone bank as soon as practicable after June 30, 1957, but not to the extent that the Telephone Bank Board determines that such retirement will impair the operations of the telephone bank. That termination of Federal investment would not even begin until June 30, 1957. In the meantime, the present Rural Electrification Administration program of 2% loans to rural telephone systems will continue.

In summary, the bill would authorize the commitment of \$300 billion of Government funds at a time when Federal activity is decreasing. It would expand rather than curtail Federal activity in this field and would postpone termination of Federal investment to a date far in the future.

For these reasons, we strongly urge the Committee not to report H.R. 1206.

The Chairman: That completes our witness list. Is there anybody else here who wants to be heard?

If not, that will close the public hearings.

The committee will meet in executive session the 19th of September. (Whereupon, at 12:10 p.m., the committee adjourned, to meet in executive session on September 19, 1957.)



