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91-98 PENN CENTRAL TRANSPORTATION COMPANY:
ADEQUACY OF INVESTOR PROTECTION

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HEARING

BEFORE THE

SPECIAL SUBCOMMITTEE ON INVESTIGATIONS

OF THE

COMMITTEE ON

INTERSTATE AND FOREIGN COMMERCE

HOUSE OF REPRESENTATIVES

NINETY-FIRST CONGRESS

SECOND SESSION

SEPTEMBER 24, 1970

Serial No. 91-98

Printed for the use of the
Committee on Interstate and Foreign Commerce

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PENN CENTRAL TRANSPORTATION CO.: ADEQUACY OF INVESTOR PROTECTION

THURSDAY, SEPTEMBER 24, 1970

HOUSE OF REPRESENTATIVES,
SPECIAL SUBCOMMITTEE ON INVESTIGATIONS,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2322, Rayburn House Office Building, Hon. Torbert H. Macdonald presiding (Hon. Harley O. Staggers, chairman).

Mr. MACDONALD. The hearing will come to order.

The purpose of today's hearing is to consider certain important aspects of the recent financial collapse of the Penn Central Transportation Co. The difficulties which the railroad has experienced have direct bearing on the jurisdictional and legislative concerns of the House Commerce Committee. The hearing today is not intended to be an exhaustive one; there are aspects of this matter which cannot be adequately taken up or even mentioned within the scope of today's hearing.

Before proceeding to the questioning of Commissioner Smith and Vice Chairman Hardin, I believe it would be in order to briefly set forth the legislative purpose behind this hearing.

Rule 11 of the House of Representatives charges the Commerce Committee with responsibility for legislation having to do with a wide variety of subject matter, including the following: "Interstate and foreign commerce generally" (rule 11(a)); "Regulation of interstate and foreign transportation, except transportation by water not subject to the jurisdiction of the Interstate Commerce Commission" (rule 11(h)); "Securities and Exchanges" (rule 11(j)).

The subject matter of today's hearing will fall under all of these topics.

Section 136 of the Legislative Reorganization Act of 1946 directs the committee to exercise continuous watchfulness over the execution by the administrative agencies of any laws within its jurisdiction. The witnesses today are the chairmen of two of the independent regulatory agencies whose activities fall within the jurisdictional responsibilities of the Commerce Committee.

House Resolution 116 of the 91st Congress authorizes this subcommittee to conduct investigations and studies relating to subject matter within the jurisdiction of the parent committee. In this connection, we are concerned with both the adequacy of existing laws themselves and of their administration by the agencies to whom the Congress has delegated regulatory authority.

Without objection, I direct that rule 11 of the House of Representatives, section 136 of the Reorganization Act of 1946, and House Resolution 116 of the 91st Congress, be inserted into the record at this point. I do this so that the jurisdictional concern and legislative purpose of this subcommittee proceeding may be clear.

(The documents referred to follow:)

RULES OF THE HOUSE OF REPRESENTATIVES

RULE XI. POWERS AND DUTIES OF COMMITTEES

All proposed legislation, messages, petitions, memorials, and other matters relating to the subject listed under the standing committees named below shall be referred to such committees, respectively:

- * * * * *
11. Committee on Interstate and Foreign Commerce.
- (a) Interstate and foreign commerce generally.
 - (b) Civil aeronautics.
 - (c) Inland waterways.
 - (d) Interstate oil compacts and petroleum and natural gas, except on the public lands.
 - (e) Public health and quarantine.
 - (f) Railroad labor and railroad retirement and unemployment, except revenue measures relating thereto.
 - (g) Regulation of interstate and foreign communications.
 - (h) Regulation of interstate and foreign transportation, except transportation by water not subject to the jurisdiction of the Interstate Commerce Commission.
 - (i) Regulation of interstate transmission of power, except the installation of connections between Government water-power projects.
 - (j) Securities and exchanges.
 - (k) Weather Bureau.
- * * * * *

SECTION 136 OF THE LEGISLATIVE REORGANIZATION ACT OF 1946, 60 STAT. 812

LEGISLATIVE OVERSIGHT BY STANDING COMMITTEES

SEC. 136. To assist the Congress in appraising the administration of the laws and in developing such amendments or related legislation as it may deem necessary, each standing committee of the Senate and the House of Representatives shall exercise continuous watchfulness of the execution by the administrative agencies concerned of any laws, the subject matter of which is within the jurisdiction of such committee; and, for that purpose, shall study all pertinent reports and data submitted to the Congress by the agencies in the executive branch of the Government.

HOUSE RESOLUTION 116, 91ST CONGRESS, AGREED TO FEBRUARY 5, 1969

IN THE HOUSE OF REPRESENTATIVES

January 9, 1969

Mr. Staggers submitted the following resolution; which was referred to the Committee on Rules

January 23, 1969

Referred to the House Calendar and ordered to be printed

February 5, 1969

Considered and agreed to

RESOLUTION

Resolved, That effective January 3, 1969, the Committee on Interstate and Foreign Commerce may make investigations and studies into matters within its jurisdiction including the following:

(1) Policies with respect to competition among the various modes of transportation, whether rail, air, motor, water, or pipeline; measures for increased safety; ownership and control of transportation facilities; adequacy of the national transportation system for defense and the needs of an expanding economy.

(2) Policies with respect to the promotion of the development of civil aviation; measures for increased safety; restrictions which impede the free flow of air commerce; promotion of travel and tourism; routes, rates, accounts, and subsidy payments; airport construction, hazards of adjacency to airports, and condemnation of airspace, aircraft, and airline liability; aircraft research and development, and market for American aircraft; air navigational aids and traffic control;

(3) Allocation of radio spectrum; community antenna television; pay television; satellite communications; ownership, control, and operations of communications and related facilities; policies with respect to competition among various modes of communication, including voice and record communications and data processing; policies with respect to governmental communications systems; coordination of communication policies both domestic and foreign; impact of foreign operations, international agreements, and international organizations on domestic and foreign communications; technical developments in the communications field;

(4) Adequacy of the protection to investors afforded by the disclosure and regulatory provisions of the various securities Acts;

(5) Adequacy of petroleum, natural gas, and electric energy resources for defense and the needs for an expanding economy; adequacy, promotion, regulation, and safety of the facilities for extraction or generation, transmission, and distribution of such resources; development of synthetic liquid fuel processes; regulation of security issues of and control of natural gas pipeline companies;

(6) Advertising, fair competition, packaging, and labeling;

(7) Research in weather, including air pollution and smog, and artificially induced weather;

(8) Effects of inflation upon benefits provided under railroad retirement and railroad unemployment programs; and inequities in provisions of statutes relating thereto, with comparison of benefits under the social security system;

(9) Adequacy of medical facilities, medical personnel, and medical teaching and training facilities; research into human diseases; provisions for medical care; efficient and effective quarantine; protection to users against incorrectly labeled and deleterious foods, drugs, cosmetics, and devices; and other matters relating to public health; protection of the public against abuse of barbiturates, amphetamines, and other dangerous drugs;

(10) The War Claims Act and the Trading With the Enemy Act, including the provisions relating to direct foreign investment;

(11) Current and prospective consumption of newsprint and other papers used in the printing of newspapers, magazines, or such other publications as are admitted to second-class mailing privileges; current and prospective production and supply of such papers, factors affecting such supply, and possibilities of additional production through the use of alternative source materials;

(12) Traffic accidents on the streets and highways of the United States; factors responsible for such accidents, the resulting deaths, personal injuries, and compensation for damages, economic losses, and measures for increased motor vehicle safety; and

(13) The administration of provisions of law relating to the above subjects and all others which are in the jurisdiction of such committee;

Provided, That the committee shall not undertake any investigation of any subject which is being investigated by any other committee of the House.

For the purposes of such investigations and studies the committee, or any subcommittee thereof, may sit and act during the present Congress at such times and places within or outside the United States, whether the House has recessed or has adjourned, to hold such hearings, and to require, by subpoena or otherwise, the attendance and testimony of such witnesses and the production of such books, records, correspondence, memorandums, papers, and documents, as it deems necessary. Subpenas may be issued under the signature of the chairman

of the committee or any member of the committee designated by him, and may be served by any person designated by such chairman or member.

The committee may report to the House at any time during the present Congress the results of any investigation or study made under authority of this resolution, together with such recommendations as it deems appropriate. Any such report, shall be filed with the Clerk of the House if the House is not in session.

Notwithstanding section 1754 of title 22, United States Code, or any other provision of law, local currencies owned by the United States shall be made available to the Committee on Interstate and Foreign Commerce of the House of Representatives and employees engaged in carrying out their official duties under section 190d of title 2, United States Code: *Provided*, That (1) no member or employee of said committee shall receive or expend local currencies for subsistence in any country at a rate in excess of the maximum per diem rate set forth in section 502 (b) of the Mutual Security Act of 1954, as amended by Public Law 88-633, approved October 7, 1964; (2) no member or employee of said committee shall receive or expend an amount for transportation in excess of actual transportation costs (3) no appropriated funds shall be expended for the purpose of defraying expenses of members of said committee or its employees in any country where counterpart funds are available for this purpose.

Each member or employee of said committee shall make to the chairman of said committee an itemized report showing the number of days visited in each country whose local currencies were spent, the amount of per diem furnished, and the cost of transportation if furnished by public carrier, or if such transportation is furnished by an agency of the United States Government, the cost of such transportation, and the identification of the agency. All such individual reports shall be filed by the chairman with the Committee on House Administration and shall be open to public inspection.

Mr. MACDONALD. The adequacy of present law and its administration has been severely tested in the Penn Central collapse. Today we initiate the first of a series of hearings to explore how well they have met that test.

Few, if any, events in our recent history have had as significant and alarming an impact upon our national economy as the June 22, 1970, announcement of the bankruptcy of the Penn Central Railroad. After decades of declining standards in railroad service to the traveling public—a decline which has been justified in the name of sound railroad economics—railroad operators appeared, in early June of this year, hat in hand, requesting of the Congress nearly a billion dollars of taxpayers' money to rescue them from a liquidity crisis. While the reasons for this crisis are still being investigated, serious doubts as to the wisdom of the financial and managerial policies of the railroads are certainly justified at this point.

When the plea for public money was rejected, the railroad management sought relief under the national bankruptcy laws. It has been reported that certain officials of the railroad have blamed their recent difficulties on "overregulation of government on all levels." I suggest that the record to be developed by this subcommittee during the course of these hearings may demonstrate that the railroad industry as a whole has suffered from too little, not too much, governmental regulation.

Long before the merger of the New York Central and the Pennsylvania Railroads became a fact, management was determined to create a conglomerate holding company with diversified interests. The final step in the creation of the conglomerate was the establishment of the Penn Central Co., as the parent holding company, one of whose interests included holding the securities of the Penn Central Transportation Co. The transportation company, which was the operating

railroad, had itself been for some time a conglomerate through its subsidiary, the Pennsylvania Co., which had substantial holdings in nonrail activities. This final step was accomplished on October 1, 1969. Less than 9 months later, the merged rail system was plummeted into bankruptcy. Bankruptcy, however, was not the fate of the parent holding company nor of the highly profitable investment company subsidiary of the railroad. The financial acumen of management, while it did not protect the railroad from bankruptcy, was able to insulate those other assets carefully beyond the reach of a government asked only to rescue the railroad, not the highly profitable nonrailroad properties.

The transfer of railroad ownership to holding companies formed to engage in diversified activities is a relatively new but accelerating practice. Railroad officials have contended that corporate diversification is the panacea which will relieve their financial woes and improve service through the greater capital resources available to the parent holding company. In fact, just the converse has seemed to be true. Financial difficulties of the railroad components have increased, the credit of the railroad components has been pledged to further non-railroad activities and customer service and facilities have deteriorated at an accelerated rate.

Holding companies have been utilized to reduce the regulatory controls of the Interstate Commerce Commission. Nonrailroad operations have been withdrawn from under the jurisdictional controls of the Commission while railroad operations, which initially financed the diversification programs of the holding companies, have been orphaned. Any bargaining powers the railroad components might once have possessed have been submerged beneath a morass of intercompany transactions intended to permit excessive investment returns by the conglomerate parents.

I am mindful of the lessons taught at great public expense 40 years ago when numerous electric and gas utilities were combined into vast public utility holding companies. At that time, the Congress was required to halt the very same abuses we are now witnessing in the conglomerate holding companies which, through subsidiaries, operate public carriers. The remedy to the abuses at that time was the Public Utility Holding Company Act of 1935. That act required the physical integration and financial simplification of utility holding company systems. It limited the operations of each system to a single integrated operating system, whose assets were capable of being physically interconnected and economically run as a single coordinated system in a single area. It was designed to preserve the advantages of localized management, efficient operation, and effectiveness of regulation. Whether this could form a reasonable basis for a solution to some of the more urgent problems now faced by the railroads is a question calling for most careful consideration.

This raises the question of what have the regulatory agencies been doing to protect the public interest.

I was somewhat surprised on reviewing the testimony offered before our committee on June 24, 1970, by high-ranking officials of the Interstate Commerce Commission that they were taken by surprise at the bankruptcy of the Penn Central Railroad. Adequate auditing and financial reporting standards are fundamental tools of any regulatory

body. Without timely and complete information about profitability and accurate projections of future earnings or losses, any ratemaking functions must be a travesty upon the regulated carrier and upon the traveling public. Despite the congressional mandate 83 years ago that the Commission embark on a program that would establish an efficient and economically viable rail system in this country, the rail system in this Nation is neither efficient nor economically viable. Therefore, we must question whether the Commission has lost touch with the economic realities of railroading today, and whether the tools which the Congress provided are being used.

On July 1, 1970, the Chairman of the Securities and Exchange Commission was asked to look into the trading in all the securities of the Penn Central Co. and its affiliates and to report back to the chairman of this subcommittee. In cooperation with the special subcommittee, the SEC solicited more than 250 brokers reporting trading activities in Penn Central stock and made the answers of the brokers available to this subcommittee.

Merely on the basis of the material we have received, we feel there is strong evidence of substantial violations of the Federal securities laws by insiders of Penn Central. This would include not only the obvious possibility of large-scale sales of Penn Central stock by insiders before the public was informed of the true financial situation of the company, but also a failure to file reports with the regulatory agencies concerned when the law clearly requires those reports. It would include misrepresentations to the public through incomplete information in prospectuses filed with the ICC. I would like to make it clear that neither the subcommittee nor its staff has taken the position that violations did in fact occur. We merely wonder and state that available evidence strongly indicates that violations may have occurred. The possibility remains that when the record is fully developed, the simple and honest explanations may rebut these indications. But the disparity of regulations applicable to transportation company securities and nontransportation companies still require correction if investors generally are to receive equality of protection.

Today, the subcommittee hopes to initiate action which will result in that record being developed. We have no intention of denying the parties involved an opportunity to be heard. On the contrary we urge all interested parties to appear before us.

We shall look forward to subsequent hearings by ourselves and investigations by both the SEC and the ICC to this opportunity.

The first witnesses to be heard this morning are Mr. Hardin and Mr. Kahn. Would you step forward, please?

It has been suggested that all the witnesses who have been notified testify today as a panel, and will Mr. Smith of the Securities and Exchange Commission and Mr. Phillip Loomis of the SEC as well as Mr. Irving M. Pollack, Director of the Division of Trading come forward, please? Are those gentlemen here?

Mr. DINGELL. Might I suggest it would be well for the chairman to consider the question of swearing the witnesses, as I understand it is a regular practice and it might be well for the committee to provide them with a copy of the rules.

Mr. MACDONALD. I personally do not feel it is necessary but if the committee desires it I do not see any harm. We are sending for copies of the rules to be before us.

All right, stand and raise your right hand. Do you solemnly swear that the testimony you are about to give before this subcommittee will be the truth, the whole truth and nothing but the truth, so help you God?

Mr. KAHN. I do.

Mr. HARDIN. I do.

Mr. SMITH. I do.

Mr. LOOMIS. I do.

Mr. POLLACK. I do.

Mr. MACDONALD. For the purpose of being helpful to the reporter, would you mind identifying yourself from left to right?

Mr. POLLACK. Irving M. Pollack, Director of the Trading and Marketing Division of the Securities and Exchange Commission.

Mr. LOOMIS. Philip A. Loomis, Jr., General Counsel of the Securities and Exchange Commission.

Mr. SMITH. Richard B. Smith, Commissioner, Securities and Exchange Commission.

Mr. HARDIN. Dale W. Hardin, Vice Chairman, Interstate Commerce Commission.

Mr. KAHN. Fritz R. Kahn, General Counsel of the Interstate Commerce Commission.

Mr. MACDONALD. With that, gentlemen, we welcome you before the committee, and we will turn over the start of the questioning to our counsel, Mr. Lishman.

Mr. LISHMAN. To expedite the hearings, the staff has compiled a series of exhibits in packets which have been submitted to members of the subcommittee, and to the witnesses, and I am going to ask that packet No. 1 be supplied to the witnesses—they have them all.

Now, each exhibit is tabbed and at the appropriate point in the hearing will be referred to by its tab letter.

Before proceeding with the questioning, it is important to note the diversification of the corporations under the ownership or control of the Penn Central Co.

At this point I should like to have in the record a chart diagramming the corporate structure of the Penn Central. Attached to that is another earlier chart prepared by the ICC in its staff study entitled, "Conglomerate Merger Studies," and these charts comprise exhibit A, which I believe the witnesses have.

Mr. MACDONALD. Do you offer them at this point in the record?

Mr. LISHMAN. Yes, sir.

Mr. MACDONALD. Without objection, so ordered.

(The material referred to will be found on p. 22.)

Mr. LISHMAN. I would like to have the entire packets in the record. Packet No. 1 contains excerpts of pertinent statutes, rules, and regulations, including excerpts from the 1933 SEC Act, 1934 act, the rules and regulations of the 1934 SEC Act, the 1940 Investment Company Act, and excerpts from the ICC Act.

Mr. MACDONALD. Without objection they will be received in the record at this point.

(The excerpts of pertinent statutes, rules, and regulations follow :)

PACKET 1
EXCERPTS OF PERTINENT STATUTES, RULES, AND
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EXCERPTS of
SECURITIES ACT OF 1933

AS AMENDED TO OCTOBER 22, 1965

[PUBLIC—No. 22—73d Congress]

[H. R. 5480]

AN ACT

To provide full and fair disclosure of the character of securities sold in interstate and foreign commerce and through the mails, and to prevent frauds in the sale thereof, and for other purposes.

*Be it enacted by the Senate and House of Representatives
of the United States of America in Congress assembled,*

TITLE I

Exempted Securities

SEC. 3. (a) Except as hereinafter expressly provided, the provisions of this title shall not apply to any of the following classes of securities:

(c) Any security issued by a common or contract carrier, the issuance of which is subject to the provisions of section 20a of the Interstate Commerce Act, as amended:²

Civil Liabilities on Account of False
Registration Statement

SEC. 11. (a) In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security (unless it is proved that at the time of such acquisition he knew of such untruth or omission) may, either at law or in equity, in any court of competent jurisdiction, sue—

(1) every person who signed the registration statement;

(2) every person who was a director of (or person performing similar functions) or partner in, the issuer at the time of the filing of the part of the registration statement with respect to which his liability is asserted;

(3) every person who, with his consent, is named in the registration statement as being or about to become a director, person performing similar functions, or partner;

(4) every accountant, engineer, or appraiser, or any person whose profession gives authority to a statement made by him, who has with his consent been named as having prepared or certified any part of the registration statement, or as having prepared or certified any report or valuation which is used in connection with the registration statement, with respect to the statement in such registration statement, report, or valuation, which purports to have been prepared or certified by him;

(5) every underwriter with respect to such security.

If such person acquired the security after the issuer has made generally available to its security holders an earning statement covering a period of at least twelve months beginning

after the effective date of the registration statement, then the right of recovery under this subsection shall be conditioned on proof that such person acquired the security relying upon such untrue statement in the registration statement or relying upon the registration statement and not knowing of such omission, but such reliance may be established without proof of the reading of the registration statement by such person.¹

(b) Notwithstanding the provisions of subsection (a) no person, other than the issuer, shall be liable as provided therein who shall sustain the burden of proof—

(1) that before the effective date of the part of the registration statement with respect to which his liability is asserted (A) he had resigned from or had taken such steps as are permitted by law to resign from, or ceased or refused to act in, every office, capacity, or relationship in which he was described in the registration statement as acting or agreeing to act, and (B) he had advised the Commission and the issuer in writing that he had taken such action and that he would not be responsible for such part of the registration statement; or

(2) that if such part of the registration statement became effective without his knowledge, upon becoming aware of such fact he forthwith acted and advised the Commission, in accordance with paragraph (1), and, in addition, gave reasonable public notice that such part of the registration statement had become effective without his knowledge; or

(3) that (A) as regards any part of the registration statement not purporting to be made on the authority of an expert, and not purporting to be a copy of or extract from a report or valuation of an expert, and not purporting to be made on the authority of a public official document or statement, he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading;

and (B) as regards any part of the registration statement purporting to be made upon his authority as an expert or purporting to be a copy of or extract from a report or valuation of himself as an expert, (i) he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or (ii) such part of the registration statement did not fairly represent his statement as an expert or was not a fair copy of or extract from his report or valuation as an expert; and (C) as regards any part of the registration statement purporting to be made on the authority of an expert (other than himself) or purporting to be a copy of or extract from a report or valuation of an expert (other than himself), he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue or that there was an omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or that such part of the registration statement did not fairly represent the statement of the expert or was not a fair copy of or extract from the report or valuation of the expert; and (D) as regards any part of the registration statement purporting to be a statement made by an official person or purporting to be a copy of or extract from a public official document, he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue, or that there was an omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or that such part of the registration statement did not fairly represent the statement made by the official person or was not a fair copy of or extract from the public official document.²

¹ This paragraph was added by Public No. 291, 73d Cong.

² Clause (C) and (D) of subsection (b)(3) were amended by Public No. 291, 73d Cong. Prior to amendment the clause read as follows:

(c) In determining, for the purpose of paragraph (3) of subsection (b) of this section, what constitutes reasonable investigation and reasonable ground for belief, the standard of reasonableness shall be that required of a prudent man in the management of his own property.¹

(d) If any person becomes an underwriter with respect to the security after the part of the registration statement with respect to which his liability is asserted has become effective, then for the purposes of paragraph (3) of subsection (b) of this section such part of the registration statement shall be considered as having become effective with respect to such person as of the time when he became an underwriter.

(e) The suit authorized under subsection (a) may be to recover such damages as shall represent the difference between the amount paid for the security (not exceeding the price at which the security was offered to the public) and (1) the value thereof as of the time such suit was brought, or (2) the price at which such security shall have been disposed of in the market before suit, or (3) the price at which such security shall have been disposed of after suit but before judgment if such damages shall be less than the damages representing the difference between the amount paid for the security (not exceeding the price at which the security was offered to the public) and the value thereof as of the time such suit was brought: Pro-

vided, that if the defendant proves that any portion or all of such damages represents other than the depreciation in value of such security resulting from such part of the registration statement, with respect to which his liability is asserted, not being true or omitting to state a material fact required to be stated therein or necessary to make the statements therein not misleading, such portion of or all such damages shall not be recoverable. In no event shall any underwriter (unless such underwriter shall have knowingly received from the issuer for acting as an underwriter some benefit, directly or indirectly, in which all other underwriters similarly situated did not share in proportion to their respective interests in the underwriting) be liable in any suit or as a consequence of suits authorized under subsection (a) for damages in excess of the total price at which the securities underwritten by him and distributed to the public were offered to the public. In any suit under this or any other section of this title the court may, in its discretion, require an undertaking for the payment of the costs of such suit, including reasonable attorney's fees, and if judgment shall be rendered against a party litigant, upon the motion of the other party litigant, such costs may be assessed in favor of such party litigant (whether or not such undertaking has been required) if the court believes the suit or the defense to have been without merit, in an amount sufficient to reimburse him for the reasonable expenses incurred by him, in connection with such suit, such costs to be taxed in the manner usually provided for taxing of costs in the court in which the suit was heard.²

(f) All or any one or more of the persons specified in subsection (a) shall be jointly and severally liable, and every person who becomes liable to make any payment under this section may recover contribution as in cases of contract from any person who, if sued separately, would have been liable to make the same payment, unless the person who has become liable was, and the other was not, guilty of fraudulent misrepresentation.

(g) In no case shall the amount recoverable

¹(C) as regards any part of the registration statement purporting to be made on the authority of an expert (other than himself) or purporting to be a copy of or extract from a report or valuation of an expert (other than himself), he had reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, and that such part of the registration statement fairly represented the statement of the expert or was a fair copy or extract from the report or valuation of the expert; and (D) as regards any part of the registration statement purporting to be a statement made by an official person or purporting to be a copy of or extract from a public official document, he had reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true, and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, and that such part of the registration statement fairly represented the statement made by the official person or was a fair copy of or extract from the public official document."

²Amended by Public No. 291, 73d Cong. Prior to amendment subsection (e) read as follows:

"(e) In determining for the purpose of paragraph (3) of subsection (b) of this section, what constitutes reasonable investigation and reasonable ground for belief, the standard of reasonableness shall be that required of a person occupying a fiduciary relationship."

²Amended by Public No. 291, 73d Cong. Prior to amendment subsection (e) read as follows:

"(e) The suit authorized under subsection (a) may be either (1) to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security or (2) for damages if the person suing no longer owns the security."

under this section exceed the price at which the security was offered to the public.

Civil Liabilities Arising in Connection With Prospectuses and Communications

SEC. 12. Any person who—

(1) offers or sells a security in violation of section 5, or

(2) offers or sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

Fraudulent Interstate Transactions

SEC. 17. (a) It shall be unlawful for any person in the offer or sale of any securities by

the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

(b) It shall be unlawful for any person, by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, to publish, give publicity to, or circulate any notice, circular, advertisement, newspaper, article, letter, investment service, or communication which, though not purporting to offer a security for sale, describes such security for a consideration received or to be received, directly or indirectly, from an issuer, underwriter, or dealer, without fully disclosing the receipt, whether past or prospective, of such consideration and the amount thereof.

(c) The exemptions provided in section 3 shall not apply to the provisions of this section.

Penalties

SEC. 24. Any person who willfully violates any of the provisions of this title, or the rules and regulations promulgated by the Commission under authority thereof, or any person who willfully, in a registration statement filed under this title, makes any untrue statement of a material fact or omits to state any material fact required to be stated therein or necessary to make the statements therein not misleading, shall upon conviction be fined not more than \$5,000 or imprisoned not more than five years, or both.

Schedule A

[NOTE: See Appendix, II-B, 2, p. 25, for requirements with respect to investment companies.]

(1) The name under which the issuer is doing or intends to do business;

(2) the name of the State or other sovereign power under which the issuer is organized;

(3) the location of the issuer's principal business office, and if the issuer is a foreign or territorial person, the name and address of its agent in the United States authorized to receive notice;

(4) the names and addresses of the directors or persons performing similar functions, and the chief executive, financial and accounting officers, chosen or to be chosen if the issuer be a corporation, association, trust, or other entity; of all partners, if the issuer be a partnership; and of the issuer, if the issuer be an individual; and of the promoters in the case of a business to be formed, or formed within two years prior to the filing of the registration statement;

(5) the names and addresses of the underwriters;

(6) the names and addresses of all persons, if any, owning of record or beneficially, if known, more than 10 per centum of any class of stock of the issuer, or more than 10 per centum in the aggregate of the outstanding stock of the issuer as of a date within twenty days prior to the filing of the registration statement;

(7) the amount of securities of the issuer held by any person specified in paragraphs (4), (5), and (6) of this schedule, as of a date within twenty days prior to the filing of the registration statement, and, if possible, as of one year prior thereto, and the amount of the securities, for which the registration statement is filed, to which such persons have indicated their intention to subscribe;

(8) the general character of the business actually transacted or to be transacted by the issuer;

(9) a statement of the capitalization of the issuer, including the authorized and outstanding amounts of its capital stock and the proportion thereof paid up, the number and classes of shares in which such capital stock is divided, par value thereof, or if it has no par value, the stated or assigned value thereof, a description of the respective voting rights, preferences, conversion and exchange rights, rights to dividends, profits, or cap-

ital of each class, with respect to each other class, including the retirement and liquidation rights or values thereof;

(10) a statement of the securities, if any, covered by options outstanding or to be created in connection with the security to be offered, together with the names and addresses of all persons, if any, to be allotted more than 10 per centum in the aggregate of such options;

(11) the amount of capital stock of each class issued or included in the shares of stock to be offered;

(12) the amount of the funded debt outstanding and to be created by the security to be offered, with a brief description of the date, maturity, and character of such debt, rate of interest, character of amortization provisions, and the security, if any, therefor. If substitution of any security is permissible, a summarized statement of the conditions under which such substitution is permitted. If substitution is permissible without notice, a specific statement to that effect;

(13) the specific purposes in detail and the approximate amounts to be devoted to such purposes, so far as determinable, for which the security to be offered is to supply funds, and if the funds are to be raised in part from other sources, the amounts thereof and the sources thereof, shall be stated;

(14) the remuneration, paid or estimated to be paid, by the issuer or its predecessor, directly or indirectly, during the past year and ensuing year, to (a) the directors or persons performing similar functions, and (b) its officers and other persons, naming them wherever such remuneration exceeded \$25,000 during any such year;

(15) the estimated net proceeds to be derived from the security to be offered;

(16) the price at which it is proposed that the security shall be offered to the public or the method by which such price is computed and any variation therefrom at which any portion of such security is proposed to be offered to any persons or classes of persons, other than the underwriters, naming them or specifying the class. A variation in price may be proposed prior to the date of the public offering of the security, but the Commission shall immediately be notified of such variation;

(17) all commissions or discounts paid or to be paid, directly or indirectly, by the issuer to the

underwriters in respect of the sale of the security to be offered. Commissions shall include all cash, securities, contracts, or anything else of value, paid, to be set aside, disposed of, or understandings with or for the benefit of any other persons in which any underwriter is interested, made, in connection with the sale of such security. A commission paid or to be paid in connection with the sale of such security by a person in which the issuer has an interest or which is controlled or directed by, or under common control with, the issuer shall be deemed to have been paid by the issuer. Where any such commission is paid the amount of such commission paid to each underwriter shall be stated;

(18) the amount or estimated amounts, itemized in reasonable detail, of expenses, other than commissions specified in paragraph (17) of this schedule, incurred or borne by or for the account of the issuer in connection with the sale of the security to be offered or properly chargeable thereto, including legal, engineering, certification, authentication, and other charges;

(19) the net proceeds derived from any security sold by the issuer during the two years preceding the filing of the registration statement, the price at which such security was offered to the public, and the names of the principal underwriters of such security;

(20) any amount paid within two years preceding the filing of the registration statement or intended to be paid to any promoter and the consideration for any such payment;

(21) the names and addresses of the vendors and the purchase price of any property, or goodwill, acquired or to be acquired, not in the ordinary course of business, which is to be defrayed in whole or in part from the proceeds of the security to be offered, the amount of any commission payable to any person in connection with such acquisition, and the name or names of such person or persons, together with any expense incurred or to be incurred in connection with such acquisition, including the cost of borrowing money to finance such acquisition;

(22) full particulars of the nature and extent of the interest, if any, of every director, principal executive officer, and of every stockholder holding more than 10 per centum of any class of stock or more than 10 per centum in the aggregate of the stock of the issuer, in any property acquired, not

in the ordinary course of business of the issuer, within two years preceding the filing of the registration statement or proposed to be acquired at such date;

(23) the names and addresses of counsel who have passed on the legality of the issue;

(24) dates of and parties to, and the general effect concisely stated of every material contract made, not in the ordinary course of business, which contract is to be executed in whole or in part at or after the filing of the registration statement or which contract has been made not more than two years before such filing. Any management contract or contract providing for special bonuses or profit-sharing arrangements, and every material patent or contract for a material patent right, and every contract by or with a public utility company or an affiliate thereof, providing for the giving or receiving of technical or financial advice or service (if such contract may involve a charge to any party thereto at a rate in excess of \$2,500 per year in cash or securities or anything else of value), shall be deemed a material contract;

(25) a balance sheet as of a date not more than ninety days prior to the date of the filing of the registration statement showing all of the assets of the issuer, the nature and cost thereof, whenever determinable, in such detail and in such form as the Commission shall prescribe (with intangible items segregated), including any loan in excess of \$20,000 to any officer, director, stockholder or person directly or indirectly controlling or controlled by the issuer, or person under direct or indirect common control with the issuer. All the liabilities of the issuer in such detail and such form as the Commission shall prescribe, including surplus of the issuer showing how and from what sources such surplus was created, all as of a date not more than ninety days prior to the filing of the registration statement. If such statement be not certified by an independent public or certified accountant, in addition to the balance sheet required to be submitted under this schedule, a similar detailed balance sheet of the assets and liabilities of the issuer, certified by an independent public or certified accountant, of a date not more than one year prior to the filing of the registration statement, shall be submitted;

(26) a profit and loss statement of the issuer showing earnings and income, the nature and source thereof, and the expenses and fixed charges

in such detail and such form as the Commission shall prescribe for the latest fiscal year for which such statement is available and for the two preceding fiscal years, year by year, or, if such issuer has been in actual business for less than three years, then for such time as the issuer has been in actual business, year by year. If the date of the filing of the registration statement is more than six months after the close of the last fiscal year, a statement from such closing date to the latest practicable date. Such statement shall show what the practice of the issuer has been during the three years or lesser period as to the character of the charges, dividends or other distributions made against its various surplus accounts, and as to depreciation, depletion, and maintenance charges, in such detail and form as the Commission shall prescribe, and if stock dividends or avails from the sale of rights have been credited to income, they shall be shown separately with a statement of the basis upon which the credit is computed. Such statement shall also differentiate between any recurring and nonrecurring income and between any investment and operating income. Such statement shall be certified by an independent public or certified accountant;

(27) if the proceeds, or any part of the proceeds, of the security to be issued is to be applied directly or indirectly to the purchase of any business, a profit and loss statement of such business certified by an independent public or certified accountant, meeting the requirements of paragraph (26) of this schedule, for the three preceding fiscal years, together with a balance sheet, similarly certified, of such business, meeting the requirements of paragraph (25) of this schedule of a date not more than ninety days prior to the filing of the registration statement or at the date such business was acquired by the issuer if the business was acquired by the issuer more than ninety days prior to the filing of the registration statement;

(28) a copy of any agreement or agreements (or, if identic agreements are used, the forms thereof) made with any underwriter, including all contracts and agreements referred to in paragraph (17) of this schedule;

(29) a copy of the opinion or opinions of counsel in respect to the legality of the issue, with a translation of such opinion, when necessary, into the English language;

(30) a copy of all material contracts referred to in paragraph (24) of this schedule, but no disclosure shall be required of any portion of any such contract if the Commission determines that disclosure of such portion would impair the value of the contract and would not be necessary for the protection of the investors;

(31) unless previously filed and registered under the provisions of this title, and brought up to date, (a) a copy of its articles of incorporation, with all amendments thereof and of its existing bylaws or instruments corresponding thereto, whatever the name, if the issuer be a corporation; (b) copy of all instruments by which the trust is created or declared, if the issuer is a trust; (c) a copy of its articles of partnership or association and all other papers pertaining to its organization, if the issuer is a partnership, unincorporated association, joint-stock company, or any other form of organization; and

(32) a copy of the underlying agreements or indentures affecting any stock, bonds, or debentures offered or to be offered.

In case of certificates of deposit, voting trust certificates, collateral trust certificates, certificates of interest or shares in unincorporated investment trusts, equipment trust certificates, interim or other receipts for certificates, and like securities, the Commission shall establish rules and regulations requiring the submission of information of a like character applicable to such cases, together with such other information as it may deem appropriate and necessary regarding the character, financial or otherwise, of the actual issuer of the securities and/or the person performing the acts and assuming the duties of depositor or manager.

E. Section 3(a) (6) of the Securities Act exempts from the registration provisions of that act "any security issued by a common or contract carrier, the issuance of which is subject to the provisions of section 20a of the Interstate Commerce Act, as amended."

Section 20a of the Interstate Commerce Act, 49 U.S.C. § 20a, defines carriers as follows:

"(1) *Carrier defined.*—As used in this section the term 'carrier' means a common carrier by railroad (except a street, suburban, or interurban electric railway which is not operated as a part of a general steam railroad system of transportation) which is subject to this part, or any corporation organized for the purpose of engaging in transportation by railroad subject to this part, or a sleeping-car company which is subject to this part."

Subsection (2) of section 20a as amended July 24, 1965, P.L. 89-86, § 1, 79 Stat. 263, describes the securities which are subject to the jurisdiction of the Interstate Commerce Commission as follows:

"§ 20a (2) *Issuance of securities; assumption of obligations; authorization.*—It shall be unlawful for any carrier to issue any share of capital stock or any bond or other evidence of interest in or indebtedness of the carrier (hereinafter in this section collectively termed 'securities') or to assume any obligation or liability as lessor, lessee, guarantor, indorser, surety, or otherwise, in respect of the securities of any other person, natural or artificial, even though permitted by the authority creating the carrier corporation, unless and until, and then only to the extent that, upon application by the carrier, and after investigation by the commission of the purposes and uses of the proposed issue and the proceeds thereof, or of the proposed assumption of obligation or liability in respect of the securities of any other person, natural or artificial, the commission by order authorizes such issue or assumption. The commission shall make such order only if it finds that such issue or assumption: (a) is for some lawful object within its corporate purposes, and compatible with the public interest, which is necessary or appropriate for or consistent with the proper performance by the carrier of service to the public as a common carrier, and which will not impair its ability to perform that service, and (b) is reasonably necessary and appropriate for such purpose: *Provided*, That nothing in this section is to be construed as applying to securities issued or obligations or liabilities assumed by the United States or any instrumentality thereof, or by the District of Columbia or any instrumentality thereof, or by any State of the United States or by any political subdivision or municipal corporation of any State, or by any instrumentality of one or more States, political subdivisions thereof, or municipal corporations."

In addition to the carriers whose securities were originally subject to the jurisdiction of the Interstate Commerce Commission under section 20a, section 214 of the Motor Carrier Act of 1935 (approved August 9, 1935, 49 Stat. 513, 557; amended June 29, 1938, c. 811, § 15, 52 Stat. 1240; amended September 18, 1940, § 22(a), 54 Stat. 924; amended July 10, 1952, c. 648, 66 Stat. 542; amended September 7, 1957, P.L. 85-309, 71 Stat. 631; and amended July 24, 1965, P.L. 89-86, § 2, 79 Stat. 263, 49 U.S.C. § 314) added the following classifications:

"Common or contract carriers by motor vehicles, corporations organized for the purpose of engaging in transportation as such carriers, and corporations authorized by order of the Commission to acquire control of any such carrier, or of two or more such carriers, shall be subject to the provisions of paragraphs (2) to (11), inclusive, of section 20a of part I of this Act (including penalties applicable in cases of violations thereof): *Provided, however*, That said provisions shall not apply to such carriers or corporations where the value of the capital stock or principal amount of other securities to be issued, together with the value of capital stock and principal amount of other securities then outstanding, does not exceed \$1,000,000, nor to the issuance of notes of a maturity of two years or less and aggregating not more than \$200,000, which notes aggregating such amount including all outstanding obligations maturing in two years or less may be issued without reference to the percentage which said amounts bear to the total amount of outstanding securities. In the case of capital stock having no par value, the value thereof for the purpose of this section shall be the fair market value as of the date of its issue; and in the case of capital stock having par value, the value for the purpose of this section shall be the fair market value as of the date of its issue, or the par value, whichever is greater: *Provided further*, That the exemption in section 3(a) (6) of the 'Securities Act of 1933,' is hereby amended to read as follows: '(6) any security issued by a common or contract carrier, the issuance of which is subject to provisions of section 20a of the Interstate Commerce Act as amended:'. *And provided further*, That the provisions of this section shall not apply to the United States or any instrumentality thereof, the District of Columbia, or any instrumentality thereof, any State of the United States or political subdivision or municipal corporation thereof, or any instrumentality of one or more States, political subdivisions thereof, or municipal corporations."

[Note: Consideration should be given to sec. 705 (5) of chap. XV of the National Bankruptcy Act as amended by Public No. 242, 76th Cong., approved July 28, 1939, c. 393, 53 Stat. 1135, dealing with railroad adjustments, which provides that for the purpose of that chapter the term "securities" shall include, in addition to those defined in sec. 20a of the Interstate Commerce Act, certificates of deposit and all other evidences of ownership of or interest in securities. However, sec. 755 of said chapter XV terminated such provisions as of July 31, 1940, except as to proceedings initiated on or before that date, c. 393, § 755, 53 Stat. 1111.]

Excerpts of S. E. C. Act of 1934

Regulation of the Use of Manipulative and Deceptive Devices

SECTION 10. It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

(a) To effect a short sale, or to use or employ any stop-loss order in connection with the purchase or sale, of any security registered on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Directors, Officers, and Principal Stockholders

SECTION 16. (a) Every person who is directly or indirectly the beneficial owner of more than 10 per centum of any class of any equity security (other than an exempted security) which is registered pursuant to section 12 of this title, or who is a director or an officer of the issuer of such security, shall file, at the time of the registration of such security on a national securities exchange or by the effective date of a registration statement filed pursuant to section 12(g) of this title, or within ten days after he becomes such beneficial owner, director, or officer, a statement with the Commission (and, if such security is registered on a national securities exchange, also with the exchange) of the amount of all equity securities of such issuer of which he is the beneficial owner, and within ten days after the close of each calendar month thereafter, if there has been a change in such ownership during such month, shall file with the Commission (and if such security is registered on a national securities exchange, shall also file with the exchange), a statement indicating his ownership at the close of the calendar month and such changes in his ownership as have occurred during such calendar month.

(b) For the purpose of preventing the unfair use of information which may have been obtained by such beneficial owner, director, or officer by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity security of such issuer (other than an exempted security) within any period of less than six months, unless such security was acquired in good faith in connection with a debt previously contracted, shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months. Suit to recover such profit may be instituted at law or in equity in any court of competent jurisdiction by the issuer, or by the owner of any security of the issuer in the name and in behalf of the issuer if the issuer shall fail or refuse to bring such suit within sixty days after request or shall fail diligently to prosecute the same thereafter; but no such suit shall be brought more than two years after the date such profit was realized. This subsection shall not be construed to cover any transaction where such beneficial owner was not such both at the time of the purchase and sale, or the sale and purchase, of the security involved, or any transaction or transactions which the Commission by rules and regulations may exempt as not comprehended within the purpose of this subsection.

Powers With Respect to Exchanges and Securities

SECTION 19. (a) The Commission is authorized, if in its opinion such action is necessary or appropriate for the protection of investors—

(4) And if in its opinion the public interest so requires, summarily to suspend trading in any registered security on any national securities exchange for a period not exceeding ten days, or with the approval of the President, summarily to suspend all trading on any national securities exchange for a period not exceeding ninety days.

**Excerpts of General
Rules and Regulations
under S. E. C. Act of
1934**

Rule 10b-5. Employment of Manipulative and
Deceptive Devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Rule 10b-6. Prohibitions Against Trading by
Persons Interested in a Distribution

(a) It shall constitute a "manipulative or deceptive device or contrivance" as used in section 10(b) of the Act for any person,

(1) who is an underwriter or prospective underwriter in a particular distribution of securities, or

(2) who is the issuer or other person on whose behalf such a distribution is being made, or

(3) who is a broker, dealer, or other person who has agreed to participate or is participating in such a distribution, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange, either alone or with one or more other persons, to bid for or purchase for any account in which he has a beneficial interest, any security which is the subject of such distribution, or any security of the same class and series, or any right to purchase any such security, or to attempt to induce any person to purchase any such security or right until after he has completed his participation in such distribution:

Excerpts of Investment Company Act of 1940

Definition of Investment Company

Sec. 3. (a) When used in this title, "investment company" means any issuer which—

(1) is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities;

(2) is engaged or proposes to engage in the business of issuing face-amount certificates of the installment type, or has been engaged in such business and has any such certificate outstanding; or

(3) is engaged or proposes to engage in the business of investing, reinvesting, owning, holding, or trading in securities, and owns or proposes to acquire investment securities having a value exceeding 10 per centum of the value of such issuer's total assets (exclusive of Government securities and cash items) on an unconsolidated basis.

As used in this section, "investment securities" includes all securities except (A) Government securities, (B) securities issued by employees' securities companies, and (C) securities issued by majority-owned subsidiaries of the owner which are not investment companies.

(b) Notwithstanding paragraph (3) of subsection (a), none of the following persons is an investment company within the meaning of this title:

(1) Any issuer primarily engaged, directly or through a wholly-owned subsidiary or subsidiaries, in a business or businesses other than that of investing, reinvesting, owning, holding, or trading in securities.

(2) Any issuer which the Commission, upon application by such issuer, finds and by order declares to be primarily engaged in a business or businesses other than that of investing, reinvesting, owning, holding, or trading in securities either directly or (A) through majority-owned subsidiaries or (B) through controlled companies conducting similar types of businesses. The filing of an application under this paragraph by an issuer other than a registered investment company shall exempt the applicant for a period of sixty days from all provisions of this title applicable to investment companies as such. For cause shown, the

Commission by order may extend such period of exemption for an additional period or periods. Whenever the Commission, upon its own motion or upon application, finds that the circumstances which gave rise to the issuance of an order granting an application under this paragraph no longer exist, the Commission shall by order revoke such order.

(3) Any issuer all the outstanding securities of which (other than short-term paper and directors' qualifying shares) are directly or indirectly owned by a company excepted from the definition of investment company by paragraph (1) or (2) of this subsection.

(c) Notwithstanding subsections (a) and (b), none of the following persons is an investment company within the meaning of this title:

(9) Any company subject to regulation under the Interstate Commerce Act, or any company whose entire outstanding capital stock is owned or controlled by such a company: Provided, That the assets of the controlled company consist substantially of securities issued by companies which are subject to regulation under the Interstate Commerce Act.

Excerpt of I. C. C. Act

Sec. 5

(4) It shall be unlawful for any person, except as provided in paragraph (2), to enter into any transaction

within the scope of subparagraph (a) thereof, or to accomplish or effectuate, or to participate in accomplishing or effectuating, the control or management in a common interest of any two or more carriers, however such result is attained, whether directly or indirectly, by use of common directors, officers, or stockholders, a holding or investment company or companies, a voting trust or trusts, or in any other manner whatsoever. It shall be unlawful to continue to maintain control or management accomplished or effectuated after the enactment of this amendatory paragraph and in violation of its provisions. As used in this paragraph and paragraph (5), the words "control or management" shall be construed to include the power to exercise control or management.

84 Stat. 907.

Control, unauthorized, unlawful.

Continuance in future unlawful.

"Control or management" construed.

Mr. LISHMAN. Packet No. II contains exhibits A to G, of which A is a diagram of Penn Central and subsidiaries; B is a balance sheet of the Pennsylvania Co. contained at page 27 of prospectus; exhibit C is a breakdown of the securities holdings of the Pennsylvania Co.; exhibit D is a letter of July 1, 1970, requesting opinion about the Pennsylvania Co. under the Investment Company Act of 1940; exhibit E deals with the use of proceeds as shown on page 4 of the prospectus; F is an article in the *Washington Post* appearing May 29, 1970; and G is another article appearing in the *Washington Post* under date of May 13, 1970. I should like to have this packet of exhibits in the record.

Mr. MACDONALD. Could I ask what purpose the articles of the newspaper are intended to serve?

Mr. LISHMAN. Well, among other things, they disclose for the first time the notice to the public of the impending bankruptcy of the Penn Central.

Mr. MACDONALD. I am sure counsel is not putting them in for any probative value.

Mr. LISHMAN. No.

Mr. MACDONALD. All right. Without objection, so ordered.

(Packet II, as previously described, follows:)

PACKET II

INDEX OF EXHIBITS

	Page
Diagram of Penn Central and subsidiaries	22
Balance sheet of Pennsylvania Co. (p. 27 of prospectus)	26
Breakdown of security holdings of Pennsylvania Co.	27
Letter of July 1, 1970 requesting opinion re Pennsylvania Co. under the Investment Company Act of 1940	28
Use of Proceeds (p. 4 of prospectus)	44
May 29, 1970, article in Washington Post	45
May 13, 1970, article in Washington Post	46

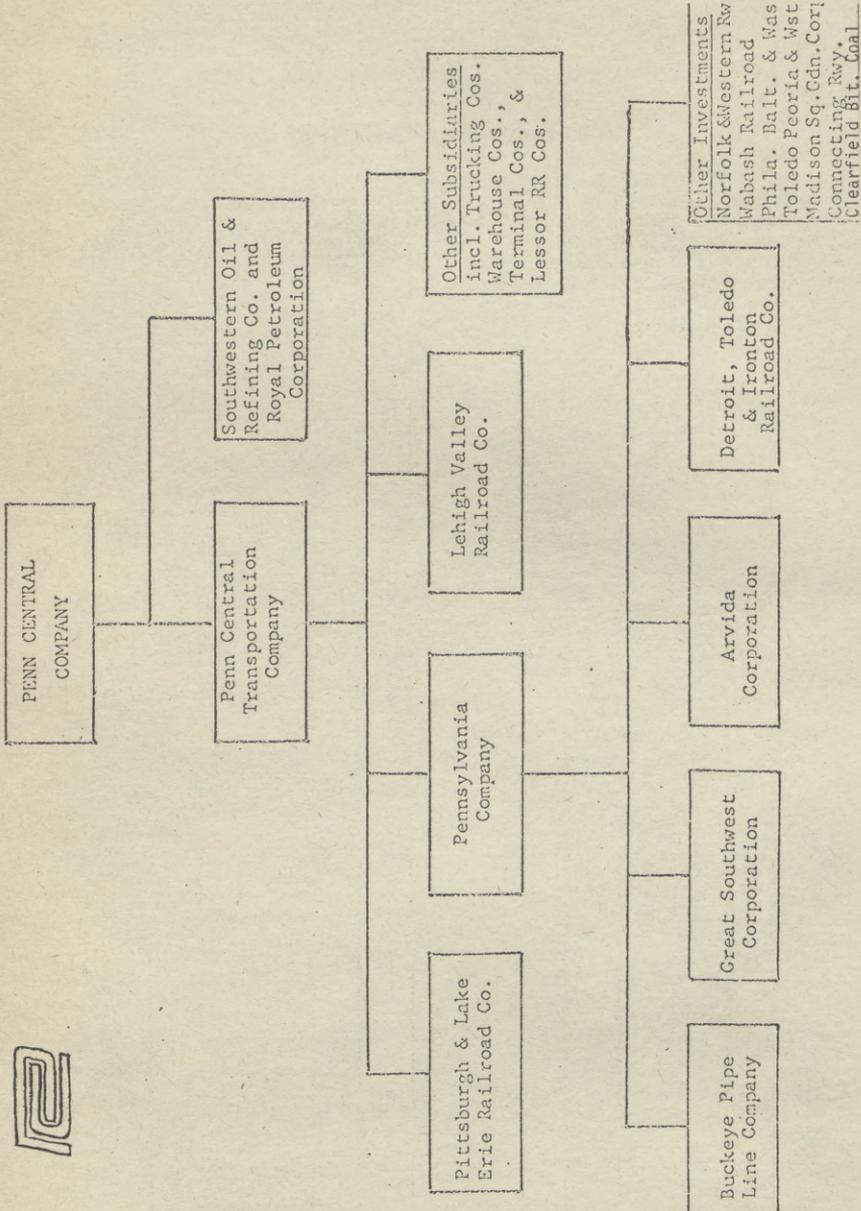


Chart 1.

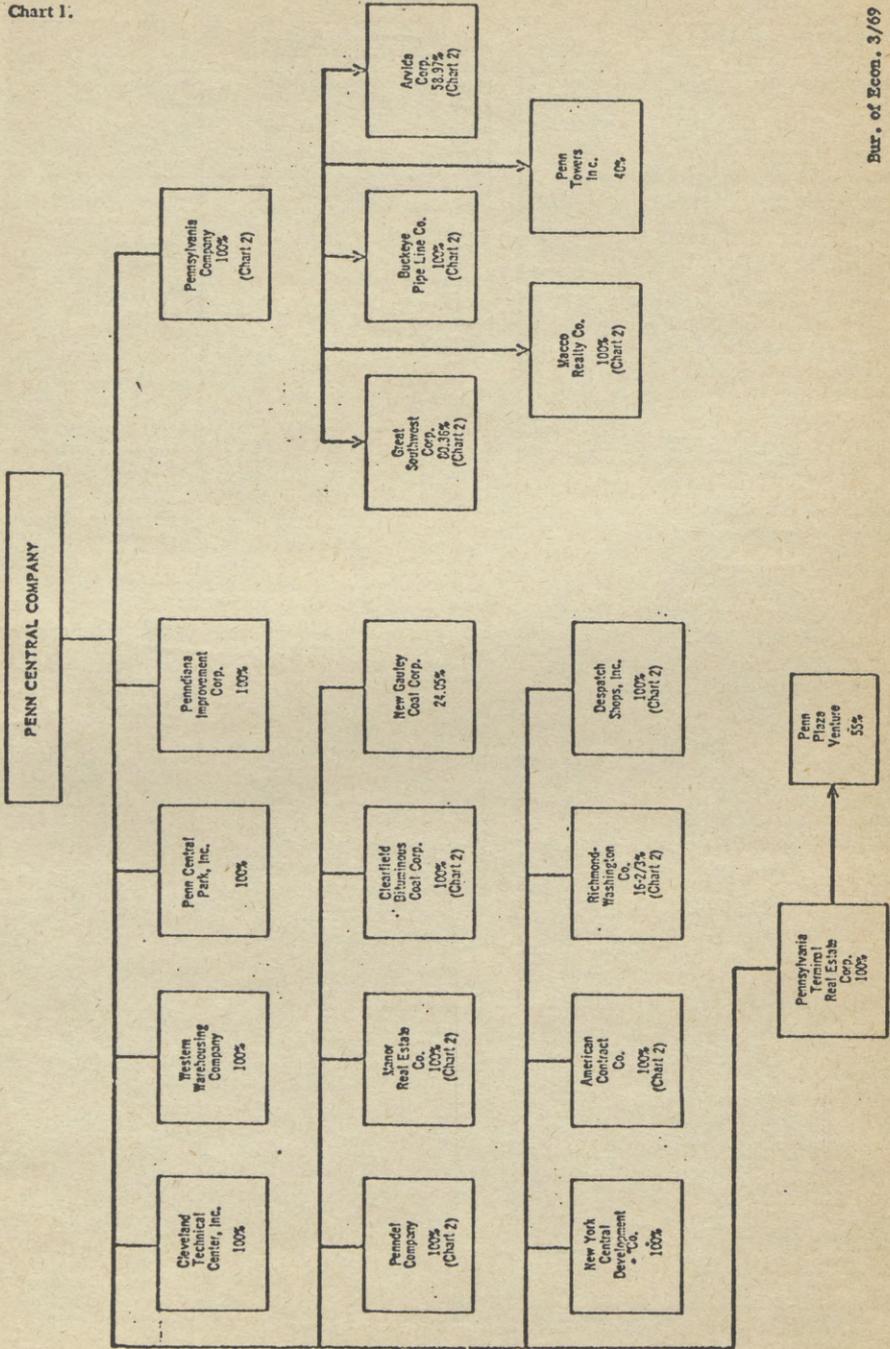
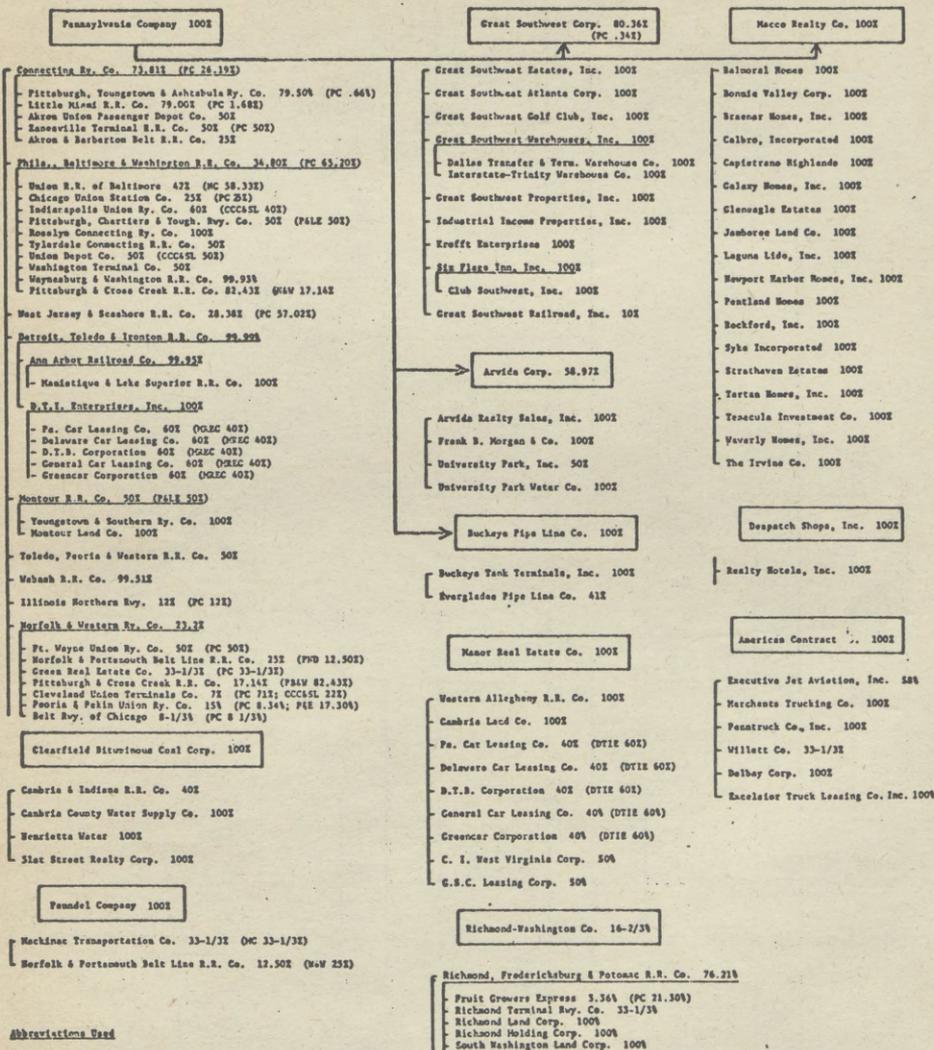


Chart 3.



Abbreviations Used

- PC - Penn Central Company
- MC - Michigan Central R.R. Co.
- C Ry. - Connecting Ry. Co.
- BNW - Norfolk & Western Ry. Co.
- NC - Northern Central Ry. Co.
- CCCSL - Cleveland, Cincinnati, Chicago & St. Louis Ry. Co.
- PAIS - Pittsburgh & Lake Erie R.R. Co.
- PRAW - Philadelphia, Baltimore & Washington R.R. Co.
- MCR - Mahoning Coal Railroad
- BE - New York, New Haven & Hartford R.R. Co.
- LV - Lehigh Valley R.R. Co.
- IND - Indiana Harbor Belt R.R. Co.
- PAE - Peoria & Eastern Ry. Co.
- WJRS - United New Jersey R.R. & Canal Co.
- NYAN - New York & Harlem R.R. Co.
- MREK - Manor Real Estate Co.
- DTIE - D.T.I. Enterprises, Inc.
- FDG - Pennel Co.
- AsEJ - Associates of the Jersey Co.
- PaCo - Pennsylvania Company

NOTES: Charts indicate situation as a pro forma basis as of December 31, 1967.
 Strick Corporation, and its affiliated companies, was sold to Prudential Insurance Co. of America and Lehman Brothers, December 1968. (Moody's)
 Madison Square Garden Corp. now owns 100% of Madison Square Garden Center, Inc. and 80% of Two Penn Plaza. (Moody's)

Chart 3.

Penn Central Company

Class I Line-Rail Railroads

- Lehigh Valley R.R. Co. 97,217
- Lehigh & Hudson River Ry. Co. 22,181 (PC 14,433)
- Bay Shore Connecting R.R. Co. 501
- Buffalo Creek R.R. Co. 501
- Iamson R.R. Co. 501
- Onondago River Ry. Co. 501 (PC 501)
- Niagara Jct. Ry. Co. 211 (PC 501)
- Black Diamond Transport Co. 1001
- Abolun Corp. 1001
- Consolidated Real Estate Company 1001
- United Real Estate Company 1001
- Pennsylvania-Reading Seashore Lines 86,641
- Allegheny & Lake Erie P.R. Co. 81,217
- Monongahela Ry. Co. 33-1/31 (PC 33-1/31)
- Norfolk P.R. Co. 501 (PC 501)
- Thompson & Southern Ry. Co. 1001
- Westmor Land Co. 1001
- Pittsburgh, Chartiers & Young Ry. Co. 501 (P&W 501)
- Rahoning State Line R.R. Co. 92,501 (PC 2,831)
- Lake Erie & Western R.R. Co. 501 (CWR 501)
- Illinois Terminal Railroad Co. 9,092

Class II Line-Rail Railroads

- Baltimore & Eastern R.R. Co. 1001
- Cherry Tree & Diamondville R.R. Co. 1001
- Central Indiana Ry. Co. 501 (CCICSL 501)
- Lake Erie & Pittsburgh Ry. Co. 1001
- Monongahela Ry. Co. 33-1/31 (PALE 33-1/31)
- New York & Long Branch R.R. Co. 501
- New York Connecting R.R. Co. 501 (CN 501) /
- Pennsylvania & Atlantic R.R. Co. 1001
- Lehigh & Hudson River Ry. Co. 14,433 (LV 22,181)
- Saratoga R.R. Co. 49,991
- Shawmutown R.R. Co. of Pa. 13,771
- Nicholas, Fayette & Greenbrier R.R. Co. 501

Class II Motor Carriers

- Pennsylvania Truck Lines, Inc. 1001
- New York Central Transport Co. 1001
- New York Central Transport Co., Inc. 1001

Class I Switching & Terminal Companies

- Belt Ry. Co. of Chicago 8-1/31 (B&V 6-1/31)
- Chicago Union Station Co. 251 (P&W 251)
- Cincinnati Union Terminal Co. 14-2/71 (CCICSL 14-2/71)
- Indiana Harbor Belt R.R. Co. 111 (PC 213)
- Calumet Western Ry. Co. 501 (PC 251)
- Lakefront Dock & Terminal Co. 501

Class II Switching & Terminal Companies

- Calumet Western Ry. Co. 251 (IHR 501)
- Dayton Union Ry. Co. 33-1/31 (CCICSL 23-1/31)
- Fort Wayne Union Ry. Co. 501 (B&W 501)
- Peoria & Pekin Union Ry. Co. 8,341 (PAE 17,301; B&W 151)
- Toledo Terminal R.R. Co. 32,151 (TC 724)
- Wilkes-Barre Connecting R.R. Co. 501
- Onondago River Ry. Co. 501 (LV 501)
- Boston Terminal Corp. 501 (MT 701) /
- Chicago River & Indiana R.R. Co. 1001
- Cleveland Union Terminal Co. 711 (CCICSL 274; B&W 71)
- Detroit Terminal R.R. Co. 251 (DC 251)
- Illinois Northern Railway 121 (PaCo 121)

Non-Operating Railroads

- Chicago, Elmhurst & Seguin Ry. 401 (PC 601)
- Detroit, Toledo & Milwaukee R.R. Co. 501 (DC 501)
- Hudson River Bridge at Albany 1001
- Lansing Manufacturers R.R. 501 (MC 501)
- Lansing Transit Railway 501 (PC 501)

Other Transportation Subsidiaries

- Canadian Pacific Car & Pkg. Trns. Co. Ltd. 501
- Merchants Dispatch Transportation Corp. 1001

Leases

- Cleveland & Pittsburgh R.R. Co. 80,191
- Conowingo Ry. Co. 28,191 (PaCo 73,811)
- (See Pennsylvania Company, Chart 1, for subsidiaries)
- Delaware R.R. Co. 84,911
- Elmore & Willingport R.R. Co. 87,571
- Erie & Pittsburgh R.R. Co. 87,561
- Northern Central Ry. Co. 80,191
- Shamokin Valley & Pottsville R.R. Co. 71,271 (PC 28,731)
- Union R.R. of Baltimore 28,211 (B&W 421)
- Venna Tunnel & Terminal R.R. Co. 1001
- Phila. & Trevost R.R. Co. 10,971 (UNTRAC 64,671)
- Phila. Belt & Washington R.R. Co. 61,201 (PaCo 91,801)
- (See Pennsylvania Company, Chart 1, for subsidiaries)
- Pittsburgh, Fort Wayne & Chicago Ry. Co. 88,501
- Pittsburgh, Youngstown & Ashkela Ry. Co. 561 (C Ry. 79,501)
- Shamokin Valley & Pottsville R.R. Co. 28,731 (PC 71,271)
- United New Jersey R.R. & Canal Co. 37,411 (UJ 1,481)
- Phila. & Trevost R.R. Co. 44,411 (PC 10,971)
- Associates of the Jersey Co. 1001
- West Jersey & Seashore R.R. Co. 57,011 (PaCo 28,341)
- Tennessee Terminal R.R. Co. 50,501 (C Ry. 501)
- Battle Creek & Sturgis Ry. Co. 14,501 (MC 81,501)
- Beach Creek R.R. Co. 79,181 (B&W 421)
- Cleveland, Cin., Chicago & St. Louis Ry. Co. 91,811
- General Indiana Ry. Co. 501 (PC 501)
- Elm. Union Term. Co. 14-2/71 (PC 14-2/71)
- Dayton Union Ry. Co. 33-1/31 (PC 33-1/31)
- Indianapolis Union Ry. Co. 421 (P&W 501)
- Union Depot Co. 501 (P&W 501)
- Cleveland Union Terminal Co. 711 (PC 711)
- Peoria & Pekin Union Ry. Co. 8,341 (PC 28,011)
- Peoria & Pekin Union Ry. Co. 17,301 (PC 6,341; B&W 151)
- Chicago & Harrisburg Coal Co. 1001
- Michigan Coal R.R. Co. 80,411
- Lake Erie & Western R.R. Co. 501 (PALE 501)
- Rahoning & Shamango Valley Co. 1001
- Mahoning State Line R.R. Co. 2,831 (PALE 82,901)
- Michigan Central P.R. 80,881
- Battle Creek & Sturgis Ry. Co. 81,501 (PC 14,501)
- Canada Southern Ry. Co. 91,811 (PC 11,071)
- Niagara River Bridge Co. 1001
- Detroit Terminal R.R. Co. 251 (PC 251)
- Indiana Harbor Belt R.R. Co. 201 (PC 213)
- Calumet Western Ry. Co. 501 (PC 251)
- Toronto, Hamilton & Buffalo Ry. Co. 21,811 (PC 37,161)
- Chicago, Milwaukee & St. Louis Ry. Co. 801 (PC 401)
- Detroit, Toledo & Milw. R.R. Co. 501 (PC 501)
- Lansing Manufacturers R.R. 501 (PC 501)
- Lansing Transit Railway 501 (PC 501)
- Detroit Manufacturers' Railroad 81,471
- Detroit River Tunnel Co. 1001
- Joliet & Northern Indiana R.R. Co. 1001
- New York & Harlem R.R. Co. 91,411
- Beach Creek R.R. Co. 811 (PC 79,181)
- Peoria & Pekin Railway Co. 28,011 (CCICSL 30,11)
- Peoria & Pekin Union Ry. Co. 17,301 (PC 8,341; B&W 151)
- St. Lawrence & Adirondack Ry. Co. 1001

It appears that this property was included in package deal between Trustees of New Haven and Penn Central Company.
See Chart 2 for abbreviations.

PENNSYLVANIA COMPANY (COMPANY ONLY)
PENNSYLVANIA COMPANY AND CONSOLIDATED SUBSIDIARIES

BALANCE SHEETS
December 31, 1969

ASSETS	Company Only (in thousands)	Consolidated
CURRENT ASSETS:		
Cash and temporary cash investments.....	\$ 23,368	\$ 38,648
Receivables:		
Transportation services	—	16,515
Real estate sales, including current portion of long-term notes.....	—	20,939
Interest	252	671
Affiliated companies	2,351	5,405
Other	984	5,509
	3,587	49,039
Materials and supplies, at cost	—	6,998
Prepaid expenses	—	2,590
Total current assets	26,955	97,275
INVESTMENTS AND ADVANCES, at cost or less (notes 2 and 4):		
Consolidated subsidiaries	257,005	—
Other	313,577	525,601
	570,582	525,601
REAL ESTATE COMPANIES—PROPERTIES HELD FOR DEVELOPMENT OR RE- SALE, at cost (note 4)		
	—	173,468
PROPERTIES (notes 3 and 4)		
	—	695,947
Less accumulated depreciation (note 3)	—	191,075
	—	504,872
DEFERRED CHARGES AND OTHER ASSETS	1,346	12,400
INVESTMENT IN CONSOLIDATED SUBSIDIARIES IN EXCESS OF NET ASSETS ACQUIRED		
	—	113,628
	\$598,883	\$1,427,244
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES (excluding debt due within one year):		
Notes payable	\$ —	\$ 41,571
Accounts payable	—	10,876
Dividends payable	816	1,019
Due to Penn Central Transportation Company	—	5,611
Accrued expenses	1,197	23,525
Other	—	1,896
Total current liabilities (excluding debt due within one year)	2,013	84,498
LONG-TERM DEBT (note 4):		
Due within one year	5,700	71,518
Due after one year	120,310	437,819
Total long-term debt	126,010	509,337
MINORITY INTEREST IN SUBSIDIARIES	—	96,949
UNAMORTIZED GAIN ON EXCHANGE AGREEMENT (note 2)	27,845	27,845
EXCESS OF NET ASSETS ACQUIRED OF CONSOLIDATED SUBSIDIARIES OVER INVESTMENT		
	—	45,962
DEFERRED INTEREST, TAXES, AND OTHER	—	30,737
AMOUNTS PAYABLE TO AFFILIATED COMPANIES	2,153	29,883
SHAREHOLDERS' EQUITY:		
4½% cumulative preferred stock of \$100 par value per share. Authorized 730,000 shares; issued 705,786 shares (note 6)	70,579	70,579
Common stock of \$25 par value. Authorized 5,600,000 shares; issued 4,985,000 shares	124,625	124,625
Retained earnings	245,658	406,829
Total shareholders' equity	440,862	602,033
	\$598,883	\$1,427,244

See accompanying notes to financial statements.

Pennsylvania Company
 Breakdown of Security Holdings on Basis
 of Market or Estimated Values Shown on
 Page 8 of Preliminary Offering Circular
 Dated April 27, 1970 and Adjusted to
 Market Prices at July 1, 1970

	4/21/70		7/1/70	
	Market*	%	Market*	%
	\$ Millions		\$ Millions	
<u>Wholly and Majority-Owned Subs.</u>				
Arvida Corp. Common-58%	\$ 36.5*	4.3	\$ 20.7*	3.4
Buckeye Pipe Line Co. Common-100%	98.0	11.4	98.0	16.3
Clearfield Bit. Coal Co. Common-100%	16.9	2.0	16.9	2.8
Detroit, Toledo & Iron RR Co. Capital-100%	40.7	4.7	40.7	6.8
Great Southwest Corp. Common-82%	312.0*	36.3	130.9*	21.8
" " " Pfd. -100%	18.9	2.2	18.9	3.1
Total Wholly & Maj.-Owned	<u>\$523.0</u>	<u>60.9</u>	<u>\$326.1</u>	<u>54.2</u>
<u>Investment Securities</u>				
Norfolk & Western RR Co. Common-23%	\$186.8*	21.7	\$128.2*	21.3
Phila., Balt. & Wash. Capital Stock-35%	29.7	3.5	29.7	4.9
Wabash RR Co. 4½% Pfd.	6.3*	0.7	4.8*	0.8
Other	113.0	13.2	113.0	18.8
Total Investment Securities	<u>\$335.8</u>	<u>39.1</u>	<u>\$275.7</u>	<u>45.8</u>
Total Securities	<u>\$858.8</u>	<u>100.0</u>	<u>\$601.8</u>	<u>100.0</u>

* Asterisk indicates securities valued at bid price for o/c securities and sale price for listed (Norfolk & Western). Other values are as estimated by Pennsylvania Co. as of April 21, 1970. Amount for Great Southwest Corp. common includes \$21.1 estimate by Pennsylvania Co. of value of warrants at April 21, 1970.

NINETY-FIRST CONGRESS

SPECIAL SUBCOMMITTEE ON INVESTIGATIONS

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ROBERT W. LISHMAN
CHIEF COUNSEL

Congress of the United States
House of Representatives

Special Subcommittee on Investigations of the
Committee on Interstate and Foreign Commerce
Room 2323, Rayburn House Office Building

Washington, D.C. 20515

July 1, 1970

Honorable Hamer H. Budge
Chairman
Securities and Exchange Commission
Washington, D. C.

Dear Mr. Chairman:

As you are aware, the Committee is presently conducting public hearings involving, among other things, the Penn Central Company and its various affiliates.

Penn Central Company, the parent holding company, owns 100 percent of the outstanding shares of Penn Central Transportation Company, operator of the now bankrupt railroad, which in turn owns 100 percent of the Pennsylvania Company. As can be seen from the enclosed copy of an offering circular dated April 27, 1970, the Pennsylvania Company holds itself out to the public and to the ICC as an investment company. More than half (approximately \$482.3 million) of the total assets (approximately \$858.8 million) of the Pennsylvania Company are represented by investments in companies not subject to regulation by the Interstate Commerce Commission.

The question arises whether under the provisions of Section 3(a)(1) of the Investment Company Act of 1940, the Pennsylvania Company may be an "investment company" and whether the thousands of stockholders of Penn Central Company could be attributed to the Pennsylvania Company. In view of the broad diversification of investments by the latter company, it appears that the exemption provided by Section 3(c)(9) of the Investment Company Act is not available.

To assist the Committee in assessing the matters now before it, a brief opinion is solicited whether the Pennsylvania Company may be an "investment company" within the meaning of Section 3(a)(1) of the Investment Company Act and, if so, whether it should be so registered with your Commission. A prompt reply will be earnestly appreciated.

Sincerely,

HARLEY O. STAGGERS
CHAIRMAN



SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

JUL 15 1970

Honorable Harley O. Staggers, Chairman
Special Subcommittee on Investigations
Committee on Interstate and Foreign
Commerce
Room 2323, Rayburn House Office Bldg.
House of Representatives
Washington, D. C. 20515

Re: The Pennsylvania Company
File No. 132-3

Dear Chairman Staggers:

In your letter of July 1, 1970 which I previously acknowledged you asked us for a brief opinion as to whether the Pennsylvania Company (the "Company") may be an investment company within the meaning of Section 3(a)(1) of the Investment Company Act of 1940 ("Act") and, if so, whether it should be so registered with the Commission.

In your letter you enclosed a copy of a Preliminary Circular dated April 27, 1970, apparently prepared for filing with the Interstate Commerce Commission and not filed with this agency, which sets forth certain business and financial information about the Company. We understand that the offering of securities proposed by this document was never made.

I have asked the staff of our Division of Corporate Regulation to consider this matter and, as discussed in more detail in the enclosed memorandum, it is the staff's tentative view based on the limited information presently available to us and set forth in the Preliminary Circular that there is a question as to whether the Pennsylvania Company is an investment company within the meaning of the Act. However, our staff is unable to express a more definite view of the Company's status without further information and legal analysis. The staff is taking active steps to obtain such information from the Company, and we hope to write you further on this matter in the near future.

Sincerely,

Hamer H. Budge
Chairman

Enclosure

MEMORANDUM OF THE DIVISION OF CORPORATE REGULATION,
SECURITIES AND EXCHANGE COMMISSION IN RESPONSE TO
LETTER DATED JULY 1, 1970 FROM HONORABLE HARLEY O.
STAGGERS.

In his letter, Chairman Staggers asked for a brief opinion as to whether the Pennsylvania Company (the "Company") may be an investment company within the meaning of Section 3(a)(1) of the Investment Company Act of 1940 ("Act") and, if so, whether it should be so registered with the Commission.

We understand the essential facts to be as follows:

Penn Central Company ("Holding Company") owns 100% of the outstanding shares of Penn Central Transportation Company ("Railroad"), and the Railroad in turn owns 100% of the common stock of the Company, a Delaware Corporation.

According to page 5 of a Preliminary Circular dated April 27, 1970, apparently prepared for filing with the Interstate Commerce Commission, the Company has outstanding, in addition to the common stock owned by the Railroad, one class of Cumulative Preferred Stock, aggregate par value \$70,579,000, as well as three classes of Collateral Trust bonds, a bank loan and one class of 9% Sinking Fund Debentures, with such debt securities aggregating \$126,010,000 in face amount.

At page 3 of the Preliminary Circular it is stated that the company "operates as an investment company with its principal interests in companies not

directly related to the railroad operations" of the Railroad. The table of assets on page 8 of the Circular states that such assets had a value, as at April 21, 1970, of approximately \$858.8 million.

Since all of the Company's assets are securities, it may fall within the definition of investment company contained in Section 3(a)(1) of the Act as an "issuer which -- (1) is or holds itself out as being engaged primarily. . . in the business of investing, reinvesting or trading in securities."

In Chairman Staggers' letter he points out that it appears that more than half of the total assets of the Company are represented by investments in companies not subject to regulation by the Interstate Commerce Commission and therefore he expresses doubt as to whether the exemption provided by Section 3(c)(9) of the Investment Company Act is available to the Company.

As Chairman Staggers knows, Section 3(c)(9) provides an exclusion from the definition of investment company for

"any company subject to regulation under the Interstate Commerce Act or any company whose entire outstanding capital stock is owned or controlled by such a company: Provided, that the assets of the controlled company consist substantially of securities issued by companies which are subject to regulation under the Interstate Commerce Act."

The Company may nevertheless argue that the present percentage of securities issued by companies subject to regulation under the Interstate Commerce Act, perhaps as much as 44%, is "substantial" within the meaning of Section 3(c)(9), in view of the fact that the Act in Section 3(a)(3)

appears to treat ownership of 40% of investment securities as substantial enough to make a company owning such securities prima facie an investment company. However, there is some indication in the legislative history of Section 3(c) (9) that "substantial" in the Section was intended to mean "substantially all." Moreover, since it appears that the Company's Cumulative Preferred stock is not owned or controlled by the Railroad, the Company appears to fail the other test of Section 3(c) (9), that the subsidiary company's "entire outstanding capital stock [be] owned or controlled by a company subject to regulation under the Interstate Commerce Act."

However, according to the Preliminary Circular, approximately \$523,000,000 or about 61% of the value of the assets of the Company consists of securities of wholly and majority-owned subsidiaries. Therefore, the company may argue that it is primarily engaged in the non-investment company businesses of its subsidiaries and not primarily engaged in investing, reinvesting, owning, holding or trading in securities.^{1/}

It is important to note that market values are available for only two of the five main wholly and majority-owned subsidiaries of the Company, with the other values being estimated by the Company. Section 2(a) (39) of the Act in effect requires investment companies to value securities for which no market quotations are readily available at fair value as determined in good faith by the board of directors. Thus, it is possible that the "estimated" values given in the Preliminary Circular

^{1/} Cf. Section 3(b) (1) which provides a specific exclusion for a company having more than 40% of its assets in "investment securities," if it is "primarily engaged, directly or through a wholly-owned subsidiary or subsidiaries, in a business or businesses other than that of investing, reinvesting, owning, holding, or trading in securities."

may not be the same as the values determined in good faith by the board of directors within the meaning of the Act.

In any event, regardless of the resolution of the foregoing uncertainties, the Company may still be an investment company, as defined by Section 3(a)(3) of the Act as a company which

"is engaged or proposes to engage in the business of investing, reinvesting, owning, holding, or trading in securities, and owns or proposes to acquire investment securities having a value exceeding 40 per centum of the value of such issuer's total assets (exclusive of Government securities and cash items) on an unconsolidated basis."

The reason for this is that, according to the Preliminary Circular, approximately 39% of the Company's assets may consist of securities of non-majority or wholly owned subsidiaries. Such securities are "investment securities" as defined in Section 3(a)(3) of the Act. Therefore, a more precise valuation of the Company's assets by its board of directors may result in the Company failing the 40 percent test of Section 3(a)(3). Moreover, our staff has recalculated the Company's percentage of investment securities as of July 1, 1970 by valuing the securities for which market quotations are available at the market prices on such date. This recalculation results in the Company having total assets of about \$602 million, with \$276 million or about 46% of its assets in investment securities.

Nevertheless, as indicated above, a substantial majority of the company's assets appears to be invested in wholly and majority owned subsidiaries and controlled companies. Therefore, the Company may be relying on Section 3(b)(1), mentioned above, or it may be entitled to a Commission order under Section 3(b)(2) of the Act declaring

it to be "primarily engaged in a business other than that of investing, reinvesting, owning, holding, or trading in securities either directly or (A) through majority-owned subsidiaries or (B) through controlled companies conducting similar types of businesses."

Before the Company could obtain such an order it would be required to file a formal application with the Commission and present evidence showing that it is primarily engaged in a non-investment company business through the ownership and control of the activities of its operating subsidiaries.

Thus, we will not be able to give a more definite view of the Company's status until we receive additional information from the Company. We are taking active steps to obtain this information from the Company with a view toward further analysis and an additional reply to Chairman Staggers.

JUL 14 1970



SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

SEP 16 1970
SEP 18 1970

Honorable Harley O. Stagers, Chairman
 Special Subcommittee on Investigations
 Committee on Interstate and Foreign Commerce
 Room 2323, Rayburn House Office Building
 House of Representatives
 Washington, D. C. 20515

Re: Pennsylvania Company
 File No. 132-3

Dear Mr. Chairman:

In my letter of July 15, 1970, attaching a memorandum of our Division of Corporate Regulation dated July 14, 1970, which you acknowledged on July 16, 1970, I stated that our staff was taking active steps to obtain additional information from Pennsylvania Company in order to be able to express a more definite view of the company's status under the Investment Company Act of 1940.

In this connection, I am enclosing a supplemental memorandum of the staff of our Division of Corporate Regulation which concludes that it appears that Pennsylvania Company is able to rely on the exclusion provided by Section 3(c)(9) of the Investment Company Act for a company subject to regulation under the Interstate Commerce Act.

Sincerely,

Hamer H. Budge
 Chairman

Enclosure

MEMORANDUM OF THE DIVISION OF CORPORATE REGULATION,
SECURITIES AND EXCHANGE COMMISSION, IN RESPONSE TO
LETTER DATED JULY 1, 1970, FROM HONORABLE HARLEY O.
STAGGERS

In his letter, Chairman Staggars asked for a brief opinion as to whether Pennsylvania Company ("Company") may be an investment company within the meaning of Section 3(a)(1) of the Investment Company Act of 1940 ("Act") and, if so, whether it should be so registered with the Commission.

Our previous memorandum of July 14, 1970 stated our tentative view, based on the limited information then available to us, that there was a question as to the status of the Company under the Act which we were unable to resolve without further information and that we were taking active steps to get that information from the Company.

As Chairman Staggars knows, Section 3(c)(9) provides an exclusion from the definition of investment company for

"any company subject to regulation under the Interstate Commerce Act, or any company whose entire outstanding capital stock is owned or controlled by such a company: Provided, that the assets of the controlled company consist substantially of securities issued by companies which are subject to regulation under the Interstate Commerce Act."

The section establishes two criteria, with the satisfaction of either one being sufficient to exclude a company from the definition of an investment company. The first criterion excludes a company subject to regulation under the Interstate Commerce Act, and the second excludes a company controlled by a company subject to such regulation where the assets of the subsidiary company consist substantially of securities of issuers which are themselves subject to such regulation.^{1/} Our memorandum of July 14, 1970 was written on the

^{1/} For a more detailed discussion, see the staff's memorandum accompanying Chairman Budge's letter to Chairman Staggars of August 21, 1970 regarding Alleghany Corporation.

assumption implicit in Chairman Staggers' letter of July 1, 1970, that the Company was relying on the second exclusion afforded by Section 3(c)(9) of the Act for a company whose entire stock is owned or controlled by a company subject to regulation under the Interstate Commerce Act.

Counsel for the Company advises us, however, that the Interstate Commerce Commission ("ICC") in 1942 in Finance Docket No. 13235, Wabash Railroad Company Control 247 I.C.C. 365, 252 I.C.C. 319, ordered that the Company be considered as a carrier subject to the provisions of Section 20(1) to (10), inclusive, and Section 20a(2) to (11), inclusive, of the Interstate Commerce Act. The ICC's authority to subject the Company to regulation under the Interstate Commerce Act, we understand, is contained in Section 5(3) of that Act. Thus, counsel for the company asserts that it is excluded from the provisions of the Act pursuant to the first criterion for exclusion afforded by Section 3(c)(9).

In the course of our inquiry, we also learned that in March 1970, the Company disposed of its controlling position in Wabash Railroad Company ("Wabash") upon which the 1942 order was predicated. When we learned of that divestment we asked the Company and the ICC whether the 1942 order was still in effect and whether, absent control of Wabash by the Company, the Company continues to be subject to the plenary jurisdiction of the ICC.

Both the General Counsel of the ICC and counsel for the Company replied (copies attached) to the effect that the disposition by the Company of its controlling stock ownership in Wabash did not of itself have any effect upon the 1942 order cited above which expressly provided that:

" . . . unless and until otherwise ordered by this Commission, said Pennsylvania Company shall be considered as a carrier subject to the provisions of Section 20(1) to (10), inclusive, and Section 20a(2) to (11), inclusive, of the Interstate Commerce Act. . . ."

The ICC has not "otherwise ordered."

There may be a question as to whether a company ordered by the ICC to be considered as a carrier subject to the Interstate Commerce Act but no longer factually entitled to carrier status may rely upon the exclusion from Investment Company Act status provided in Section 3(c)(9) of the Act (cf. Hoover v. Allen 241 F. Supp. 213 (S. D. N. Y. 1965)). However, it is not necessary to decide that question in this case.

Both the General Counsel of the ICC and counsel for the Company point out that while the Company no longer controls the Wabash, it remains in control of Detroit, Toledo & Ironton Railroad Company and the Toledo, Peoria and Western Railroad Company,^{2/} both common carriers by railroad. Accordingly, the Company asserts that since it now is - for both reasons of procedure and substance - a carrier subject to ICC's jurisdiction under Section 20a of the Interstate Commerce Act, it clearly follows that it remains excluded from the coverage of the Investment Company Act by reason of Section 3(c)(9) thereof.

Based on the foregoing, it appears that Pennsylvania Company is able to rely on the exclusion provided by Section 3(c)(9) of the Act for a company subject to regulation under the Interstate Commerce Act.

SEP 15 1970

2/ Toledo, Peoria & Western Railroad Company Control, 295 I.C.C. 523 (1957).

Interstate Commerce Commission

OFFICE OF THE GENERAL COUNSEL

Washington, D.C. 20423

FRK:chl

August 6, 1970

Mr. Solomon Freedman, Director
 Securities and Exchange Commission
 Division of Corporate Regulation
 Washington, D. C. 20549

RECD. SEC.

AUG 1 01970

Re: Pennsylvania Company
File No. 132-3

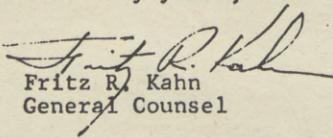
Dear Mr. Freedman:

This is in reply to your letter of August 3, 1970, concerning the Pennsylvania Company, a company which is not a carrier but has been designated by the Interstate Commerce Commission to be a carrier for certain purposes under the provisions of section 5(3) of the Interstate Commerce Act.

As I thought I had explained to Mr. Lewis J. Mendelson, Senior Special Counsel of your Division, when we spoke on the telephone on July 23, 1970, the status of a holding company such as this does not depend upon its remaining in control of those carriers, the acquisition of which led to its designation as a carrier under the statutory provisions. Thus, although the Pennsylvania Company may no longer control the Wabash Railroad Company, it remains in control of the Detroit, Toledo and Ironton Railroad Company and the Toledo, Peoria and Western Railroad Company, among other carriers. Accordingly, the Pennsylvania Company continues to be a carrier under section 5(3) of the Act, in the absence of Commission action to the contrary. A similar construction of the law recently was sustained in Sandor Schwartz v. Allegheny Corp., 282 F. Supp. 161 (S.D. N.Y. 1968).

If I can be of further cooperation and assistance, I should be pleased to oblige.

Sincerely yours,


 Fritz R. Kahn
 General Counsel

SECURITIES AND EXCHANGE COMMISSION

RECEIVED

AUG 11 1970

DIVISION OF CORPORATE REGULATION



PENN CENTRAL

REC'D S.E.C.

AUG 13 1970

DAVID L. WILSON
GENERAL ATTORNEY
LEGAL DEPARTMENT
SIX PENN CENTER PLAZA
PHILADELPHIA, PA. 19104

August 11, 1970

Mr. Solomon Freedman
Director
Division of Corporate Regulation
Securities and Exchange Commission
Washington, D.C.

SECURITIES AND EXCHANGE COMMISSION
RECEIVED

Re: Pennsylvania Company
Your File No. 132-3

AUG 13 1970

Dear Mr. Freedman:

This will respond to your letter of August 3, 1970, concerning the status of Pennsylvania Company under various provisions of the Interstate Commerce Act. You ask that I give you my further opinion on this matter in three specified respects.

In my judgment the disposition by Pennsylvania Company of its controlling stock ownership in Wabash Railroad Company did not by itself have any effect upon the Order issued by the Interstate Commerce Commission in 1942 in Finance Docket No. 13235. As the enclosed copy shows, that Order expressly provided that:

"...unless and until otherwise ordered by this Commission, said Pennsylvania Company shall be considered as a carrier subject to the provisions of Section 20(1) to (10), inclusive, and Section 20a(2) to (11), inclusive, of the Interstate Commerce Act..."

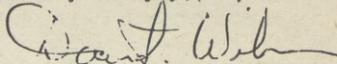
Since the I.C.C. has not "otherwise ordered," it is my view that the situation remains unchanged since the date of the 1942 Order. (See Louisville & Jeffersonville Bridge and Railroad Company, Etc. 290 I.C.C. 725, 732-733 (1955).)

PENN CENTRAL TRANSPORTATION COMPANY

You next inquire as to my opinion on any additional factual or legal considerations which might affect the jurisdiction of the I.C.C. in the case of Pennsylvania Company. As you are undoubtedly aware Pennsylvania Company remains in substantially total control of Detroit, Toledo & Ironton Railroad Company which is a common carrier by railroad. In addition, the I.C.C. in (Toledo, Peoria & Western Railroad Company Control, 295 I.C.C. 523 (1957)) authorized Pennsylvania Company to exercise joint control over the Toledo, Peoria & Western Railroad Company along with the Santa Fe. Accordingly, Pennsylvania Company remains in fact a non-carrier which has been authorized by Order of the I.C.C. to acquire control over two or more carriers through ownership of their capital stock.

Finally, you request my view on whether Pennsylvania Company under all of the facts applying can be regarded as excluded from the definition of an investment company pursuant to the Investment Company Act of 1940. Since it has been shown above that Pennsylvania Company now is - for both reasons of procedure and substance - a carrier subject to I.C.C.'s jurisdiction under Section 20a of the Interstate Commerce Act, it clearly follows that it remains excluded from the coverage of the Investment Company Act by reason of Section 3(c)(9) thereof.

Very truly yours,



David L. Wilson
General Attorney

DLW:mak
Enc.

ORDER

At a Session of the INTERSTATE COMMERCE COMMISSION, Division 4,
held at its office in Washington, D. C., on the 28th day of April, A. D. 1942.

Finance Docket No. 13235

WABASH RAILROAD COMPANY CONTROL

Upon consideration of the supplemental application of The Pennsylvania Railroad Company and the Pennsylvania Company, and further consideration of the record in this proceeding, and said division having, on July 29, 1941, made and filed a report, and on the date hereof, a supplemental report, containing its findings of fact and conclusions thereon, which reports are hereby referred to and made a part hereof:

It is ordered, That acquisition by The Pennsylvania Railroad Company and the Pennsylvania Company of control of the Wabash Railroad Company through ownership of its capital stock, and indirect control thereby of the subsidiary companies of the Wabash Railroad Company specified in said report of July 29, 1941, upon the terms and conditions in that report found just and reasonable, be, and it is hereby, approved and authorized: Provided, however, and this authorization is granted subject to the express condition, that until and unless otherwise authorized by this Commission, The Pennsylvania Railroad Company shall maintain or cause to be maintained joint rates, joint routes, interchange points, and channels of trade through gateways of the Wabash Railroad Company as they existed under operation of the properties of the Wabash Railway Company at the date of said previous report.

It is further ordered, That, unless and until otherwise ordered by this Commission, said Pennsylvania Company shall be considered as a carrier subject to the provisions of section 20(1) to (10), inclusive, and section 20a(2) to (11), inclusive, of the Interstate Commerce Act, applicable to the Pennsylvania Railroad Company and the Wabash Railroad Company: Provided, That as to applicability of said provisions of section 20 and section 20a to said Pennsylvania Company this order shall take effect and be in force on and after the date hereof, except that as to the provisions of section 20 pertaining to reports, it shall be deemed effective as of January 1, 1942.

It is further ordered, That, within 10 days after execution of the trust agreement to be made between the Pennsylvania Company and the Fidelity-Philadelphia Trust Company, and Thomas H. McMerny, and the Indenture to be made between the Wabash Railroad Company and the Marine Midland Trust Company of New York, respectively, a verified copy of said agreement or said indenture, in the form in which it was executed, shall be filed with this Commission by the carrier party thereto.

It is further ordered, That The Pennsylvania Railroad Company, the Pennsylvania Company, or the Wabash Railroad Company, as the case may be,

shall report to this Commission all pertinent facts concerning the termination of all or any part of any trust created by the said agreements or indentures by sale of the stock or otherwise, within 10 days after such termination.

And it is further ordered, That nothing herein is to be construed as authorizing the sale or other disposition of said stock, or any change in the trustees under said indentures, without previous authorization from this Commission.

By the Commission, division 4.

(SEAL.)

W. P. BARTEL,

Secretary.

USE OF PROCEEDS

The net proceeds from the sale of the Debentures offered hereby, estimated at \$ _____, will be used by Pennco (i) to purchase from Railroad all of the outstanding stock of Manor Real Estate Company ("Manor") and Despatch Shops, Inc. ("DSI") including Railroad's open account advances to Manor, at the book net worth of such companies (\$26.3 million and \$16.8 million, respectively) and the face amount of such advances (\$24.1 million), all as of March 31, 1970, (ii) to reimburse its treasury for the purchase from Railroad on March 31, 1970, of all of the outstanding stock of Clearfield Bituminous Coal Company ("CBC") at the book net worth of such company (\$16.9 million) and (iii) subject to approval of the Interstate Commerce Commission, to purchase a \$ _____ million note of Railroad with the same maturity date as, and a higher interest rate than, the Debentures and with installments of principal comparable in percentage of principal and dates to the sinking fund payments applicable to the Debentures. See "Business—Companies Being Purchased from Railroad". Pending receipt of the proceeds from the sale of the Debentures, up to \$50 million may be borrowed by Pennco from banks and either loaned to one of Railroad's subsidiaries to repay advances previously made to it by Railroad or applied to the purchase of Manor or DSI. Any such borrowings will be repaid upon the sale of the Debentures.

Funds provided to Railroad by Pennco have been used in the past and may continue to be used by Railroad as a source of cash. During 1970 Railroad has budgeted capital expenditures of approximately \$100 million (exclusive of equipment acquisitions, all of which are separately financed) and has maturities of long-term indebtedness aggregating \$106 million, exclusive of indebtedness of others guaranteed by Railroad. It is expected that the funds to provide for such capital expenditures, long-term debt maturities and other cash requirements will be provided from the proceeds of the Debentures offered hereby, short-term indebtedness (in addition to renewals or extensions of existing short-term debt) and long-term financing to be provided either by Pennco or from other sources, including, to the extent realized, any cash generated by the operations of Railroad. Reference is made to the loss incurred by Railroad in the first quarter of 1970 set forth under "Business—Railroad Operations". For further information concerning the financial condition of Railroad and its parent, Penn Central, reference is also made to the financial statements included herein generally and specifically to the Statement of Consolidated Source and Application of Funds of Penn Central, to Note 10 to the Financial Statements of Penn Central and to the scheduled maturities of long-term debt in Note 7 to the Financial Statements of Penn Central. While various plans for meeting the future financial requirements of Railroad are under consideration, no specific plans have been adopted and no commitments have been obtained. The participation of Pennco in meeting these requirements may be limited, as indicated above, by the requirement to maintain Net Tangible Assets (as defined) at 300% of funded debt and the restrictions on the amount of dividends it may pay and against further Railroad Investments (as defined) unless Non-Rail Assets (as defined) equal or exceed 250% of funded debt. See "Description of Debentures—Certain Covenants".

At May 8, 1970, Railroad had outstanding \$152.1 million of commercial paper pursuant to orders of the Interstate Commerce Commission authorizing up to \$200 million of such paper. To the extent that commercial paper outstanding has been less than \$200 million, Railroad has borrowed under a \$50 million bank line of credit. As additional backing for its commercial paper Railroad has available \$50 million under the Credit Agreement referred to under "Introduction". Between April 21, 1970 (the day preceding the announcement of the operating results of Railroad for the three months ended March 31, 1970) and May 8, 1970, maturities and payments of commercial paper exceeded sales of commercial paper by \$41.3 million. Of the commercial paper outstanding at May 8, 1970, approximately \$75 million matures prior to June 30, 1970, and the balance at various dates to December 16, 1970.

Since December 31, 1969 a subsidiary of Penn Central has borrowed, with the guarantee of Penn Central, approximately \$59 million in Swiss francs, bearing an average interest rate of approximately 10.1% and maturing approximately one year from date of issue, and such funds were indirectly made available to Railroad.

(From Washington Post, May 29, 1970)

Penn Central Postpones Bond Sale

From News Dispatches

Penn Central Co., which operates the world's largest privately-owned railroad, announced yesterday it was postponing next week's sale of \$100 million in debentures for its Pennsylvania Co. subsidiary.

No reason was given, but spokesmen for the Penn Central said representatives were working on alternate means of financing.

The offering had been scheduled for June 2 through a group of underwriters managed by First Boston Corp., Glore Forgan Staats Inc. and Salomon Bros. & Hutzler.

The bonds were to be 25-year maturity and were to carry a 10½ per cent coupon. There had been some speculation in the financial community that the company would have difficulty selling the bonds, even at that high rate.

Pennsylvania Co. had planned to use net proceeds of the sale to purchase from Penn Central Transportation Co., another subsidiary that operates the railroad properties, securities it holds in Manor Real Estate Co., Clearfield Bituminous Coal Co. and Dispatch Shops, Inc. These three firms are primarily engaged in non-railroad activities.

Meanwhile bond prices continued firm in generally light retail activity.

Tax-exempt dealers said their sector is better as two major offerings that came Wednesday attracted good retail buying.

(From Washington Post May 13, 1970)

Penn Central Defends Solvency, Vows Growth

By William H. Jones

Washington Post Staff Writer

PHILADELPHIA, Pa., May 12—Penn Central board chairman Stuart H. Saunders vigorously defended the solvency of his company today at the annual stockholder's meeting here.

Saunders said he and other officers had no intention to "pursue liquidation of our company, but to do everything in our power to fulfill the great potential of the corporation."

Responding to a suggestion by Mrs. Wilma Sess of New York, chairman of a group of 100 stockholders and a veteran attendee of annual meetings, that come Wall Street sources feared for the transportation-based holding company's future, in view of "heavy" debts, Saunders said:

"Obviously, no organization can continue to lose money on such a scale as we have experienced the last year or so," but he pledged management to work at making Penn Central solvent, to make it grow and to make it prosper. Saunders said the company, with \$8 billion in assets, had a debt of about \$2.5 billion.

In the first quarter of 1970, Penn Central lost \$17.2 million compared to a net income of \$1.6 million the previous year. He told shareholders who have not received dividends for the last two quarters and whose shares today fell to a post-merger low of 15 1/4 on the New York Stock Exchange, down 2 1/2 points, Saunders and the company's new president, Paul A. Gorman, had little encouraging news.

The new president, who came to Penn Central five months ago from Western Electric Company, where he also was president, conceded he was "unhappy" about the "unsatisfactory performance" of the company. Moreover, he indicated the task of reversing a declining trend takes a long

AAR Says Profits Worst Since 1861

The Association of American Railroads this week told the Interstate Commerce Commission that earnings reports for the first quarter of 1970, "by far the worst since the recession year of 1861," made urgent railroad requests for a 6 per cent increase in freight rates.

Dr. Burton N. Behling, vice president for finance of the AAR, said in a statement filed with the ICC that net rail operating income plunged from \$142 million during the first quarter last year to \$50 million this year. The ICC opens oral hearings on the rate request here May 20.

time. About 700 persons filled an auditorium at Philadelphia Civic Center for the meeting, which lasted more than three hours.

In large measure, company officers indicated today, a turn-around in Penn Central's fortunes rests primarily on two potential actions by the United States government:

• Railroad passenger service in the nation has reached a "crisis point," Saunders said, affecting Penn Central more than any other company. He called for swift House action

on the bill recently passed in the Senate to establish a private corporation to run intercity passenger trains. In each year since the Feb. 1, 1963 merger of the Pennsylvania and New York Central railroads, Saunders told the stockholders, the company lost more than \$100 million on passenger operations, "a dominant factor in keeping our railroad in the red."

• Saunders said he was "quite confident" the Interstate Commerce Commission wants to "keep this industry strong and viable" and thus would approve, effective June 2, a new across-the-board 6 per cent increase in pay rates. Hearings on the new rates, which Saunders said today would bring his company \$75 to \$90 million a year in additional revenues, open next week in Washington.

To emphasize the urgency Saunders feels over rail passenger operations, he asked all stockholders today to contact immediately members of the House Interstate and Foreign Commerce Committee, headed by Rep. Harley O. Staggers (D-W.Va.) and to urge passage of the rail corporation bill.

Responding to stockholder's questions, Saunders said Penn Central would not pay dividends until earnings improved. The company paid \$1.80 per share during 1969 but dropped dividends for the last quarter of 1969 and the first quarter of 1970. A number of retired stockholders noted today they rely on dividend payments as a major income source.

Mr. LISHMAN. I would like to address this question to the representative of the ICC. Is it correct that the Penn Central Co., a Delaware corporation, is the parent holding company which owned a hundred percent of the Penn Central Transportation Co., the operating company which runs the railroad?

TESTIMONY OF DALE W. HARDIN, VICE CHAIRMAN, INTERSTATE COMMERCE COMMISSION; FRITZ R. KAHN, GENERAL COUNSEL, ICC; RICHARD B. SMITH, COMMISSIONER, SECURITIES AND EXCHANGE COMMISSION; PHILIP A. LOOMIS, JR., GENERAL COUNSEL, SEC; AND IRVING M. POLLACK, DIRECTOR, DIVISION OF TRADING AND MARKETING

Mr. HARDIN. Yes, that is correct, Mr. Lishman.

Mr. LISHMAN. Is it also correct that the transportation company owns 100 percent of the voting stock of the Pennsylvania Co. which is the investment company subsidiary with substantial holdings in stocks of both transportation and nontransportation companies and real estate, both railroad and nonrailroad real estate?

Mr. HARDIN. That is correct.

Mr. LISHMAN. Now you have before you, I believe, a printed copy of a prospectus dated April 27, and filed April 29, 1970, with the ICC by the Pennsylvania Co. covering an issue of \$100 million sinking fund debentures due 1995? Will you please summarize how this prospectus was processed by the ICC?

Mr. KAHN. Mr. Lishman, this was part of an application filed by the Pennsylvania Co. for Commission authorization under section 20(a) of the Interstate Commerce Act to make this security issue. The information submitted by the applicant was incomplete, and the application was never fully processed by the Commission or its staff.

Mr. LISHMAN. Was it commented on?

Mr. KAHN. At no time was it commented on by the Commission.

Mr. LISHMAN. In what respect was it incomplete?

Mr. KAHN. As you will note on the face, Mr. Lishman, among other things, the percentage of interest to be paid was not filled in, and the details of the proposed issue were never furnished the Commission. And, as you well know, Mr. Lishman, that the inquiries by the company indicated that the issue would not be received by the financial community and it was that information, the receptivity of the issue, that was never transmitted to the Commission.

Mr. LISHMAN. In other words, among other thing, as I understand it, the underwriters were not named in the prospectus as organizationally filed.

Mr. KAHN. There evidently were none that were willing to underwrite the issue.

Mr. LISHMAN. Now, is it correct that an amended prospectus was filed by the Pennsylvania Co. with the ICC on May 12, 1970? You have a copy of that before you, I think.

Mr. KAHN. We simply have exhibit 4, Mr. Lishman.

Mr. LISHMAN. Do you know whether or not such an amended prospectus was filed on May 12?

Mr. KAHN. We will accept that, but it would contain the same lack of complete information.

Mr. HARDIN. I am informed, Mr. Lishman, that we have copies of the amended circular but that it was never filed.

Mr. MACDONALD. Could I interrupt? If it was not filed, how did you get a copy of it?

Mr. HARDIN. This is Mr. Matthew Paolo, Director of our Bureau of Accounts.

**STATEMENT OF MATTHEW PAOLO, DIRECTOR, BUREAU OF
ACCOUNTS, INTERSTATE COMMERCE COMMISSION**

Mr. PAOLO. During the examination of accounts and records of the Penn Central Transportation Co. we obtained a copy of this document but it has never officially or it had never been officially filed with the Commission.

Mr. MACDONALD. Well, just for continuity could you tell us what date you first saw it?

Mr. PAOLO. I could not tell you.

Mr. MACDONALD. If you cannot, you can furnish it later.

Mr. PAOLO. I will furnish it later.

(See app. A, p. 137.)

Mr. LISHMAN. Is it correct that the May 12 prospectus was substantially identical with that filed on April 27 except that it did include the names of underwriters?

Mr. PAOLO. If you are addressing that to me, I have not examined it that closely.

Mr. LISHMAN. Could you furnish that information for the record?

Mr. PAOLO. I will.

(See app. A, p. 137.)

Mr. DINGELL. Mr. Chairman, could we have copies of the two documents filed with the committee for purposes of inclusion in the record?

Mr. LISHMAN. We have a copy of it.

Mr. DINGELL. Would it be appropriate that it be inserted at this point?

Mr. MACDONALD. Without objection, so ordered.

Mr. KAHN. The document will speak for itself.

(Packet III follows:)

PACKET III

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TABLE I.CHRONOLOGY OF SIGNIFICANT DATES

February 26	Financial statements published for the year ended December 31, 1969
March 26	Request filed with ICC for approval of \$100 million debt offering; no financial statements included at this time
April 22	Penn Central announced 1st quarter consolidated loss of \$17,229,000 (railroad by itself lost \$62.7 million)
April 29	Prospectus, with financial statements for year ended December 31, 1969, filed with ICC covering debt offering
May 12	Amended prospectus with some financial statements filed with ICC; annual meeting of stockholders at which Saunders, Penn Central's Chairman, promised to avoid liquidation
May 19*	Meeting between Saunders and Treasury Secretary Kennedy at which time Saunders advised Kennedy that bankruptcy was imminent without governmental assistance
May 27	Meeting of Board of Directors at which the cancellation of the public offering was authorized followed by a meeting of Finance Committee at which the causes for cancellation were further discussed
May 28	Announcement of withdrawal of public offering which was scheduled to have taken place on June 2
June 1	Saunders' pay increased 18% to \$279,000
June 8	Saunders and Bevan (Chairman of Finance Committee) ousted; Gorman becomes new chairman and chief executive
June 22	Petition for reorganization under Bankruptcy Act filed by the Penn Central Transportation Company in the United States District Court in Philadelphia

*Neither the facts of this meeting nor the subject matter discussed were publicly disclosed until after the filing of the Bankruptcy Petition in June.

NINETY-FIRST CONGRESS

SPECIAL SUBCOMMITTEE ON INVESTIGATIONS

HARLEY O. STAGGERS, W. VA., CHAIRMAN

SAMUEL H. FRIZDEL, MD.
 TORBERT F. MADDONATY, MASS.
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 LIONEL VAN DERLIN, CALIF.
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WILLIAM L. SPRINGER, ILL.
 SAMUEL L. DEVINE, OHIO
 ANCHER NELSEN, MINN.
 HASTINGS KEITH, MASS.
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 JAMES T. BROVHILL, N.C.
 JAMES HARVEY, MICH.

ROBERT W. LIEMMAN
CHIEF COUNSEL

Congress of the United States
 House of Representatives

Special Subcommittee on Investigations of the
 Committee on Interstate and Foreign Commerce
 Room 2323, Rayburn House Office Building

Washington, D.C. 20515

July 2, 1970

Honorable Hamer H. Budge
 Chairman
 Securities and Exchange Commission
 Washington, D. C.

Dear Mr. Chairman:

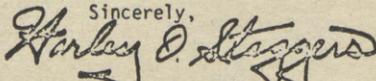
This Committee is currently conducting public hearings involving, among other things, the Penn Central Company and its various subsidiaries including the Penn Central Transportation Company which operates the railroad and is now in reorganization pursuant to the Bankruptcy Act. The Penn Central Company, which is the parent holding company, owns 100% of the outstanding stock of the Transportation Company. The Transportation Company owns 100% of the outstanding common stock of the Pennsylvania Company.

The common stock and debentures of the Penn Central Company, the debentures of the Penn Central Transportation Company, and the preferred stock and debentures of the Pennsylvania Company are listed for trading on the New York Stock Exchange. During the period May 15 to June 15, 1970, the short interest in Penn Central stock on the Exchange increased more than 300%. At the same time, the market values of all the securities of these issuers have declined substantially.

To assist the Committee in fulfilling its oversight responsibilities it is requested that the staff of your Commission conduct a market study of the trading in all the securities involved for the period May 1, 1970 to June 26, 1970. Please make available to this Committee as soon as possible copies of the responses of the various brokers to your inquiry. Copies of the ownership reports filed for the months of May and June 1970 for all three companies are also requested. Any comments you or your staff may wish to make after analyzing the data obtained could be submitted when available and would be most helpful.

Your cooperation with the Committee in this matter will be greatly appreciated.

Sincerely,



HARLEY O. STAGGERS
 CHAIRMAN

TABLE II

SALES OF PENN CENTRAL STOCK THROUGH SELECTED BROKERS

BROKER	Mar 30 Apr 3	1/ May 11-15	2/ May 18-22	3/ May 25-29	June 1-5	Mar 30 - Jun 26
Butcher & Sherrerd*	21,100	175,000	202,900	6,500	6,400	506,900
Salomon Bros.*	-----	63,900	12,600	1,600	-----	471,400
Goldman Sachs*	-----	4,900	62,100	153,600	1,100	432,500
Shields & Co.	200	200	5,200	169,900	300	192,800
Pershing & Co.	1,900	400	3,900	92,100	14,400	162,600
Wm. O'Neill & Co.	-----	-----	11,300	149,200	-----	160,500
Loeb, Rhoades*	800	2,700	23,600	10,000	11,400	120,200
Lehman Bros.*	-----	2,000	81,600	1,300	-----	101,600
Mitchum, Jones	-----	35,400	28,100	9,700	-----	91,100
E. F. Hutton*	4,400	3,000	20,900	1,500	3,700	77,900
Hayden, Stone*	1,900	7,300	10,300	25,600	7,300	74,200
Drexel, Harriman*	300	3,600	31,000	10,800	5,000	53,000
Subtotal	30,600	298,400	493,500	631,800	49,600	2,444,700
All Others	64,400	61,600	61,800	119,900	504,200	4,282,500
Total volume	95,000	360,000	555,300	751,700	553,800	6,727,200

1/ Example of normal volume

2/ Week of Meeting between Saunders and Kennedy (May 19)

3/ Debt offering cancelled on Thursday and large public selling began on Friday (May 29)

* Member of underwriting group

TABLE IV

SIGNIFICANT SALES BY BANKS AND OTHERS REPRESENTED ON BOARD OF DIRECTORS OF PENN CENTRAL

SELLER	April 27-	May 4-8	May 11-15	May 18-22	May 25-29	June 1-5	Total	
	May 1						June 23	
Chase Manhattan Bank	2,700	9,900	1,000	124,000	152,300	15,200	412,000	412,000
Chase Fund (3)	-----	-----	60,000	-----	-----	-----	60,000	60,000
Morgan Guaranty	11,500	1,000	-----	4,800	44,900	150,200	264,700	264,700
Provident National Bank (4)	6,200	-----	2,000	6,200	3,000	8,408	37,833	37,833
Alleghany Corporation	-----	-----	-----	-----	96,000	-----	96,000	96,000
Investors Diversified Service	-----	13,900	36,500	67,500	133,700	-----	251,600	251,600
Trustees, University of Pa. (5)	-----	-----	3,000	91,700	-----	-----	104,700	104,700

INSTITUTION

INDIVIDUAL OF PENN CENTRAL BOARD

CHASE MANHATTAN BANK

Stuart T. Saunders

MORGAN GUARANTY

John T. Dorrance, Jr.
Thomas L. Perkins

PROVIDENT NATIONAL BANK

David C. Bevan
John M. Seabrook

ALLEGHANY CORPORATION

Fred M. Kirby (resigned Penn Central 3/25/70).
Carlos J. Routh (resigned Penn Central 3/25/70).
Daniel E. Taylor (resigned Alleghany 3/23/70).

(1) Week of meeting between Saunders and Kennedy.
(2) Debt offering cancelled on Thursday, May 28, and large public selling began on Friday.
(3) Relationship, if any, to Chase Manhattan Bank unknown.

(4) Provident National Bank sold through at least 20 different brokers.

(5) David C. Bevan was Financial Vice President of Penn Central and a director of Provident National Bank. Gaylord P. Harnwell, new Chairman of the Board of Penn Central, was a director of Penn Central and a trustee of the University.

NINETY-FIRST CONGRESS

ROBERT W. LEHRMAN
CHIEF CLERK

SPECIAL SUBCOMMITTEE ON INVESTIGATIONS

HARLEY G. TAGGERT, W. VA., CHAIRMAN

JACQUES H. FETTER, ILL.
ROBERT H. FORTMAYOR, MASS.
RONI J. JIMAN, CALIF.
JOHN E. MOORE, CALIF.
JOHN D. SPENCER, MICH.
PAUL G. HONORS, FLA.
JONEL VAN DERLIN, CALIF.
L. J. PICKLE, TENN.

WILLIAM L. SPRINGER, ILL.
SAMUEL L. DAVIS, OHIO
ANGUS NELSON, MONT.
MARTINUS KEITH, MASS.
GLENN QUINN-FISHER, MONT.
JAMES T. BROVILL, N.C.
JAMES HARVEY, MICH.

Congress of the United States
House of Representatives

Special Subcommittee on Investigations of the
Committee on Interstate and Foreign Commerce
Room 2323, Rayburn House Office Building
Washington, D.C. 20515

July 27, 1970

Honorable Hamer H. Budge
Chairman
Securities and Exchange Commission
Washington, D. C.

Dear Mr. Chairman:

This is in reference to Investment Company Act Release Number 6117 regarding the application of Alleghany Corporation, a registered non-diversified closed-end management investment company, pursuant to Section 8(f) of the Investment Company Act of 1940 for an order declaring that Alleghany has ceased to be an investment company, as defined by the Act. I note that Alleghany first registered under the Act on November 1, 1940. On October 4, 1945 its registration was terminated by Commission order because as a result of its acquisition of control of Chesapeake and Ohio Railway Company it

"had become subject to regulation under the Interstate Commerce Act and had thus ceased to be an investment company by reason of Section 3(c)(9) of the Act which excludes from the definition of investment company any company subject to regulation under the Interstate Commerce Act."

As a result of investments made thereafter, on April 10, 1968, Alleghany again registered under the Act. On April 30, 1970, pursuant to the order of the Interstate Commerce Commission the corporation became an operating motor carrier.

Alleghany is now asserting in its current application that it

"has ceased to be an investment company within the meaning of the Act by reason of Section 3(c)(9) which excludes from the definition of investment company any company subject to regulation under the Interstate Commerce Act."

In the staff memorandum you forwarded to me on July 15, 1970, it was indicated that the exemption provided by Section 3(c)(9) of the Investment Company Act was intended to be available only if substantially all the investment company's investments were made in carriers regulated by the Interstate Commerce Commission. This would appear to be a necessary conclusion. Otherwise, it would appear that the provisions of the Act could be readily evaded through the device of including an operating motor or rail carrier in the investments made by the investment company.

As you have gathered from my letter of July 1, 1970, the Committee is concerned about the applicability of the Investment Company Act to conglomerate holding companies which have transportation companies as components. Testimony of officials of the Interstate Commerce Commission has been given to this and other Congressional Committees that the ICC lacks regulatory jurisdiction beyond the component transportation company. I would also like to point out that, as I understand, the ICC claims it lacks jurisdiction to regulate non-carrier investments of regulated transportation companies. This would appear to mean, for example, that while the Penn Central Transportation Company is subject to regulation, its parent holding company, Penn Central Company, and its investment company subsidiary, Pennsylvania Company, are not so subject. In light of this testimony, the question is raised whether the granting of an order pursuant to Section 8(f) exempting Alleghany from the provisions of the Investment Company Act would be in accordance with the public interest and with the intent of Congress in creating an exemption for investment companies which are fully regulated by the Interstate Commerce Commission. Certainly, if the testimony of the officials of that Commission is accepted, then investors in investment companies regulated by the Interstate Commerce Commission would receive far less protection than is assured by your Commission to investors in other investment companies.

Of course, I am sure that in its consideration of the merits of the application, your Commission will also consider the fact that Alleghany Corporation controls Investors Diversified Services. As of December 31, 1969, approximately one-half of Alleghany's investments in corporate securities was represented by its investment in I.D.S.

To assist this Committee in determining whether adequate regulatory controls exist under present law or whether legislative changes may be called for, you are requested for a full report on the nature and extent of the application of Alleghany, the basis for the exemption, if granted, and what regulatory controls of the ICC over the entire Alleghany Corporation complex you may determine are sufficient in the public interest and for the protection of the investors. To assist you and your staff in evaluating this matter, I am enclosing a copy of a Committee print regarding regulatory controls of the Interstate Commerce Commission over the conglomerate mergers.

Your attention to this request will be appreciated.

Sincerely,

HARLEY O. STAGGERS
CHAIRMAN

(Investment Company Act Release No. 6117)

ADMINISTRATIVE PROCEEDING
FILE NO. 3-2536UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
July 16, 1970

<hr/>	
In the Matter of	:
	:
ALLEGHANY CORPORATION	:
	:
350 Park Avenue	:
New York, New York 10022	:
	:
(811-1635)	:
	:
Investment Company Act of 1940	:
<hr/>	

NOTICE OF FILING OF
APPLICATION FOR ORDER
PURSUANT TO SECTION 8(f) OF
THE ACT DECLARING COMPANY
HAS CEASED TO BE AN INVESTMENT
COMPANY

NOTICE IS HEREBY GIVEN that Alleghany Corporation ("Applicant"), a Maryland corporation registered as a non-diversified, closed-end management investment company under the Investment Company Act of 1940 ("Act"), has filed an application pursuant to Section 8(f) of the Act for an order declaring that Applicant has ceased to be an investment company as defined by the Act. All interested persons are referred to the application on file with the Commission for a statement of the representations contained therein, which are summarized below.

Applicant was organized on January 26, 1929, and first registered under the Act on November 1, 1940 as a closed-end non-diversified management investment company. On June 5, 1945, Applicant was authorized by the Interstate Commerce Commission ("ICC") to acquire control of the Chesapeake & Ohio Railway Company ("Ohio") and, indirectly, of its subsidiary carriers. On October 4, 1945, Applicant's registration under the Act was terminated by Commission order because Applicant, having acquired Ohio had become subject to regulation under the Interstate Commerce Act and had thus ceased to be an investment company by reason of Section 3(c)(9) of the Act which

excludes from the definition of investment company any company subject to regulation under the Interstate Commerce Act. In 1955 Applicant was authorized by the ICC to acquire control of the New York Central Railroad Company ("Central") and affiliates, continuing Applicant's status as a company subject to regulation under the Interstate Commerce Act.

Applicant states that after the merger of Central and the Pennsylvania Railroad Company on February 1, 1968, Applicant considered itself to continue to hold carrier status as such status had not been revoked by the ICC and also considered itself still subject to regulation under the Interstate Commerce Act and thus excluded from the definition of investment company by reason of Section 3(c)(9). Applicant also, however, considered itself to be no longer in control of a carrier. Applicant registered as a non-diversified closed-end management investment company on April 10, 1968. Applicant states that it registered under the Act to eliminate such uncertainty, if any, as might have existed as to its status as a company subject to regulation under the Interstate Commerce Act and to eliminate any possibility of liability for doing business as an unregistered investment company.

Applicant states that it entered into an agreement dated September 4, 1968, as amended September 27, 1968, pursuant to which it acquired 99.07% of the outstanding common stock and 100% of the outstanding 5% Cumulative Preferred Stock of Jones Motor Co., Inc. ("Jones"), a Pennsylvania motor common carrier, and agreed subject to Interstate Commerce Commission approval, to merge a new subsidiary of Applicant with Jones. All shares of Jones common and preferred stock were deposited in a voting trust with Marine Midland Grace Trust Company of New York as independent voting trustee. The merger agreement between Applicant, its subsidiary and Jones provided for the acquisition by Applicant of the motor carrier operating rights and most of the assets and liabilities of Jones contingent upon ICC approval thereof.

Applicant states that its intention to assume motor carrier status and to apply for an order terminating its status as a registered investment company was disclosed in a Form N-8B-1 Registration Statement filed pursuant to the Act on September 9, 1968. Applicant further states that

the Registration Statement provided, among other things, that Applicant could invest in companies for the purpose of exercising control or management. Applicant states that on April 25, 1969, its stockholders approved an amendment to Applicant's Articles of Restatement of Charter to permit Applicant to engage in business as a motor carrier and authorized it, by a vote of 6,096,937 common shares and 170,190 preferred shares in favor, and 8,803 common shares and 245 preferred shares against, to cease to be an investment company for purposes of the Act.

On January 27, 1970, the ICC authorized Applicant to acquire the operating rights and property of Jones and its subsidiary, Erie Trucking Company. Applicant states that on April 30, 1970, pursuant to the order of the Interstate Commerce Commission, it consummated its acquisition of Jones and thereby became an operating motor carrier.

Applicant asserts that, by virtue of the order of the ICC and the subsequent acquisition of the operating rights and property of Jones, Applicant has become subject to regulation under the Interstate Commerce Act as a motor carrier. Applicant further asserts that it, therefore, has ceased to be an investment company within the meaning of the Act by reason of Section 3(c)(9) which excludes from the definition of investment company any company subject to regulation under the Interstate Commerce Act. Applicant states it is now subject to all provisions of Part II of the Interstate Commerce Act including, inter alia, the securities provisions of Section 214.

Section 8(f) of the Act provides, in pertinent part, that when the Commission, upon application, finds that a registered investment company has ceased to be an investment company, it shall so declare by order, and upon the taking effect of such order, the registration of such company shall cease to be in effect.

NOTICE IS FURTHER GIVEN that any interested person may not later than August 4, 1970, at 5:30 p.m., submit to the Commission in writing a request for a hearing on the matter accompanied by a statement as to the nature of his interest, the reason for such request and the issues of fact or law proposed to be controverted or he may request that he be notified if the Commission should order a hearing thereon. Any such communication

should be addressed: Secretary, Securities and Exchange Commission, Washington, D. C. 20549. A copy of such request shall be served personally or by mail (air mail if the person being served is located more than 500 miles from the point of mailing) upon Applicant at the address stated above. Proof of such service (by affidavit or in case of an attorney-at-law by certificate) shall be filed contemporaneously with the request. At any time after said date, as provided by Rule 0-5 of the Rules and Regulations promulgated under the Act, an order disposing of the application herein may be issued by the Commission upon the basis of the information stated in said application, unless an order for hearing upon said application shall be issued upon request or upon the Commission's own motion. Persons who request a hearing or advice as to whether a hearing is ordered will receive notice of further developments in this matter, including the date of the hearing (if ordered) and any postponements thereof.

For the Commission, by the Division of Corporate Regulation, pursuant to delegated authority.

Orval L. DuBois
Secretary



SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

AUG 21 1970

Honorable Harley O. Stagers, Chairman
Special Subcommittee on Investigations
Committee on Interstate and Foreign Commerce
Room 2323, Rayburn House Office Building
House of Representatives
Washington, D. C. 20515

Dear Mr. Chairman:

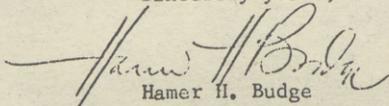
In your letter of July 27, 1970, which the Commission previously acknowledged, you asked us for a full report on the nature and extent of an application by Alleghany Corporation ("Alleghany") pursuant to Section 8(f) of the Investment Company Act of 1940 ("Act") requesting an order that Alleghany had ceased to be an investment company; the basis for the order, if granted; and what regulatory controls of the Interstate Commerce Commission ("ICC") over the entire Alleghany complex the Commission deemed sufficient in the public interest and for the protection of investors. As supplemental information you provided a copy of a Committee print regarding regulatory controls of the Interstate Commerce Commission over conglomerate mergers.

The attached memorandum illustrates that Alleghany, as a company subject to regulation under the Interstate Commerce Act, would be entitled, under the present law, to the order requested. In this regard, you state that you understand that the ICC asserts that it lacks jurisdiction to regulate non-carrier investments of ICC regulated transportation companies. The SEC traditionally limits its comments to issues arising under the federal securities laws. Thus we express no opinion with respect to the question you raise of the jurisdictional limits of the ICC. In connection with the securities laws, however, the non-carrier investments of Alleghany would be subject to the reporting and protective requirements of the Investment Company Act, but for the exclusion provided by Section 3(c)(9).

The Commission remains of the opinion that investors in companies such as Alleghany are entitled to the protections of the Investment Company Act. To make such protections available, however, will require a statutory amendment, at least along the lines previously recommended and as discussed in the attached memorandum.

I am sure you appreciate that under our present jurisdictional limits the Commission has virtually no discretion in this matter. Accordingly, the Commission issued the requested order today.

Sincerely yours,



Hamer H. Budge
Chairman

(Investment Company Act Release No. 6168)

ADMINISTRATIVE PROCEEDING
FILE NO. 3-2336UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
August 21, 1970

In the Matter of	:
ALLEGHANY CORPORATION	:
350 Park Avenue	:
New York, New York 10022	:
(811-1635)	:
Investment Company act of 1940	:

ORDER PURSUANT TO SECTION
8(f) OF THE ACT DECLARING
COMPANY HAS CEASED TO BE AN
INVESTMENT COMPANY

The Commission on July 16, 1970, issued a notice (Investment Company Act Release No. 6117) of an application filed by Alleghany Corporation ("Alleghany") for an order, pursuant to Section 8(f) of the Investment Company Act of 1940 ("Act"), declaring that Alleghany has ceased to be an investment company as defined in the Act.

The notice gave interested persons an opportunity to request a hearing and stated that an order disposing of the application might be issued upon the basis of the information stated therein. No request for a hearing has been filed and the Commission has not ordered a hearing.

The Commission has considered the matter and finds that the facts set forth in the application establish that Alleghany has ceased to be an investment company. Alleghany itself has acquired the motor carrier operating rights, the assets and the liabilities of Jenco Motor Co., Inc. By virtue of this acquisition Alleghany has been adjudicated to be a carrier by the Interstate Commerce Commission ("ICC") and by order is subject to the ICC's plenary jurisdiction under the Interstate Commerce Act. Accordingly, Alleghany is excluded from the definition of investment company by reason of Section 3(c)(9).

Accordingly, it is hereby ordered, pursuant to Section 8(f) of the Act, that the registration of Alleghany Corporation under the Act shall forthwith cease to be in effect.

By the Commission.

Orval L. DuBois
Secretary

MEMORANDUM OF THE DIVISION OF CORPORATE REGULATION,
 SECURITIES AND EXCHANGE COMMISSION, IN RESPONSE TO
 LETTER DATED JULY 27, 1970 FROM HONORABLE HARLEY O. STAGGERS

On October 30, 1969, the Commission sent to Chairman Staggers a memorandum of the Division of Corporate Regulation entitled "Possible Dual Regulatory Status Of Investment Company - Carriers." This memorandum stated, inter alia, that: Alleghany was attempting to simplify its regulatory status by acquiring and operating a motor carrier, Jones Motor Co.; that Alleghany had filed at least three applications with the Interstate Commerce Commission ("ICC"); that if the ICC granted Alleghany's applications and subjected Alleghany to its plenary jurisdiction under Sections 5(2), 5(3), 20, 20(a), 12(1) or comparable sections of the Interstate Commerce Act Alleghany intended to file an application with the Commission pursuant to Section 8(f) of the Investment Company Act of 1940 ("Act") to terminate its status as an investment company; and that the Commission would consider that under present law, Alleghany was "subject to regulation by the Interstate Commerce Commission" within the meaning of Section 3(c)(9) of the Act, and, a fortiori, excluded from the definition of an investment company. (Memorandum pp. 2-4, 7.) The 18 page memorandum discussed the background of Alleghany as an investment company, as a carrier, and the questions raised by Alleghany Corporation v. Breswick & Co. et al.^{1/}

^{1/} 353 U.S. 151 (1957); 355 U.S. 415 (1958). Cf. Hoover v. Allen, 241 F. Supp. 213 (S.D.N.Y. 1965).

On July 16, 1970 a notice was published of the filing of an application by Alleghany requesting an order pursuant to Section 8(f) of the Act declaring that Alleghany had ceased to be an investment company.^{2/} In his letter, Chairman Staggers requests a full report on the nature and extent of Alleghany's application, the basis for the exemption, if granted, and what regulatory controls of the ICC over the entire Alleghany complex the Commission determines to be sufficient in the public interest and for the protection of investors.

The following facts, all of which are matters of record, appear from Alleghany's application.

Alleghany, a Maryland corporation, was organized on January 26, 1929, and first registered under the Act on November 1, 1940 as a closed-end, non-diversified, management investment company. On June 5, 1945, Alleghany was authorized by the ICC to acquire control of the Chesapeake & Ohio Railway Company ("Ohio") and, indirectly, of its subsidiary carriers.^{3/} On October 4, 1945, Alleghany's registration under the Act was terminated by Commission order because Alleghany,^{4/} having acquired Ohio, had become subject to regulation under the Interstate Commerce Act, and had thus ceased to be an investment company by reason of Section 3(c)(9) of the Act which excludes from the definition of investment company any company subject to regulation under the Interstate Commerce Act. In 1955 Alleghany was authorized by the ICC to acquire control of the New York Central Railroad

^{2/} Investment Company Act Release No. 6117.

^{3/} C & O Ry. Co. - Purchase, 261 I.C.C. 239 (1945)

^{4/} Alleghany Corporation, 20 SEC 731 (1945); Investment Company Act Release No. 809.

Company ("Central") and its affiliates, thereby continuing Alleghany's status as a company subject to regulation under the Interstate Commerce Act.^{5/}

After the merger of Central and the Pennsylvania Railroad Company on February 1, 1968, Alleghany considered itself to continue to hold carrier status as such status had not been revoked by the ICC and also considered itself still subject to regulation under the Interstate Commerce Act and thus excluded from the definition of investment company by reason of Section 3(c)(9). Alleghany also, however, considered itself to be no longer in control of a carrier. Accordingly, Alleghany registered as a closed-end, non-diversified, management investment company on April 10, 1968. Alleghany's registration statement stated Alleghany was registering under the Act to eliminate any uncertainty that might exist as to its status as a company subject to regulation under the Interstate Commerce Act and to eliminate any possibility of liability for doing business as an unregistered investment company.

On September 4, 1968 Alleghany entered into an agreement (as amended September 27, 1968) pursuant to which it made a tender offer for and ultimately acquired 99.07% of the outstanding common stock and 100% of the outstanding 5% Cumulative Preferred Stock of Jones Motor Co., Inc. ("Jones"), a Pennsylvania motor common carrier, and agreed, subject to Interstate Commerce Commission approval, to merge a new subsidiary of Alleghany, Alleghany Trucking Company, Inc. ("Trucking"),

^{5/} Louisville & J.B. & R. Co. Merger, 290 I.C.C. 725, aff'd., 295 I.C.C. 11(1955).

with Jones. All shares of Jones common and preferred stock were deposited in a voting trust with Marine Midland Grace Trust Company of New York as independent voting trustee. The merger agreement between Alleghany, Trucking and Jones provided for the acquisition by Alleghany of the motor carrier operating rights and most of the assets and liabilities of Jones contingent upon ICC approval.

Alleghany's intention to assume motor carrier status and to apply for an order terminating its status as a registered investment company was disclosed in a Form N-8B-1 Registration Statement filed pursuant to the Act on September 9, 1968. Alleghany's Registration Statement provided, among other things, that Alleghany could invest in companies for the purpose of exercising control or management. Alleghany's stockholders, at their annual meeting on April 25, 1969, approved an amendment to Alleghany's Articles of Restatement of Charter to permit it to engage in business as a motor carrier and at the same meeting authorized it, by a vote of 6,096,937 common shares and 170,190 preferred shares in favor, and 8,803 common shares and 245 preferred shares against, to cease to be an investment company for purposes of the Act.

On January 27, 1970, the ICC authorized Alleghany to acquire the operating rights and property of Jones and its subsidiary, Erie ^{6/} Trucking Company. Pursuant to the order of the I.C.C., Alleghany on

6/ Alleghany Corporation - Control and Purchase - Jones Motor Co. Inc. - and Control Erie Trucking Company, 109 M.C.C. 333 (1970). Alleghany's total investment in Jones was \$28,838,315. On December 31, 1969, Alleghany's assets totaled \$174,428,160. Thus Alleghany's investment in Jones represented, on an unconsolidated basis, approximately 16% of its total assets if taken at years-end, 1969, and approximately 12.5% of total assets on a consolidated basis.

April 30, 1970, consummated its acquisition of Jones; transferred the motor carrier operating rights, assets and liabilities of Jones to itself; and thereby it became an operating motor carrier licensed by the I.C.C.

Based on the above facts on May 22, 1970, Alleghany filed an application pursuant to Section 8(f) of the Act requesting an order of the Commission declaring that Alleghany has ceased to be an investment company and that its registration has ceased to be in effect. Section 8(f) of the Act provides that:

"Whenever the Commission, on its own motion or upon application, finds that a registered investment company has ceased to be an investment company, it shall so declare by order and upon the taking effect of such order the registration of such company shall cease to be in effect. If necessary for the protection of investors, an order under this subsection may be made upon appropriate conditions. The Commission's denial of any application under this subsection shall be by order."

Should an order issue pursuant to Section 8(f), Alleghany would be deemed to be a company other than an investment company, and the Act would be inapplicable to it. Alleghany would thus be free from both the reporting requirements of the Act and the unique prophylactic protections the Act affords to investors.

In asserting the appropriateness of such an exemptive order, Alleghany relies exclusively on Section 3(c)(9) of the Act which provides an exclusion from the definition of investment company for

"any company subject to regulation under the Interstate Commerce Act, or any company whose entire outstanding capital stock is owned or controlled by such a company: Provided, that the assets of the controlled company consist substantially of securities issued by companies which are subject to regulation under the Interstate Commerce Act."

In effect, Section 3(c)(9) establishes two criteria, with the satisfaction of either one being sufficient to exclude a company from the definition of an investment company. The first criteria excludes a company subject to regulation under the Interstate Commerce Act, and the second excludes its controlled companies the assets of which consist substantially of securities of issuers which are themselves subject to such regulation. The legislative history of Section 3(c)(9) elucidates this double thrust of the Section.

Generally speaking, it is the purpose of the Act to subject to its regulation all "large liquid pools of the public's savings" which have been entrusted to others for investment. In this regard, the Act provides for the registration and regulation of any company which falls within the definition of an investment company. Section 3(a)(1) of the Act defines as an investment company any company which is primarily engaged, or holds itself out as being primarily engaged, in the business of "investing, reinvesting, or trading in securities." To cover situations in which such primary engagement is not readily apparent because the company is either directly, or through controlled companies, engaged in an industrial or other business together with investing in securities, Section 3(a)(3) raises the presumption of an investment company if, among other things, more than 40 percent of the company's assets consist of securities other than those of

^{7/} Hearings before a Subcommittee of the Committee on Banking and Currency, United States Senate, on S. 3580 (76th Congress, 3d Sess.), p. 33, (hereinafter referred to as 1940 Senate Hearings).

majority-owned subsidiaries.

Section 3(b)(2) provides a means for rebutting the presumption raised by Section 3(a)(3) upon a showing that the company is primarily engaged in a business or businesses other than that of an investment company. In this regard, the original bill, S. 3580, contained no counterpart of Section 3(c)(9), as the exemptive provisions of Section 3(b)(2) were considered sufficiently broad to have made unnecessary any specific exemption or exclusion. Thus counsel for the Commission stated to the Congress that Section 3(b)(2) would "fortify the exemption of companies which are essentially industrial corporations or railway companies which may have a substantial part of their assets ^{8/} in marketable securities. (emphasis added).

Despite the stated intention of Section 3(b)(2), the Association of American Railroads submitted to Congress a "clarifying" amendment which was the precursor of present Section 3(c)(9). The Association's proposal would have provided an exclusion from the definition of investment company to "any company subject to regulation under the Interstate Commerce Act and any company whose entire out-^{9/}standing capital stock is owned or controlled by such company."

^{8/} 1940 Senate Hearings, p. 177.

^{9/} 1940 Senate Hearings, pp. 776-777. It is interesting to note that while Section 3(b)(2) apparently was concerned only with railway companies and the Association represented only Class I Railroads, their proposal provided an exclusion for all ICC regulated carriers.

Section 3(c)(9) as passed by Congress, however, added a caveat to the second clause of the proposal and thus excluded, first, any company subject to regulation under the Interstate Commerce Act, and second, its controlled companies the assets of which consist substantially of securities of issuers which are themselves ^{10/} subject to such regulation. In this regard Alleghany relies on ^{11/} the first exclusion afforded by the Section.

^{10/} See Hearings before a Subcommittee of the Committee on Interstate and Foreign Commerce, House of Representatives, 86th Cong., 1st Sess. 1959), p. 404. (Hereinafter referred to as 1959 House Hearings). See also Sen. Rep. No. 1775, 76th Cong., 3d Sess., (1940), p. 13 and H.R. Rep. No. 2639, 76th Cong., 3d Sess., (1940), p. 12 both of which indicate that if a controlled company, or in other words, a company to which the first exclusion is not available, wishes to avail itself of the second exclusion of Section 3(c)(9), the controlled company must have substantially all of its assets in ICC regulated issuers. The word "all", however, does not appear in the Section itself. Compare this Congressional intent to that of the Commission draftsmen of the Act, who apparently would have permitted, under a Section 3(b)(2) test, a railway company, i.e., a company relying on the first exclusion, to have a substantial part of its assets in investment securities. (See text accompanying footnote 9).

^{11/} By letter dated July 15, 1970, the Commission sent to Chairman Staggers a memorandum dated July 14, 1970 concerning the applicability of Section 3(a)(1) and the availability of Section 3(c)(9) to the Pennsylvania Company, a wholly-owned subsidiary of the Penn Central Transportation Company. We had previously been under the impression that unlike Alleghany, the Pennsylvania Company was relying on the second exclusion afforded by Section 3(c)(9). It was in this regard that the Commission's memorandum raised the legislative history, applicable only to the second exclusion, indicating that "substantial" was meant to mean "substantially all." The Division of Corporate Regulation is continuing its inquiry regarding the status of the Pennsylvania Company.

As noted above, Alleghany first registered under the Act on November 1, 1940. In 1945, immediately before the Commission terminated Alleghany's registration pursuant to Section 8(f) 86 percent of Alleghany's assets of \$83 million, taking investments at the then current market values, were invested in carriers and only about 5 percent in the securities of noncarrier issuers. Shortly after the termination of its investment company status Alleghany began a program of disposition of its carrier stock and by 1954 had sold all of its railroad securities except its interest in the Missouri Pacific Railroad Company, such interest representing 7% of Alleghany's assets. In 1955, Alleghany acquired control of the New York Central Railroad Co. and by 1959 its interest in carriers amounted to 22 percent of its assets. As Alleghany's remaining assets consisted of investment securities Alleghany fell within the 40 percent presumptive test of an investment company contained in Section 3(a)(3) of the Act.^{12/} However, as Alleghany remained subject to regulation under the Interstate Commerce Act within the meaning of Section 3(c)(9) it was excluded from the Section 3(a)(3) definition of an investment company.

On January 15, 1959, at the Commission's request, then Chairman Oren Harris of the Interstate and Foreign Commerce Committee introduced a bill (H.R. 2481, 86th Cong., 1st Sess.) to amend certain provisions

^{12/} See text accompanying footnote 8. See also 1959 House Hearings, p. 406.

^{13/}
of the Act. Among the provisions of H.R. 2481 was a proposed amendment designed to limit Section 3(c)(9) which the then Commission Chairman, Mr. Gadsby, aptly referred to as "an excuse ---
^{14/}
to escape regulation." In a sectional analysis presented to the Subcommittee, the Commission described the problem with Section 3(c)(9), and indeed the problem with Alleghany, as follows:

"Section 7 - Modification of exception for company to regulation under the Interstate Commerce Act

"Present law - Section 3(c)(9) contains an exception from the act for any company subject to regulation under the Interstate Commerce Act.

"Problem - The intent of Section 3(c)(9) in providing an exception from the Act was to avoid subjecting a railroad or a railroad holding company to dual regulation under both the Interstate Commerce Act and the Investment Company Act. As written the section may be used, and has been used, by companies which are essentially investment companies to escape the more pertinent, if more pervasive, regulation under the Investment Company Act by subjecting themselves to the limited regulation under the Interstate Commerce Act designed for different purposes.

"In fact, regulation by both the SEC and the Interstate Commerce Commission (ICC) of such a company which is primarily an investment company but which is also the holder of railroad securities would involve little, if any, duplication or conflict, and the burdens thereof, if any, would be minimal. It is anomalous that section 3(c)(9) which was designed to protect stockholders of

^{13/} 1959 House Hearings, p. 107. The bill was reported out by the Interstate and Foreign Commerce Committee (H.R. Rep. No. 2178, 80th Cong., 1st sess.), was passed by the House, and transmitted to the Senate. No action was taken thereon by the Senate. S. 1181, the counterpart of the House Bill, was introduced on February 25, 1959, but was never reported out of Committee. See Hearings before a Subcommittee of the Committee on Banking and Currency, United States Senate, 86th Cong., 1st sess. (1959), (hereinafter referred to as 1959 Senate hearings). See also Annual Reports of the Securities and Exchange Commission: 21st Report, 1955 at pp. 101-102; 22nd Report, 1956 at pp. 188- 189; 23rd Report, 1957 at p. 10; and 25th Report, 1959 at p. 11.

^{14/} 1959 House Hearings, p. 140. The Commission also characterized Section 3(c)(9) as a "loophole". 1959 House Hearings, p. 404.

a railroad holding company against possible burdens of dual regulation can be used by the management of the company at its will, even though it is essentially an investment company, to deprive these stockholders of the protections and safeguards of the Investment Company Act.

"The most significant case in point is the Alleghany Corp. matter which is described in the Commission's reports to the Congress for the fiscal years ended 1955 (pp. 101-102), 1956 (pp. 188-189) and 1957 (pp. 165-166). The bulk of the assets of this company has consisted of investment securities, including a large investment in Investors Diversified Services, Inc., an investment company itself which controls or manages, directly and indirectly, \$2½ billion of investors funds. A relatively smaller investment of Alleghany Corp. has been its holdings of New York Central Railroad stock. Because of its control over the railroad, and in connection with a transaction involving the railroad system, Alleghany Corp. was deemed to be a "carrier" and subjected to certain regulation by the ICC under the Interstate Commerce Act. Thus, Alleghany became entitled to an exception from the Investment Company Act although its business by far was, and has been, that of an investment company.

"Remedy in the bill - It is proposed to modify Section 3(c)(9) to provide that the exception shall not apply to a company which the Commission finds and by order declares to be primarily engaged in the business of investing, reinvesting, owning, holding or trading in securities. 15/

15/ Id. at p. 124. The amended section would have excluded from the definition of investment company the following:

"(9) Any company A) which is subject to regulation under the Interstate Commerce Act: Provided, That this exception shall not apply to a company which the Commission finds and by order declares to be primarily engaged, directly or indirectly, in the business of investing, reinvesting, owning, holding, or trading in securities; or (B) whose entire outstanding stock is owned or controlled by a company excepted under clause (A) hereof: Provided, That the assets of the controlled company consist substantially of securities issued by companies which are subject to regulation under the Interstate Commerce Act." (1959 House Hearings, pp. 95, 132).

In testifying on this proposed amendment, Chairman Gadsby noted that the Section 3(c)(9) "loophole" deprived investors in companies such as Alleghany of the more pertinent and appropriate supervision of the Investment Company Act, since the companies need comply only with the more limited type of regulation under the Interstate Commerce Act which was designed for different purposes.^{16/} Chairman Gadsby then noted that dual regulation would involve insubstantial duplication or conflict,^{17/} but that in any event

"it is inappropriate for a corporation which is primarily engaged in the business of investing, reinvesting, owning, holding and trading in investment securities, to be excluded from the Investment Company Act, and that its investors be deprived of the protections and safeguards which Congress has considered essential, simply because the company has acquired, with some small fraction of its assets, common carriers, or to some minor extent directly engaged in the business of an interstate carrier."^{18/}

In view of the above it is clear that the Commission is required to view and apply Section 3(c)(9) as providing an exclusion from the Act for a company subject to the plenary jurisdiction of the ICC such as Alleghany.^{19/} As evidenced by the foregoing, such a view is required by the statutory language of the Act and by the Congressional intent expressed in the Act's legislative history. Concomitantly, the Commission has also recognized, for over a decade, that Section 3(c)(9)

^{16/} 1959 House Hearings, p.140.

^{17/} Ibid. The ICC agreed with this view. 1959 Senate Hearings, pp. 148-149, p. 525.

^{18/} 1959 House Hearings, p. 141.

^{19/} See footnote 1 and the accompanying text. See also the memorandum of October 30, 1969, for a complete discussion of the Breswick litigation, supra.

has afforded companies which are in fact investment companies, a "loophole" from regulation; that this "loophole" is subject to abuse; and that companies which seek to avail themselves of this loophole should be required by Congress to be subjected, in effect, to a vigorous test of proof such as that of Section 3(b)(2). Thus the Commission in 1959 requested the introduction and urged the passage of H.R. 2481 in order to "strengthen the safeguards and protections afforded the public under the securities laws by tightening jurisdictional provisions, ^{20/}and/ correcting certain inadequacies revealed through administrative experience ---." (emphasis added).

Chairman Stagers, in conclusion, has asked what regulatory controls of the ICC would be necessary for the protection of investors. In answer, it should be noted that the Investment Company Act and the Interstate Commerce Act are independently oriented and each has its own point of focus and concern. If Section 3(c)(9) has truncated investor protection, it would seem that the appropriate remedy would be an amendment of that Section to delimit the broad scope of the exclusion it provides. This is the view the Commission advocated in 1959.

20/ 1959 House Hearings, Gadsby, p. 107.

Served February 6, 1970

MF-3080

 INTERSTATE COMMERCE COMMISSION

No. MC-F-10444¹
 ALLEGHANY CORPORATION—CONTROL AND PURCHASE—
 JONES MOTOR CO., INC.—AND CONTROL ERIE TRUCKING
 COMPANY

Decided January 27, 1970

1. In No. MC-F-10444, acquisition by Alleghany Corporation of control of Jones Motor Company, Inc., and its motor carrier subsidiary, Erie Trucking Company, through purchase of capital stock of Jones Motor Company, Inc.; and merger of a wholly owned subsidiary of Alleghany Corporation into Jones Motor Company, Inc.; and subsequently the merger of Jones Motor Company, Inc., into Alleghany Corporation for ownership, management, and operation; and acquisition by Fred M. Kirby and Allan P. Kirby, Jr., individually and as coguardians of the property of Allan P. Kirby, an incompetent, of control of the operating rights and property through the transaction, approved and authorized, subject to conditions.
2. In Finance Docket No. 25686, Jones Motor Company, Inc., authorized to issue not exceeding 100 shares of its common stock, par value \$1.
3. In Finance Docket No. 18656, previous orders of Commission vacated.
4. In No. MC-FC-70907, application dismissed.

David G. Macdonald and M. Lauck Walton for applicants.

Bernard A. Gould and Warren I. Cohn for Bureau of Enforcement.

REPORT OF THE COMMISSION

HARDIN, Commissioner:

Alleghany Corporation, a holding company with total assets in excess of \$200 million, is at present subject to dual regulation under the Investment Company Act and the Interstate Commerce Act (act). It seeks, by a series of transactions hereinafter discussed, to become a motor common carrier subject to the plenary jurisdiction of the Interstate Commerce Commission under part

¹This report also embraces Finance Docket No. 25686, Jones Motor Co., Inc., Stock; Finance Docket No. 18656, Louisville & Jeffersonville Bridge and Railroad Company, Merger, Etc.; and No. MC-FC-70907, Alleghany Corporation, Transferor, Jones Motor Company, Inc., Transferor.

II of the act. Although it is alleged that the proposed transactions, if consummated, would result in a termination of Alleghany's position as major investor and participant in the management of railroads and a shift of this great wealth and managerial experience to the motor carrier industry, no party, government agency or department, or carrier has intervened in support or in opposition to the proposed transaction. In order to prevent the important considerations involved in the subject transactions being decided on an unopposed record, we directed our Bureau of Enforcement to participate as a party in the title and embraced proceedings for the purpose of developing the record.

By a petition filed October 14, 1968, in Finance Docket No. 18656, Louisville and Jeffersonville Bridge and Railroad Company, Merger, Etc., Alleghany Corporation (Alleghany), of New York, N. Y., seeks to vacate orders of the Commission, dated March 2, 1955, and May 24, 1955, holding Alleghany, by virtue of its control of the New York Central Railroad Company, was to be considered as a carrier subject to certain provisions of the Interstate Commerce Act, as amended, to the same extent that those provisions are applicable to the New York Central Railroad Company and its carrier subsidiaries and affiliates.

By an application filed October 29, 1968, in No. MC-FC-70907, under section 212(b) of the act, Alleghany and Jones Motor Company, Inc. (Jones), of Spring City, Pa., a common carrier by motor vehicle subject to part II of the Interstate Commerce Act, seek authority for the transfer of the operating rights of the latter to the former.

By a second application filed April 9, 1969, as amended, in No. MC-F-10444, Alleghany seeks authority under section 5 of the Interstate Commerce Act to acquire control of Jones and its subsidiary Erie Trucking Company (Erie), also of Spring City, through the purchase of the capital stock of Jones. Alleghany also seeks to merge a wholly owned subsidiary of itself into Jones and subsequently the operating rights and properties of Jones into Alleghany for ownership, management, and operation. By the same application, Fred M. Kirby, also of New York, and Allan P. Kirby, Jr., of Morristown, N. J., individually and as coguardians of the property of Allan P. Kirby, an incompetent, seek authority under section 5 of the act to acquire control of the operating rights and property through the transaction.

By a separate application filed May 15, 1969, in Finance Docket No. 25686, as a matter directly related to the above proceedings

109 M.C.C.

Jones seeks authority to issue 100 shares of its common stock, par value \$1.

By separate orders of division 3, dated January 24, 1969, in Finance Docket No. 18656, and No. MC-FC-70907, the Bureau of Enforcement (Bureau) was directed to participate as a party in the proceedings for the purpose of developing the record. By order dated August 14, 1969, it was likewise ordered to participate in No. MC-F-10444 and Finance Docket No. 25686. By the same order, the matters in all the above-numbered proceedings were consolidated for consideration and resolution. The matters were ordered handled under modified procedure. In so ordering the division also requested the parties discuss the following issues: (1) whether Alleghany controls or has the power to control Penn Central Company (Penn Central), as the percentage of stock held by a person, where less than a majority, is nondeterminative of the issue of control, *Chemical Leaman Tank Lines, Inc.—Pur.—Ryder*, 104 M.C.C. 686, 707; (2) whether Alleghany is affiliated with Penn Central within the meaning of section 5(6) of the act and, if so, whether the acquisition would enable such a rail carrier to use such service by motor vehicle to public advantage in its operations and not unduly restrain competition; (3) whether the authority for Alleghany to acquire the operating rights of Jones is properly sought under section 212(b) of the act; (4) whether the acquisition of control of Jones and its affiliates by Alleghany under section 5(2) of the act is consistent with the public interest, in view of the representation by Alleghany that the primary purpose for the acquisition of Jones, and its affiliates, is to enhance its tax position, and to insure Alleghany's continued regulation by this Commission; and (5) whether, under section 5, Commission approval of the proposed transaction is required in view of the fact that the transaction may involve only a noncarrier and a carrier and its subsidiaries, which carrier and its subsidiaries may comprise a single established system, *Louisville & J. B. & R. Co. Merger*, 295 I.C.C. 11, hereinafter sometimes referred to as the *Louisville case*, and *Kansas City Southern Industries, Inc., Control*, 317 I.C.C. 1, 4.

Jones, under a certificate issued in No. MC-4963 and sub-numbered proceedings, as described in the application, is authorized to operate, in interstate or foreign commerce, as a motor common carrier of general commodities, with exceptions, over regular routes extending between Chicago, Ill., St. Louis, Mo., and Fort Madison, Iowa, on the west, and Nashua, N. H., Boston,

Mass., Providence, R. I., New York, N. Y., Philadelphia, Pa., and Baltimore, Md., on the east, via such principal intermediate points as Detroit, Mich., Toledo, Akron, and Cleveland, Ohio, Pittsburgh, Harrisburg, and Allentown, Pa., Trenton and Jersey City, N. J., Hartford, Conn., and Worcester, Mass.; and between Harrisburg and Baltimore and Bristol, Va., and Charlotte, N.C., via Harrisburg, Lynchburg, and Martinsville, Va., and High Point, N. C.

Erie, as described in the application, under a certificate issued in No. MC-23135 is authorized to operate, in interstate or foreign commerce, as a motor common carrier (1) of general commodities, with exceptions, over regular routes, between Buffalo, N. Y., and Erie, Pa., and between Erie and New York, N. Y., serving the intermediate point of Kane, Pa., and various off-route points; and (2) over irregular routes, of general commodities, between Erie, on the one hand, and, on the other, points in New York and in Pennsylvania within 80 miles of Erie, excluding Buffalo and Bradford, Pa., and between Kane, on the one hand, and, on the other, points in Pennsylvania within 80 miles of Erie, excluding the same two Pennsylvania points.

By an order dated November 17, 1969, in No. MC-F-10553, Jones Motor Co., Inc.—Merger—Erie Trucking Company and No. MC-4963 (Sub-No. 32), Jones Motor Co., Inc., Review Board No. 5 authorized the merger of the operating rights and property of Erie into Jones for ownership, management, and operation, and the acquisition by Marine Midland Grace Trust Company (Marine Midland), of New York, as voting trustee, of control of the operating rights and property through the transaction. By the same order certain irregular-route authority of Erie is to be converted to regular-route authority. The transaction has not been consummated.

Pursuant to authority granted under section 5(2) of the act on October 6, 1969, in No. MC-F-10328, Jones Motor Co., Inc.—Control and Merger—Mitchell's Express, Review Board No. 5 authorized acquisition by Jones of control of Mitchell's Express (Mitchell), of Portsmouth, N.H., merger of the operating rights and property of the latter into the former for ownership, management, and operation, and acquisition by Marine Midland of control of the operating rights and property through the transaction. Mitchell operates under a certificate issued in No. MC-16020, in interstate or foreign commerce as a motor common carrier of general commodities, with exceptions, over regular routes, between Boston, and Ogunquit, Maine, serving intermediate and

off-route points, and roadbuilding material, over irregular routes, between Swampscott, Mass., on the one hand, and, on the other, points in Strafford and Rockingham Counties, N.H. This transaction has also not yet been consummated.

Pursuant to authority granted under section 210a(b) of the act on August 5, 1968, in No. MC-F-10190, Jones Motor Co., Inc.—Purchase—Medill Transfer, Inc., as extended by order of December 18, 1968, Jones leased the operating rights of Medill Transfer, Inc., William H. Christison, Trustee in Bankruptcy (Medill), of East Peoria, Ill. Medill, under a certificate of registration issued in No. MC-99996 (Sub-No. 1), is authorized to operate as a motor common carrier of general commodities within a 50-mile radius of Allentown, Ill., and to transport such property to or from any point outside such authorized area of operations for a shipper or shippers within such area. Vendee commenced operations under the lease on September 3, 1968. The 5(2) application of Jones to purchase Medill was approved on December 12, 1969, by operation of law.

Penn Central operates as a rail common carrier generally on the east from Montreal, Canada, through Boston to Norfolk, Va., and on the west, from Mackinaw City, Mich., through Chicago to St. Louis.

Alleghany proposes to acquire control of Jones and its subsidiaries through purchase of the capital stock of Jones, and thereafter to merge a newly formed, wholly owned subsidiary of Alleghany, Alleghany Trucking Company (Trucking), into Jones, and, further, transfer to Alleghany, Jones' cash and receivables, prepaid items, franchises and operating rights, and the stock of its subsidiaries. Alleghany will assume substantially all of the current liabilities of Jones, while Jones retains essentially its revenue equipment and real property as well as its revenue equipment obligations. Alleghany proposes that it will become a motor carrier subject to part II of the act operating in interstate commerce through its Jones Motor Division and wholly owned subsidiary, Erie Trucking Company.

By letter agreement dated September 4, 1968, Alleghany agreed to make a tender offer of \$21 per common share and \$100 plus accrued dividends per preferred share of capital stock of Jones and certain stockholders of Jones agreed to sell their shares pursuant to the tender offer. Alleghany agreed to purchase tendered shares if at least 51 percent of outstanding shares of Jones were tendered. Shares purchased were to be deposited with a voting trustee, Marine Midland.

By an agreement dated September 26, 1968, between Alleghany and Marine Midland, Marine Midland agreed to accept all stock tendered through the above tender offer in order for Alleghany to avoid any question under section 5 of the act. Marine Midland was then to exercise all stockholders' rights as to the stock deposited to take any action necessary to protect the shares of stock. The shares are to be released upon surrender of the voting trust certificates delivered to Alleghany, accompanied by a certificate requesting release and certifying one or more of the following: (1) that the shares to be released have been sold to one or more persons not affiliated with Alleghany; (2) that an opinion has been rendered by counsel for Alleghany that assumption of control of Jones by Alleghany would not violate the act; (3) that an order has been issued by the Commission terminating its order of March 2, 1955, in *Louisville & J. B. & R. Co. Merger, supra*; or (4) that an order has been issued by the Commission approving release of such shares for any reason whatsoever.

By a letter agreement dated September 27, 1968, Trucking would be merged into Jones with Jones as the surviving corporation. Pursuant to the merger plan, the 100 shares of Trucking's \$0.01 par stock will be converted into 100 shares of Jones' newly issued common stock of \$1 par value. The \$99 excess will be charged to Jones' additional paid-in capital. Alleghany will surrender without consideration to Jones the shares of common stock of Jones held by Alleghany or its voting trustee. These shares will be converted into additional paid-in capital by Jones. The remaining shares of Jones held by minority stockholders will be converted into the right to receive \$21 per share. Trucking will transfer to Jones an amount to satisfy this obligation. Further, Jones will purchase from Alleghany and retire its outstanding preferred stock. Alleghany will waive payment and these preferred shares will also be converted into additional paid-in capital by Jones. As of January 10, 1969, 605,715 shares, or 98.19 percent of the outstanding shares of common stock, and all of the 3,356 outstanding shares of preferred stock of Jones were acquired by the voting trustee for Alleghany.

In related Finance Docket No. 25686, Jones is seeking authority under section 214 of the act for the issuance of 100 shares of \$1 par value common stock. Such 100 shares, as previously mentioned, will be issued to Alleghany in conversion for all of the 100 outstanding shares of Trucking. Upon completion of the proposed control and purchase, Alleghany will hold the 100 shares of the

newly issued common stock of Jones, and Jones will have no other capital stock outstanding.

One of the primary reasons presented by Alleghany for acquisition of the operating rights of Jones is to lessen its tax burden. Such burden arises from the fact that Allan P. Kirby, as of February 28, 1969, was the beneficial owner of 4,084,813 shares, or 56.21 percent of the outstanding common stock of Alleghany. Alleghany is, therefore, for Federal income tax purposes, considered a personal holding company since one person (less than 5 individuals) owns more than 50 percent of its stock and has "personal holding income," (60 percent or more of adjusted gross income consists of dividends and interest) and is therefore subject to a 70-percent penalty tax on the "undistributed personal holding income." Alleghany does not want to distribute all such income to avoid the tax. With Alleghany the recipient of the operating revenue generated by its Jones Motor Division, it alleges it would be an operating company rather than a holding company for Federal tax purposes. It could then retain and reinvest net earnings and would not be subject to the 70-percent penalty tax.

Evidence of past operations by Jones under its operating rights is reflected in an abstract of shipments showing all shipments transported in January 1969. The traffic handled consisted of a wide variety of commodities, showing service to points throughout Jones' authority.

In its verified statement filed on October 1, 1969, Alleghany stated that as of February 1, 1968, the date of the Penn Central merger authorized by the Commission in *Pennsylvania R. Co.—Merger—New York Central R. Co.*, 327 I.C.C. 475, Alleghany received and still holds 196,195 shares or 0.81 percent of the 24,104,708 shares outstanding of Penn Central stock. In addition, Allan P. Kirby, controlling stockholder of Alleghany, received and presently holds 390,130 shares or 1.62 percent of the outstanding Penn Central shares. Combining their interests, Alleghany and Kirby together own 2.43 percent of the outstanding Penn Central stock. Alleghany's shares in Penn Central are held in its own name but the Kirby shares are among those held in the name of Sigler and Company.

Alleghany is also the controlling shareholder of Investors Diversified Services, which serves as an investment advisor and distributor for a group of mutual funds. As of September 30, 1969, these mutual funds held 391,900 shares or 1.63 percent of the outstanding shares of Penn Central. It is alleged investment

decisions for these funds are made solely by their investment committees, over which Alleghany and the Kirby family exercise no control or power to control.

Included in the verified statements was a list of the 30 largest stockholders of Penn Central as of April 3, 1969. From this it can be seen that the 2.43 percent held by Alleghany and Kirby together would make the Kirby interests the second largest shareholders in Penn Central, the largest being the trustees of the New York, New Haven & Hartford Railroad Company which owns 950,-116 shares, or 3.94 percent of the total outstanding shares. If, however, the shares held by Alleghany, Kirby, and Investors Diversified are totaled, the combined holding of 4.06 percent of Penn Central stock exceeds that owned by the trustees of the New York, New Haven & Hartford Railroad Company.

By application filed April 28, 1969, in Finance Docket No. 25660, *Penn Central Holding Company—Acquisition of Control—Penn Central Company*, dismissed August 7, 1969, for lack of jurisdiction, it was shown that Penn Central Holding Company (Holding), a noncarrier, was to acquire control of Penn Central and subsidiaries effective October 1, 1969. Holding has a 14-member board of directors, 1 of which is Fred M. Kirby, president and chairman of the board of Alleghany. Three directors of Alleghany, namely, Messrs. Fred M. Kirby, Daniel E. Taylor, and Carlos J. Routh, serve on the 22-member board of directors of Penn Central, now the transportation operating company.

Three members of the Alleghany board of directors, Messrs. Fred M. Kirby, Carlos J. Routh, and Charles T. Hill, serve on the 14-man board of directors of Pittston Company. Mr. Routh is vice chairman of the Pittston board. Pittston Company was found by the Commission in *Pittston Co.—Control—Brink's, Inc.*, 75 M.C.C. 345, to be a carrier subject to the act under section 5(3). Two large motor carriers, Brink's, Inc., and United States Trucking Company, holding extensive authority issued by the Commission, are under the control of Pittston. In addition, Pittston controls a Canadian carrier, Direct Winters Transport Limited, which carrier holds limited Commission authority.

Mr. Fred M. Kirby, in addition to his other duties, serves as a director of U. S. Industries, Inc. U. S. Industries controls B & P Motor Express, Inc., a carrier operating under a certificate issued by this Commission.

Mr. John J. Burns, a director of Alleghany as well as vice president-financier of Alleghany Corporation, is a director of

Specialized Services, Inc. Specialized Services, Inc., controls Superior Trucking Company, Inc., a carrier operating under a certificate issued by the Commission. Mr. Burns owns 3.3 percent of the voting stock and 1.4 percent of the nonvoting stock of Specialized Services, Inc.

Messrs. Allan P. Kirby, Jr., and Andrew Van Pelt, directors of Alleghany, are directors of the Pittsburgh & Lake Erie Railroad Company, while Mr. Ralph K. Gottshall, a director of Alleghany, serves as director of the Philadelphia, Baltimore and Washington Railroad and the Baltimore and Eastern Railroad Company.

International Utilities, Inc., controls Ryder Truck Lines, Inc., a carrier subject to Commission jurisdiction. Alleghany owns a beneficial interest in 114,200 shares of common stock of International Utilities, Inc. Voting control of these shares is held by The Franklin National Bank. Alleghany also has investments in the securities of other carriers. These investments include a beneficial interest in 20,753 shares of class B capital stock of the Missouri Pacific Railroad Company (MoPac), constituting 52.2 percent of 39,371 shares of such stock outstanding as of December 31, 1968. Alleghany also has a beneficial interest in 2,200 shares of the class A capital stock of MoPac or less than 1 percent of the 1,861,577 shares of such stock outstanding as of December 31, 1968. Voting control of all of Alleghany's MoPac shares is vested in The Franklin National Bank.

The directors of Alleghany, other than Allan and Fred M. Kirby, collectively own, control, or have a beneficial interest in 23,060 shares of Penn Central stock. All of the directors of Alleghany in their individual capacity collectively own, control, or have a beneficial interest in 92,815 shares of Pittston Company, or approximately 2 percent of the outstanding stock.

In response to the issues raised by the order of August 14, 1969, Alleghany argues that neither it nor the Kirby family control nor have the power to control Penn Central. In support of this argument they cite the hearing examiners' report in *Pennsylvania R. Co.—Merger—New York Central R. Co.*, *supra*, at page 639, wherein it is stated that:

*** we do not believe that Alleghany's holdings of 5.8 percent of the outstanding capital stock in the merged company would afford sufficient momentum to obtain control of the proposed company.

It is further contended that if Alleghany had been a controlling party at the time of the above-cited case it would have had to be a

party to the application before the Commission would have had jurisdiction to approve the merger, citing *U. S. v. Marshall Transport Co.*, 322 U.S. 31. With the consummation of the Penn Central merger, it is alleged that the holdings of Alleghany and the Kirby family in Penn Central have decreased, as have their membership and influence on the board of directors. In regard to the question raised by the Commission as to whether Alleghany is affiliated with Penn Central within the meaning of section 5(6) of the act, Alleghany maintains that a mere minority stock ownership or minority representation on the board of directors alone does not give rise to section 5(6) affiliation. Instead, it is argued such relationship ordinarily arises from the existence of a financial or business relationship with the carrier. Alleghany alleges it has no commercial, financial, or other arrangements of any kind with Penn Central, has no control over Penn Central operations, and holds less than 10 percent of the seats on the Penn Central board. It is further alleged that since the investment in Jones is of almost equal value to that Alleghany already has in Penn Central there will be no economic motive to manage one in the interest of the other. If its argument that it is not affiliated with Penn Central within the meaning of section 5(6) is accepted, Alleghany points out the proviso of section 5(2)(b) of the act is not applicable.

As to whether acquisition of control of Jones is consistent with with public interest, Alleghany claims that public interest includes not only direct benefits to the shipping public but also indirect benefits through strengthening of the financial condition of the carrier involved, leading to longrun economies for the public. It is readily admitted the original intention in acquiring Jones was to avoid classification as a personal holding company under the Internal Revenue Code and thus to conserve funds which would otherwise have to be paid under the penalty tax provision. Still, it is argued the funds so saved will be available for improvement of Jones' carrier operations. It is claimed that it is in the public interest to have the union of a company having substantial financial resources with a carrier allegedly having a large need for cash to successfully continue its service. It is alleged that Alleghany's tax savings will make available to Jones approximately \$8,815,000 between 1969 and 1973. This will allow Jones to improve plant and equipment and achieve a growth rate not possible without the help of a company such as Alleghany. In support of its position that it is in the public interest for a company to realize tax savings if passed on to the carrier being acquired, Alleghany cites *Quinn Freight Lines, Inc.—Control and Merger*, 87 M.C.C. 257.

Alleghany turns last to the jurisdictional question concerning whether the Commission has jurisdiction to consider the applications and, if so, whether under section 212(b) or section 5(2) of the act. It is argued that despite the fact Alleghany was ordered in the *Louisville* case to be considered a carrier subject to the provisions of section 20(1) to (10), inclusive, and section 20a(2) to (11), inclusive, of the act, the order constituted Alleghany a carrier only for the purposes enumerated therein and not a carrier within the meaning of sections 5(2) and 5(4) of the act.

It is further argued that the acquisition of Erie by Jones does not alter the situation in that Jones and Erie are an established family of carriers within the meaning of *Woods Industries, Inc.—Control—United Transports, Inc.*, 85 M.C.C. 672. Citing the same case, it is further argued that the change in Alleghany's control of Erie from indirect to direct stock ownership would not result in approval being required under section 5(2). If the two transactions involved are treated separately, Alleghany argues, the acquisition of control of the carriers would not be subject to Commission approval; only the second transaction would fall under section 212(b).

In the alternative, Alleghany argues, if the two described transactions are to be treated as a single transaction it will necessitate section 5(2) approval in that it involves acquisition by a noncarrier of stock control of one carrier and in effect control and merger of a second carrier.

In summary, Alleghany states the jurisdictional problem is one of fact. It prays the Commission find Alleghany does not control Penn Central and grant all relief except that requested in No. MC-FC-70907, which it asks be dismissed. It prays that the termination of the section 5(3) order in Finance Docket No. 18656 be made effective with consummation of the transaction in No. MC-F-10444 when Alleghany will become a carrier.

The verified statement of the Bureau, filed October 30, 1969, briefly summarized the facts previously set forth by Alleghany. Citing the prior decisions of the Commission as to the distinction between control of a single established system and control over nonintegrated systems, the Bureau asks that the Commission find the "single established system" rule was not originally contemplated by Congress, is contrary to Commission practice prior to the *Louisville* case, is an unjustified discrimination in favor of holding companies having single established carrier systems, and is contrary to the public interest of having the

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Commission maintain close supervision over those controlling important sectors of our national transportation system. In the alternative it is argued that section 5(2) would be applicable both because the involved transactions involve alterations in the present structure of Jones and the recent acquisitions by Jones have made alterations in the internal structure of Jones which acquisitions have not been in effect long enough to be fully integrated into the Jones operations. It thus contends that the proposed transactions for acquisition of control by Alleghany over Jones are ones which fall within the purview of section 5 of the act and that the application filed in No. MC-FC-70907 under section 212(b) be dismissed.

DISCUSSION AND CONCLUSIONS

Before we may consider the substantive issues raised by these applications we must determine the jurisdictional question as to whether the applications are to be considered under section 212(b) or section 5(2) of the act. There is no evidence of record that we are here dealing with a single established transportation system to bring the proposed transaction within the rule established in the *Louisville* case. Even if Jones and Erie were to be regarded as constituting a single transportation system the outstanding temporary authority under which Medill is operated would prevent the existence of a single transportation system. Being operated only under a lease, Medill cannot be considered integrated into the Jones or the Jones-Erie system. It is possible, but by no means certain, that if the Jones' application to purchase Medill, filed under section 5(2), is consummated, then the operations under Medill's authority may be integrated with the Jones' operations. In any event, it is premature to consider Medill as part of the Jones "system." It is obvious that Alleghany, upon approval of this application, will succeed Jones in operating Medill under the lease. In so doing it cannot be doubted Alleghany is acquiring two or more carriers and therefore jurisdiction lies under section 5(2) rather than section 212(b). Further, the section 212(b) application cannot be considered as an isolated transaction divorced from the Jones-Erie merger and the acquisition of control or the purchase of the motor carrier properties of Medill and Mitchell. Certainly, it is proper for the Commission to consider the totality of the situation that will result from approval of either the section 212(b) application or

the section 5 application. All the transactions have as their common purpose the establishment of Jones as a motor carrier subsidiary of Alleghany in a more viable position than Jones was as an independent motor carrier. Hence, when viewed as the capstone of a series of interrelated transactions, it becomes apparent that section 5 and not section 212(b) is the applicable section under which the application should be processed.

Applicants by letter dated November 3, 1969, filed in lieu of a reply statement, stated that they concur with the Bureau's view that the Commission should entertain jurisdiction under section 5(2) of the act. There being no doubt that jurisdiction lies under the provisions of section 5(2) rather than under section 212(b), the application in No. MC-FC-70907 is hereby dismissed and the application in No. MC-F-10444 is hereby considered on its merits.

Having decided the jurisdictional question we must now determine the present status of Alleghany in order to place consideration of the application to acquire Jones in the proper perspective. The question as to whether Alleghany controls or has the power to control Penn Central was resolved by the Commission in *Pennsylvania R. Co.—Merger—New York Central R. Co.*, 327 I.C.C. 475, 481, in its adopting the findings of the hearing examiners, the examiners having found Alleghany's holdings did not provide it sufficient momentum to obtain control of Penn Central. No evidence has been submitted since that time to lead us to believe Alleghany's position has changed so as to place it in a position that it exercises control or has the power to control the Penn Central. We therefore see no reason to disturb our prior holding.

While Alleghany does not control Penn Central, there remains for decision whether with consummation of the proposal Alleghany and Penn Central will be affiliated within the meaning of section 5(6) of the act.

Section 5(6) of the act provides:

For the purposes of this section a person defined in section 1(3)(a) to include a corporation shall be held to be affiliated with a carrier if, by reason of the relationship of such person to such carrier (whether by reason of the method of, or circumstances surrounding organization or operation, or whether established through common directors, officers, or stockholders, a voting trust or trusts, a holding or investment company or companies, or any other direct or indirect means), it is reasonable to believe that the affairs of any carrier of which control may be acquired by such person will be managed in the interest of such other carrier.

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Section 5(2)(b) further states:

That if a carrier by railroad subject to this part, or any person which is controlled by such a carrier, or affiliated therewith within the meaning of paragraph (6), is an applicant in the case of any such proposed transaction under section 5(2) involving a motor carrier, the Commission shall not enter *** an order approving the transaction unless it finds that the transaction proposed will be consistent with the public interest and will enable such carrier to use service by motor vehicle to public advantage in its operations and will not unduly restrain competition.

Applying the quoted statutory provisions to this case, if Alleghany is found to be affiliated with Penn Central within the meaning of section 5(6), approval of the section 5(2) application may not be given unless the express findings of the 5(2)(b) proviso may be made vis-a-vis Penn Central and Jones.

In making such a determination, the test is not whether such person controls or has the power to control the carrier it is alleged to be affiliated with, but whether the legal and economic relationship between the two is such as to make it reasonable to believe the carrier to be acquired will be managed in a common interest with the other carrier. Managed in a common interest does not mean in the sole or even principal interest of such carrier, but in any material degree. *Southwestern Greyhound Lines, Inc.—Merger*, 39 M.C.C. 243.

In order to determine whether affiliation exists between the Penn Central and Alleghany, whether "it is reasonable to believe that the affairs of any carrier [Jones] of which control may be acquired by such person [Alleghany] will be managed in the interest of such other carrier [Penn Central]," a number of factors must be examined. A factor of particular significance is whether the person in question is dependent upon the continued successful operation of the "other carrier," either because of personal stock investment in the company or because the company is indebted to him. *Porto Transport, Inc.—Purchase—Sommer's Motor Lines*, 70 M.C.C. 70. Another factor to be considered is representation on the board of directors of the "other carrier," such being regarded as participation in management. *Southwestern Greyhound Lines, Inc.—Merger, supra*. These factors standing alone will not automatically be considered to establish that affiliation exists but must be viewed along with the other facts existing in the particular case in order to decide if affiliation exists.

Alleghany does have a substantial investment in Penn Central stock. As of June 30, 1969, the market value of Alleghany's Penn Central stock was said to total \$9,687,128 or approximately 5 percent of Alleghany's total assets. Advancing the following argument, Alleghany disclaims any intention of managing Jones in the interest of Penn Central:

Nor will Jones be managed, as a matter of fact or of law, in the interest of Penn Central. As of June 30, 1969, and as reported in the Semi-Annual Report to Shareholders, the indicated market value of Alleghany's Penn Central stock was \$9,687,128, and its investment in Jones (at cost plus unrealized equity in earnings since October 1, 1968) was listed at \$14,200,417. There is, therefore, no economic motive to manage one in the interest of the other since the value of the investments are similar in amount. In addition, Alleghany's investment in Penn Central, around 5 percent of Alleghany's total assets, does not support the inference that Jones Motor would be managed consistent with the interests of Penn Central. (See, *e.g.* *Harold C. Davis*, 70 M.C.C. 70 (1956)). Stated otherwise, Alleghany has no intention to manage Jones in the interest of Penn Central; the intention is to manage Jones in its own best interests and for the benefit of its shippers, employees, and the general public.

Alleghany's investment in the Penn Central, referred to in the quoted argument, does not take into consideration the value of the Penn Central shares held or controlled by individual Alleghany directors or the 391,900 shares of Penn Central held by Investors Diversified Services, Inc. Assuming that Alleghany's interest in Penn Central has only a monetary value of \$9,687,128, this approximately \$9 million interest plus the reported value of the Jones' shares totals \$23,887,545, or approximately 10 percent of Alleghany's total assets. It is reasonable to conclude that if a choice were presented of soliciting noncompetitive traffic or traffic presently transported by the Penn Central, Alleghany's management would not deliberately set about to depreciate the value of its Penn Central investment by actively competing for Penn Central traffic through reduced rates or better service. This consideration is especially significant since Jones operates in the same territory served by Penn Central. Conversely, it may be presumed, but cannot be proved, that the management of the Penn Central, many formerly high officials in the New York Central Railroad when the Central was controlled by Alleghany, would favor Alleghany as a motor carrier over other motor carriers in connection with plan I TOFC service or other joint-line arrangements.

Alleghany does have representation on the Penn Central board as well as on the boards of the following subsidiary rail carriers, the Pittsburgh & Lake Erie Railroad Company, the Philadelphia, Baltimore and Washington Railroad, and the Baltimore & Eastern Railroad Company. As a result of this representation on the board of the Penn Central and subsidiary rail carriers, greater than would be expected based solely on Alleghany's stockholdings, Alleghany does participate in the management decisions of Penn Central. Participation in the management of the largest railroad system in the territory presently served by Jones would obviously give Alleghany as a motor carrier a competitive advantage over other motor carriers operating in the same area. Alleghany, for example, would know long in advance of the general public, other motor carriers, and the Commission whether under their section 5a agreement the rail carriers had agreed to file for a general increase in rates, the date of filing said increase, the amount of increase, commodities exempted from said increase, and arguments to be advanced in support of said increase. All this information would be available to Alleghany as a motor carrier despite the fact that its representation on the Penn Central board was insufficient to control the railroad.

On the basis of Alleghany's investment in Penn Central, its representation on the Penn Central board, its previous position of dominance over the affairs of the New York Central (and hence its close association with the top management of the railroad), and the fact that both the Penn Central and Jones operate in the same general territory, we conclude that it is reasonable to believe that the proposed transaction would, if consummated without special conditions, result in affiliation within the meaning of section 5(6) of the act. It is, therefore, necessary to determine whether the proposed transactions are consistent with section 5(2)(b) of the act.

The absence of Penn Central as a party to these proceedings, coupled with the conclusion that Alleghany does not control Penn Central within the meaning of section 5(2) of the act as distinguished from affiliation under section 5(6), makes it impossible to conclude that the proposed transactions will enable the Penn Central to use the services presently rendered by Jones to public advantage in its operation and will not unduly restrain competition.

While not admitting that affiliation would result from approval of the proposed transactions, Alleghany, apparently in a desire

to remove impediments to the proposed transaction, in its application stated, in part, as follows:

Alleghany is willing to accept a condition to Commission approval of the transactions proposed herein that its shares of capital stock of MoPac shall continue to be held in trust, and that its shares of the capital stock of the Penn Central, and any other carrier securities subsequently acquired, shall be similarly deposited in trust, and that the Commission shall continue to exercise jurisdiction over said trust or trusts.

This offer was repeated in an affidavit of record by Fred M. Kirby, chairman of the board of directors and president, Alleghany Corporation, in the following manner:

12. As set forth in its Application to the Commission under §5 of the Act, Alleghany is willing to accept as a condition to Commission approval of the proposed acquisition by Alleghany of Jones Motor Co., Inc., the deposit of Alleghany's shares of the capital stock of Penn Central with an independent trustee subject to continuing Commission jurisdiction.

The placing of Penn Central shares in trust, suggested by Alleghany, is but at best a stopgap measure. While the trust would probably serve to prevent Alleghany from participating in the management of the Penn Central (and we shall hereinafter require that the board members of Alleghany serving on the board of directors of the Penn Central, its subsidiaries, and its holding company immediately resign their directorships with the Penn Central, its subsidiaries, and its holding company), it would not serve to reduce Alleghany's interest in the financial condition of the Penn Central. This financial interest is one of the factors considered in our determination of affiliation. Investment by a motor carrier, which Alleghany seeks to become, of 5 percent of its total assets in railroad stock appears inconsistent with the status of a motor carrier. The 5-percent figure includes only Alleghany's investment in Penn Central and it is noted that its investment in MoPac stocks and bonds substantially increases the percent of assets invested in railroad securities. It is not our intention to allow a motor carrier certificate to be used as a shield to prevent regulation by the Securities and Exchange Commission while Alleghany continues to engage primarily in investment rather than in transportation activities. Accordingly, we direct that as a condition to approval of this application Alleghany trustee all stock it may have in Penn Central, its subsidiaries, or any company affiliated with the Penn Central for a period not longer than 5 years with direction to the trustee to dispose of said stock
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during the period of the trust. Prior to consummation of the transaction proposed herein, Alleghany shall submit for approval of the Commission a plan showing how it intends to effectuate such trusteeship. While undoubtedly the divestiture of Penn Central shares by the trustee may have certain tax consequences, i.e., either the sale will result in a profit or a loss, Alleghany may avoid the tax consequence by electing not to consummate the proposed transaction. Further, the record before us indicates that the trustee should experience little difficulty in disposing of 390,130 shares of Penn Central now owned by Alleghany. Contained in the affidavit of Fred M. Kirby, previously referred to, is the following statement:

15. As of April 9, 1969, the date of the aforesaid Application under §5, the total amount of the capital stock of Penn Central owned by the funds sponsored by IDS [Investors Diversified Services, Inc.] was 1,020,000 shares or approximately 4.23% of the total amount outstanding, all of which were held for investment purposes only and not for purposes of control. As of this date [September 30, 1969], all but 391,900 of said shares, representing approximately 1.63% of the Penn Central capital stock outstanding, have been sold.

We will further require as a condition to approval that all interlocking directorates between Alleghany and Penn Central, its subsidiaries, and affiliates be terminated. Prior to consummation, proof of such termination shall also be submitted to the Commission. *Chesapeake & O. Ry. Co. Purchase*, 261 I.C.C. 239. Still further, in accordance with Alleghany's suggestion, and our own independent evaluation of the situation, we shall require as a condition for consummation of the proposal that the trusteeship of Alleghany's MoPac securities, as previously ordered by the Commission, be continued subject to the continuing jurisdiction of the Commission. The Commission in the future may either in response to a petition or on its own motion institute an investigation to determine whether the trust should be continued or whether Alleghany's divestiture of MoPac securities should be required.

The Penn Central shares not owned by Alleghany, but controlled by Fred M. Kirby and Allan P. Kirby, Jr., as coguardians of the property of their father, Allan P. Kirby, present a special problem. The 390,130 shares of Penn Central owned by Allan P. Kirby represent 1.62 percent of the outstanding Penn Central shares. While Fred M. Kirby and Allan P. Kirby, Jr., are by the terms of the conditions imposed relating to interlocking

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directorships prohibited from serving on the board of both Alleghany and Penn Central, either brother may resign his position with Alleghany and serve on the Penn Central board. In order to forestall the possibility of one of the coguardians electing to serve on the Penn Central board and the other coguardian electing to serve on the board of Alleghany, it is appropriate that a condition be fashioned to prevent the Kirby family from serving as a bridge over which affiliation between the Penn Central and Alleghany might be established. Accordingly, we shall require that the Penn Central shares owned by Allan P. Kirby under the control of Fred M. Kirby and Allan P. Kirby, Jr., as coguardians of their father's property, be deposited with an independent voting trustee under an agreement subject to the prior approval of the Commission. While not at this time directing that said trust be terminated by divestiture of Penn Central shares within a prescribed period, we shall retain continuing jurisdiction over the trust for the purpose of imposing in the future additional conditions or modifying the trust if warranted by then existing factual conditions.

There is also present in the record evidence of various interlocking directorates between Penn Central, Pittston Company, Alleghany, International Utilities, Inc., and other carriers. The cancellation of the interlocking directorates that exist between Alleghany and Penn Central should do much to simplify the relationship between these carriers. Other than in the situation that would exist between Alleghany and Penn Central if the proposed transaction were approved without conditions, the record does not contain sufficient evidence to determine the relationship between Alleghany and these other carriers and holding companies. If it should subsequently appear that these other carriers have become affiliated with Alleghany within the meaning of section 5(6) of the act or are otherwise operating in violation of the act, we expressly reserve the right to reopen these proceedings for the purpose of imposing further conditions upon Alleghany. At this time we will merely require that Alleghany's shares of International Utilities, Inc., be continued to be controlled by an independent voting trustee.

Before reaching the issues presented by the section 5(2) application, we must first determine whether the facts of record disclose a section 5(4) violation. Section 5(4) provides, in part, as follows:

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It shall be unlawful for any person, except as provided in paragraph (2) [with Commission approval], to enter into any transaction within the scope of subparagraph (a) thereof, or to accomplish or effectuate, or to participate in accomplishing or effectuating, the control or management in a common interest of any two or more carriers, however such result is attained* * *.

There can be no doubt that there was a statutory violation. In acquiring the outstanding stock of Jones and Erie without prior Commission approval, Alleghany violated the provisions of section 5(4) of the act. In an attempt to insulate itself from Jones' operations and thereby avoid the continuing violation of the statute, Alleghany immediately placed legal ownership and management responsibility for the carriers in the hands of Marine Midland. The trust so created was drafted in terms obviously designed to meet the requirements for independent voting trusts heretofore approved by the Commission in proceedings with similar factual situations. See *Missouri Pac. R. Co.—Control—Chicago & E.I.R. Co.*, 327 I.C.C. 279, 319.

The Commission does not view with favor the purchase of control and then placing the stock in trust. This practice is contrary to the intent of the statute in that the statute envisions approval of control by the Commission before and not after the purchase of control. The provisions of section 5 were not written by the Congress to be circumvented by carriers eager not to lose a good "deal," and those who do so flout the intent of Congress and impede the Commission in the discharge of its duties under the law. The purchase of control without prior Commission approval, even if the stock is placed in trust, constitutes a violation of the law and as such placed in serious question the fitness of Alleghany as a carrier. We made clear in our recent decision in *East Texas Motor Frt.—Control—Consolidated*, 109 M.C.C. 213, that actions similar to those taken here would not be condoned in the future. We again repeat the admonition stated therein that there is no excuse for violating the act to consummate a transaction.

It is noted that the unlawful control and the placing of the stock in trust occurred prior to our decision in *East Texas Motor Frt.—Control—Consolidated*, *supra*. While this may constitute a mitigating circumstance, it will not serve to excuse future violations. In this connection we believe it appropriate to specifically advise Alleghany that its representation contained in its application, that "Alleghany is willing* * * [that] any other carrier securities subsequently acquired, shall be similarly deposited in trust" is

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totally unacceptable to the Commission. If Alleghany as a motor carrier should purchase other carrier securities, it will subject itself to possible prosecution for violation of section 5 of the act. The placing of stock in trust will not serve to excuse or mitigate a consummated statutory violation.

Further, although section 5(11) of the act relieves parties to an approved section 5(2) application "from the operation of the anti-trust laws and of all other restraints, limitations, and prohibitions of law, Federal, State, or municipal, insofar as may be necessary to enable them to carry into effect the transaction so approved," this immunity is limited to operations conducted in accordance with the provisions of the Interstate Commerce Act and Commission imposed conditions. "Regulated industries are not *per se* exempt from the Sherman Act," *Georgia v. Pennsylvania R. Co.*, 324 U.S. 439, 456, and see also *Pan American World Airways v. U. S.*, 371 U.S. 296, 304-306.

Even though we have found a statutory violation through the unlawful acquisition of control, we are not free to summarily deny the application. Instead, we must examine the entire record in order to dispose of the application in a manner which would best serve the public interest. A violation of section 5(4) will not automatically defeat a transaction, if overriding public interest considerations plainly call for an opposite result. As to whether the proposed transaction is in the public interest, it need not be repeated that the tax consequences of a transaction have always been taken into account by the Commission in its consideration of applications under section 5(2). Tax benefits legally obtained have been considered as being salutary and even as grounds for delaying consummation of a merger if it would benefit the vendee. See *Arkansas-Best Freight System, Inc.—Control—Delta*, 93 M.C.C. 474. A tax saving is, therefore, a proper objective. However, an application to acquire a carrier solely because it will provide vendee certain tax benefits and for no other reason stands in a different position. Approval of an acquisition of that type would be tantamount to allowing vendee to simply milk vendor of its assets for its own good. Such a sycophantic transaction would obviously not be in the public interest. Alleghany has made clear its purposes are other than simply obtaining such benefits. The benefits it obtains are to be reinvested in Jones in order to improve its operations. The obtaining of tax benefits and reinvestment of the benefits to the advantage of Jones and thereby the shipping public is indeed salutary and in the public interest.

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Alleghany has in the past been subject to regulation by the Commission only under section 5(3) of the act. As a result of the transaction here proposed, Alleghany admits it will become a motor carrier subject to part II of the Interstate Commerce Act through the transfer to itself of the operating rights and assets previously held by Jones. In becoming such a carrier Alleghany must fully realize it is now subject to all provisions of that part of the act, including the securities provisions of section 214. Its future activities will be expected to be those proper for a carrier operating in the public interest and in accordance with the national transportation policy. All securities issued by Alleghany, except to the extent limited by section 214 of the act, must be in full compliance with the provisions of section 20a(2) of the act and applicant may be certain any future applications for issuance of securities will be closely scrutinized to ascertain that they are fully in compliance with the act.

In the past it has appeared Alleghany desired to use this Commission as a shelter to protect itself from the harshness of regulation of other agencies and it indeed admits that its purpose in being before the Commission here is at least in part to find such protection. The Interstate Commerce Act was not passed to provide a safe harbor from the other agencies of the Federal and State governments. Its purpose, as stated in the national transportation policy, was:

to promote safe, adequate, economical, and efficient service and foster sound economic conditions in transportation and among the several carriers***.

If regulation under the act results in leniency toward certain activities of carriers, it is because such leniency fosters the more important goals stated above. Alleghany will in the future be subject to the same type of regulation as other carriers. However, it is not to be expected that it will be protected from the regulation of any other agency to the extent the law may permit that agency to exercise concurrent jurisdiction over it.

In view of our action herein making Alleghany a carrier subject to part II of the act, we may vacate the previous orders of the Commission of March 2, 1955, and May 24, 1955, making Alleghany a noncarrier subject to regulation under the provisions of section 5(3) of the act.

Inasmuch as we are approving the transactions, we are not requiring of Alleghany the divestiture of Jones stock, though
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acquired unlawfully, provided that the complete transaction which we herein authorize is consummated within the 180-day period which is provided in our order. That order will render the Marine Midland trust revocable and will permit Alleghany to take legal title to the Jones securities now held therein. Consequently, in the event Alleghany does not assume control of Jones within the 180-day period, it would be expected to immediately dispose of its holdings in Jones' stocks and notify this Commission promptly when this has been done, disclosing in detail the manner in which disposal of the stock has been accomplished. Otherwise, consideration will be given to the institution of a proceeding under section 5(7) of the act, designed to accomplish the divestiture.

We find, in No. MC-F-10444, that the acquisition by Alleghany Corporation of the operating rights and property of Jones Motor Company, Inc., and its subsidiary, Erie Trucking Company, through merger of Alleghany Trucking Company, a wholly owned subsidiary of Alleghany Corporation, into Jones Motor Company, Inc.; and subsequently the merger of Jones Motor Company, Inc., into Alleghany Corporation for ownership, management, and operation, and the acquisition by Fred M. Kirby and Allan P. Kirby, Jr., individually and as coguardians of the property of Allan P. Kirby, an incompetent, of control of the operating rights and property through the transaction, constitute a transaction within the scope of section 5(2)(a) of the act, and that subject to the conditions heretofore enumerated it will be consistent with the public interest; and that if the transaction is consummated, Alleghany Corporation will be entitled to operate under the rights of Jones Motor Company, Inc., confirmed in No. MC-4963 and No. MC-4963 (Sub-Nos. 4, 7, 8, 9, 10, 13, 14, 15, 19, 20, 21, 22, 23, 24, 26, and 28), and of Erie Trucking Company confirmed in No. MC-23135, which rights are authorized to be embraced in a certificate to be issued in its name, with duplications eliminated; provided, however, that prior to consummation Alleghany Corporation and Fred M. Kirby and Allan P. Kirby, Jr., as coguardians of the property of Allan P. Kirby shall, subject to the just and reasonable conditions heretofore set forth, (a) deposit their holdings in Penn Central Company, Penn Central Transportation Company, its subsidiaries and affiliates, with independent voting trustees, (b) terminate all interlocking directorates of Alleghany Corporation, Penn Central Company, Penn Central Transportation Company, and their subsidiaries and affiliates, and (c) continue in trust the shares of MoPac and International Utilities, Inc., owned by Alleghany.

We further find, in Finance Docket No. 25686, that issuance by Jones Motor Company, Inc., of not to exceed 100 shares of its common stock, par value \$1 per share (a) is for a lawful object within its corporate purposes and compatible with the public interest, which is necessary and appropriate for, and consistent with, the proper performance by it of service to the public as a common carrier, and which will not impair its ability to perform that service, and (b) is reasonably necessary and appropriate for such purposes.

We further find, in Finance Docket No. 18656, the orders of the Commission dated March 2, 1955, and May 24, 1955, finding Alleghany to be a carrier subject to the provisions of section 20(1) to (11), inclusive, and section 20a(2) to (11), inclusive, of the Interstate Commerce Act, be vacated.

We further find, in No. MC-FC-70907, transfer of the operating rights of Jones Motor Company in No. MC-4963 and No. MC-4963 (Sub-Nos. 4, 7, 8, 9, 10, 13, 14, 15, 19, 20, 21, 22, 23, 24, and 28) to Alleghany Corporation under section 212(b) of the act, be dismissed.

An appropriate order will be entered.

COMMISSIONER TUGGLE, whom COMMISSIONER JACKSON joins, concurring in part:

I agree with the grant of authority and the requirement that the Alleghany and Kirby holdings in Penn Central be placed with an independent trustee.

I disagree with the requirement that the Alleghany trustee dispose of the Penn Central holdings within 5 years. In my opinion, measuring the size of Alleghany's holdings—which represent about 5 percent of its total worth and less than a 1-percent interest in Penn Central—against the statute's definition of "control" or "affiliation," I find that these holdings, in the trust agreed upon by Alleghany, represent only an investment and nothing more. As such, I find it inconsistent to require Alleghany to eventually sell off its stock without requiring as much from the Kirbys. It makes no difference how much of Alleghany's resources are invested in railroad stock, including MoPac, as long as the spectre of control or affiliation does not haunt the relationship. Without that threat, the condition on Alleghany is unreasonable.

CHAIRMAN STAFFORD, dissenting:

Clearly, Alleghany violated section 5(4) of the act in acquiring the outstanding stock of Jones and Erie without prior Commission

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approval. While I agree with the majority finding that such a violation will not automatically defeat the transaction, I find nothing in the record to show that overriding public interest warrants its approval. Alleghany's primary purpose in acquiring Jones, and its affiliates, is to lessen its tax burden. The fact that funds conserved by approval of the transaction will be made available for carrier investment by Jones and thus benefit the public indirectly is not what I consider to be of overriding public interest. Jones is a viable, financially sound and well managed corporation and I feel certain that it could continue to adequately serve the public in the future as it has in the past without benefit of Alleghany's tax savings. In *Central of Georgia Ry. Co. Control*, 307 I.C.C. 39, 43, and 44, the Commission stated:

The public interest is concerned not only with improvements in transportation service, but also with the maintenance of respect for and the observance of the law. If the Frisco is permitted to retain the fruits of its unlawful conduct, and we sanction such conduct, which we consider to have been in flagrant disregard of the law, others will be encouraged to pursue a like course and to present a *fait accompli* for our approval. Obviously, such is not in accord with the intent of the statute; i.e., that we pass upon "proposed" acquisitions of control prior to their consummation, including the justness and reasonableness of the terms upon which such control is to be acquired. If the indicated practice were generally followed, our administration of the statute in the public interest would be seriously hindered, if not defeated.

The fact that Alleghany placed the outstanding stock of Jones and Erie in trust immediately after acquiring it does not constitute, in my opinion, such a profusion of good faith so as to warrant condonation of the unlawful purchase. Alleghany is presently subject to partial regulation by the Commission and it is inconceivable to me that its officers and counsel did not know of the requirements of section 5.

Alleghany's principal business is in investing in stock interests in other companies and the transactions proposed in this proceeding would not change this situation. I do not believe it was the intent of Congress that this Commission enter into the field of regulation of companies whose principal business is other than that of public carriage, except where necessary in furtherance of the national transportation policy. I cannot find that need here. See *Edward Hines Lbr. Co. Merger*, 312 I.C.C. 364, 367.

Furthermore, the report of the majority clearly recognizes the dangers inherent in Alleghany becoming a motor carrier. The
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report goes to great lengths to soften the impact by conditions which would, among other things, assure that Alleghany could not control Penn Central. The report rationalizes the real reason for the transaction, i.e., the tax benefits by accepting Alleghany's statement that it will reinvest such benefits to improve the operations of Jones.

This Commission has consistently found in its regulation of security issues that carriers should be prohibited from issuing securities for noncarrier purposes. Its sole departure from that rule was the approval in 1962 of a stock issue by Greyhound Corporation for the purpose of acquiring the stock of a noncarrier, Boothe Leasing Corporation. In later cases the Commission reaffirmed its position against capitalization of noncarrier property, pointing out that even in the Greyhound-Boothe Leasing case the carriers' investment in carrier property was adequate to support Greyhound's increased capitalization resulting from the stock exchange.

Following consummation of the instant case, Alleghany would be grossly overcapitalized by Commission standards for motor carriers. Had the situation been reversed, i.e., had Alleghany first acquired motor carrier rights, it is doubtful that it would have obtained Commission approval for the issuance of securities to acquire its noncarrier investments. Although there are no securities involved in consummating the instant case, any securities which Alleghany may issue in the future would be subject to Commission approval even though the purpose of such issue would probably be noncarrier and outside of the Commission's transportation expertise. The majority report refers to the salutary effect of tax benefits when such benefits are to be reinvested in the carrier business. We have no assurance that such reinvestment would be made. Sound business practice would dictate that Alleghany invest its money in whichever of its investments offers the best return. While the Commission has approved diversification by motor carrier holding companies, it has adhered to the principle that carriers' investments in nontransportation properties should be limited. Approval of this case is a dangerous departure from that principle.

COMMISSIONER TIERNEY did not participate.

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ORDER

At a General Session of the INTERSTATE COMMERCE COMMISSION, held at its office in Washington, D. C., on the 27th day of January 1970.

No. MC-F-10444

ALLEGHANY CORPORATION—CONTROL AND PURCHASE—
JONES MOTOR CO., INC.—AND CONTROL ERIE TRUCKING
COMPANY

Finance Docket No. 25686

JONES MOTOR CO., INC., STOCK

Finance Docket No. 18656

LOUISVILLE & JEFFERSONVILLE BRIDGE AND RAILROAD
COMPANY MERGER, ETC.

No. MC-FC-70907

ALLEGHANY CORPORATION, TRANSFEREE, JONES MOTOR
COMPANY, INC.; TRANSFEROR

Investigation of the matters and things involved in these proceedings having been made, and said Commission on the date hereof having made and filed a report containing its findings of fact and conclusions thereon, which report is hereby made a part hereof:

It is ordered, That acquisition by Alleghany Corporation of the operating rights and property of Jones Motor Company, Inc., and its subsidiary, Erie Trucking Company, merger of Alleghany Trucking Company, a wholly owned subsidiary of Alleghany Corporation, into Jones Motor Company, Inc., and the merger of Jones Motor Company, Inc., into Alleghany Corporation for ownership, management, and operation, and acquisition by Fred M. Kirby and Allan P. Kirby, Jr., individually and as coguardians of the property of Allan P. Kirby, an incompetent, of control of the operating rights and property through the transaction, approved and authorized upon the terms and conditions set forth in the said report of the Commission.

It is further ordered, In Finance Docket No. 25686, that Jones Motor Company, Inc., be, and it is hereby, authorized to issue not exceeding 100 shares of its common stock, par value \$1 per share, for the purposes and upon the conditions set forth in the said report.

It is further ordered, That in Finance Docket No. 18656, the prior orders of the Commission dated March 2, 1955, and May 24, 1955, be vacated to the extent set forth in the said report.

It is further ordered, In No. MC-FC-70907, that the application be, and it is hereby, dismissed.

It is further ordered, That if the parties to the transaction herein authorized desire to consummate same, they shall (1) promptly take such steps as will insure compliance with sections 215, 217, and 221(c) of the Interstate Commerce Act, and with the rules, regulations, and requirements prescribed thereunder, and (2) confirm in writing to this Commission immediately after this consummation the date on which consummation has actually taken place.

It is further ordered, That if the authority herein granted is exercised, Alleghany Corporation shall submit for consideration a sworn statement, and one copy thereof, hereby required, within 60 days after the consummation of the transaction, showing all expenditures made in connection with the transaction authorized, including the consideration, legal and other fees, commission, and any other costs incidental to the transaction, the assets acquired and liabilities assumed, including loans incurred to consummate the transaction, indicating the account number and title to which each item has been, or is to be, debited or credited.

It is further ordered, That Jones Motor Company, Inc., shall report concerning the matters involved in Finance Docket No. 25686 in conformity with the order of the Commission, division 3, dated May 20, 1964, as amended, respecting applications filed under section 214 of the act (49 CFR 1115.6).

It is further ordered, That except as authorized in Finance Docket No. 25686, the common stock authorized to be issued shall not be sold, pledged, repledged, or otherwise disposed of

by Jones Motor Company, Inc., unless and until so ordered or approved by this Commission.

It is further ordered, That nothing herein shall be construed to imply any guarantee or obligation as to said stock, or dividends thereon, on the part of the United States.

It is further ordered, That recital, in said report, of financial data shall not be construed as approval of accounting methods which have been followed or expenditures represented thereby.

It is further ordered, That this order shall be effective on the date it is served.

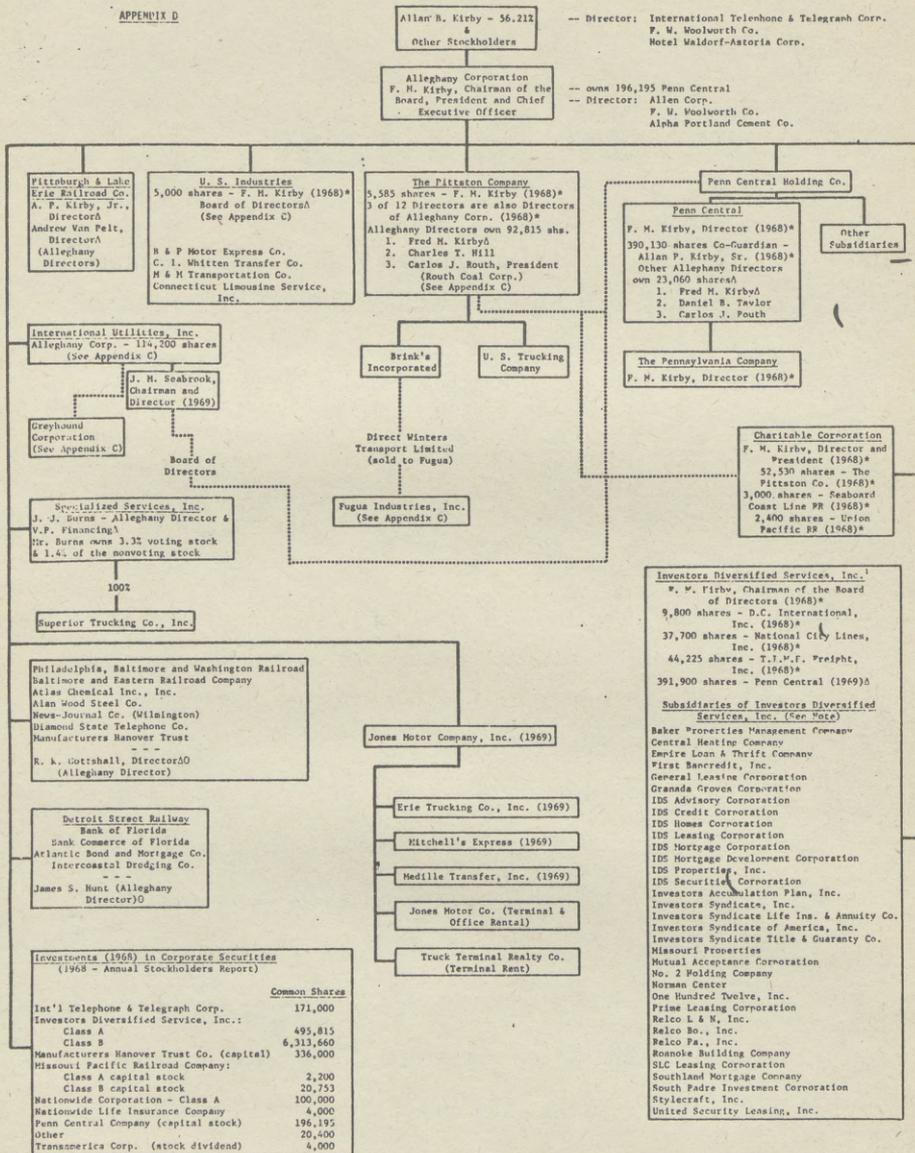
And it is further ordered, That unless the authority herein granted is exercised within 180 days from the effective date of this order, this order shall be of no further force or effect.

By the Commission.

H. NEIL GARSON,
Secretary.

(SEAL)

APPENDIX D



Note: At December 31, 1968, Investors Diversified Services, Inc. was a nonreporting non-carrier subsidiary of respondent. Investors Diversified Services, Inc. acts as investment adviser and distributor for six mutual fund companies and, in addition to its own investments in securities, selects and supervises the portfolio investments of its wholly-owned subsidiaries and the fund companies.

† World Who's Who in Commerce and Industry (Chicago, Illinois: Hargis - Who's Who, 1967).

* Allegheny Corporation - 1968 Annual Report, Item 209, Page 218.

Source: Docket HC-F-10296* -- Docket HC-F-10444.

91ST CONGRESS
1ST SESSION

H. R. 7373

IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 20, 1969

Mr. STAGGERS introduced the following bill; which was referred to the Committee on Interstate and Foreign Commerce

A BILL

To amend the Interstate Commerce Act to provide that a person which is not a carrier may acquire control of a carrier only with the approval and authorization of the Interstate Commerce Commission.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 That section 5 (2) (a) (i) of the Interstate Commerce Act
4 (49 U.S.C. 5 (2) (a) (i)) is amended by striking out "or
5 for a person which is not a carrier to acquire control of two
6 or more carriers through ownership of their stock or other-
7 wise; or for a person which is not a carrier and which has
8 control of one or more carriers to acquire control of an-
9 other carrier through ownership of its stock or otherwise;"

VI--O

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- 1 and inserting in lieu thereof "or for a person which is not
- 2 a carrier to acquire control of a carrier through ownership
- 3 of its stock or otherwise;".

TABLE V
PURCHASES BY THE PENN CENTRAL EMPLOYEES THRIFT PLAN

<u>WEEK ENDED</u>	<u>NUMBER OF SHARES</u>
April	
3	1,500
10	2,500
17	1,500
24	3,300
May	
1	4,600
8	2,300
15	4,400
22	4,400
29	2,000
June	
5	4,900
12	5,000
19	5,600
26	---
Total	42,000

Mr. LISHMAN. Each prospectus contains the customary caveat that the issuance and sales of the debentures referred to in the prospectus are subject to authorization by the ICC. Is that correct?

Mr. KAHN. I would assume so. I have not heretofore seen the May filing, and I will accept your word that that language is in here.

Mr. LISHMAN. The document is in front of you. We may be able to tell you what page that is on.

Mr. KAHN. Fine.

Mr. LISHMAN. It is right on the front page.

Mr. KAHN. That language appears here.

Mr. LISHMAN. And it also appears in the prospectus that in connection with the authorization, the Commission does not pass upon the adequacy or accuracy of the merits of the securities. That is correct, is it not?

Mr. KAHN. Correct.

Mr. LISHMAN. Now, is it correct that this caveat is substantially the same as that contained with respect to prospectuses filed with the Securities and Exchange Commission? I would like to ask that of the Commissioner.

Mr. SMITH. It is substantially similar to our—to the legend on Commission prospectuses, although there are differences. I would like to be able to make a more word-for-word comparison than I am able at this short notice. I do not have our standard legend before me.

Mr. LISHMAN. Well, may I ask—

Mr. SMITH. There are some differences in the wording but it is substantially comparable. Our prospectuses do have a statement to the effect, and I do not have the exact wording before me.

Mr. LISHMAN. I just wanted to get the substantiality.

Mr. SMITH. Yes.

Mr. LISHMAN. Now, were the April 29 or May 12 prospectuses of the Pennsylvania Co. filed with the SEC?

Mr. SMITH. No, they were not. They were exempted.

Mr. LISHMAN. Why not?

Mr. SMITH. They are exempted under section 3(a)(6) of the Securities Act of 1933.

Mr. LISHMAN. I am addressing myself to the SEC. At this point we would like to refer to exhibit D, which is a copy of a letter dated July 1, 1970, from Chairman Staggers, requesting an opinion as to whether the Pennsylvania Co. may be subject to the provisions of the Investment Company Act of 1940. There is attached to that letter an interim reply from the SEC, stating:

It is the staff's tentative view based on the limited information presently available, that there is a question as to whether the Pennsylvania Company is an investment company within the meaning of the Act.

On September 18, 1970, Chairman Staggers was advised by the SEC that, in its opinion, Pennsylvania Co. is not an investment company within the meaning of section 3(c)(9) of the Investment Company Act of 1940. Is that correct?

Mr. SMITH. That is correct.

Mr. LISHMAN. Is it the view of the SEC that a company having less than half of the value of its holdings in companies subject to regulation under the Interstate Commerce Act is, nevertheless, eliminated

from regulation under the Investment Company Act of 1940 if the company itself is subject to regulation under the Interstate Commerce Act?

Mr. SMITH. The question was whether that does eliminate it? Yes, it does.

Mr. LISHMAN. Is it a fact that the Pennsylvania Co. at the time of issuing the April and May prospectuses, was not registered as an investment company with the SEC?

Mr. SMITH. It was not so registered.

Mr. LISHMAN. If the Pennsylvania Co. had been registered as an investment company with the SEC, what requirements would it have had to fulfill before its offering could be authorized and marketed?

Mr. SMITH. It would have been required to comply with the requirements of the 1933 act with respect to the offering of its securities. In addition, there are substantive requirements under the 1940 act with respect to capital structure and other matters that it would have been required to have complied with, aside from the offering of the securities.

Mr. LISHMAN. I am going to come back to some of those matters in detail later, but now I would like to shift and ask a question of the ICC.

What are the requirements of the ICC with respect to the issuance and marketing of debentures contemplated in the April prospectuses, particularly with respect to requirements of disclosure and making of reports?

Mr. KAHN. The Pennsylvania Co., as you indicated, Mr. Lishman, has been designated by the Interstate Commerce Commission to be a carrier under section 5(3) of the Interstate Commerce Act. Accordingly, any securities issued by it would have had to comply with the provisions of section 5(3) of the act, which I shall not take the time to read. In addition, the Pennsylvania Co. has long been designated by the Interstate Commerce Commission as a carrier for purposes of accounting and reporting requirements and it has filed, and continues to file, with the Interstate Commerce Commission reports and maintains accounts in accordance with the Commission's accounting requirements.

Mr. LISHMAN. I will turn to the SEC.

If the Pennsylvania Co. had filed its prospectus with the SEC instead of the ICC, is it not a fact that, in accordance with schedule A of the Securities Act of 1933, it would have been required to disclose the annual remuneration, both direct and indirect, paid to its principal officers and directors?

Mr. SMITH. The requirement with respect to all officers and directors as a group and to the three highest paid officers, those over \$30,000 a year.

Mr. LISHMAN. Is it true also that schedule A would require disclosure of stock options outstanding and, particularly, the options held by management?

Mr. SMITH. Yes, sir.

Mr. LISHMAN. Is it also true that schedule A would require a full disclosure of any material interest, direct or indirect, which any officer or director of Pennsylvania Co. may have had in any material transaction with the company?

Mr. SMITH. Yes, sir.

Mr. LISHMAN. Would it also—

Mr. SMITH. Within a certain period of time prior to the offer.

Mr. LISHMAN. What period of time would that be?

Mr. SMITH. Two years, I believe.

Mr. LISHMAN. Would this include disclosure of interest payments made by the company to any bank represented on the board of directors if the amount exceeded \$30,000?

Mr. SMITH. I am not sure of the answer to that. I do not think so where there is merely a common director between the two.

Mr. LISHMAN. Could we get a definitive answer on that for the record, please?

Mr. SMITH. Yes.

(See app. B, p. 165.)

Mr. LISHMAN. Would they also be required to show legal fees to a law firm represented on the board of directors if the annual fees involved exceeded \$30,000?

Mr. MACDONALD. Perhaps we could save time if the gentleman whom you seem to be consulting, if he would identify himself.

Mr. SMITH. I have with me Alan Levinson, who is director of our Division of Corporation Finance, which is the division which processes 1933 act prospectuses.

Mr. MACDONALD. Mr. Levinson, do you have a direct answer to the question asked by Mr. Lishman?

STATEMENT OF ALAN LEVINSON, DIRECTOR, DIVISION OF CORPORATION FINANCE, SECURITIES AND EXCHANGE COMMISSION

Mr. LEVINSON. If Mr. Lishman would repeat the question I will do that.

Mr. LISHMAN. Would schedule A require legal fees to a law firm represented on the board of directors to be disclosed if the annual fees involved exceeded \$30,000?

Mr. LEVINSON. If it was on form S-4 the answer is "Yes." If it is on form S-1, which is our form of registration for industrial companies, the answer could be "No."

Mr. SMITH. I should add that form S-4 is our registration form for closed-end investment companies, which would have been the Pennsylvania Co. had it been subject to the 1940 act.

Mr. MACDONALD. Do you want to add something to that?

Mr. LEVINSON. In further response, we will supplement that in writing to you.

Mr. LISHMAN. We would appreciate having that.

(See app. B, p. 168.)

Mr. LISHMAN. Would you say it is a reasonable assumption that Congress, in including these requirements in schedule A of the 1933 act, determined these were material facts necessary for an informed investment decision?

Mr. SMITH. Yes, sir; that is the purpose of schedule A.

Mr. LISHMAN. I would like to note for the record, and the ICC may correct me if I am wrong, that the April and May prospectuses, which Pennsylvania Co. filed or furnished the ICC, do not disclose

any information about management compensation, stock options, or material interests in transactions to which I have referred above.

Mr. KAHN. Mr. Lishman, the Commission would like to correct the record and point out that while this information is not included in the prospectus, it most certainly is included in the annual report form filed by the Pennsylvania Co. with the Interstate Commerce Commission, at least in part.

Mr. LISHMAN. Is that annual report supplied to investors?

Mr. KAHN. That annual report is available to investors; yes, sir.

Mr. DINGELL. That was not the question that was asked; is it supplied to investors?

Mr. KAHN. Upon request and payment of appropriate reproduction charges it will be supplied investors.

Mr. DINGELL. So, the answer is very different. In effect, it is not supplied. If you have a most diligent and adroit investor who is willing to spend money and who is knowledgeable in ICC procedures he might be able to procure it. Perhaps you might indicate to the committee what number of requests have been made for this document by investors in Penn Central or any of its holding companies, affiliates, or subsidiaries.

Mr. KAHN. I have no idea, Mr. Dingell.

Mr. DINGELL. It would be fair to say probably none; would that be a fair answer?

Mr. KAHN. I do not say that would be; no, sir.

Mr. DINGELL. But a very small number.

Mr. KAHN. That is relative, yes, sir.

Mr. DINGELL. Considering the number of stockholders.

Mr. MACDONALD. If I can interject, the answer is no, it is not supplied, it is made available.

Mr. KAHN. Yes, sir.

Mr. LISHMAN. Made available when?

Mr. KAHN. Upon request.

Mr. DINGELL. And the document relative—

Mr. LISHMAN. But there is no legal requirement that that had to be furnished to the prospective investor.

STATEMENT OF JOHN MATTRAS, SUPERVISING ATTORNEY, INTERSTATE COMMERCE COMMISSION

Mr. MATTRAS. I am John Mattras.

Mr. LISHMAN. Would you state your position?

Mr. MATTRAS. I am an attorney at the Interstate Commerce Commission, supervising attorney.

We require prospectuses to furnish substantially the same information as that required by the SEC. Now, in this case this prospectus was not approved. It had not gone to the stage where we looked at it. It is conceivable we would have asked this and many other additional bits of information. We have at times requested changes in a prospectus, so that it is entirely possible that the prospectus was not adequate, and in view of the fact it was not processed, we cannot say whether we would have required it, but they should have supplied the same information as they would have with the SEC.

Mr. LISHMAN. May I ask the ICC to supply this committee with five prospectuses where this information that I am shown appears in schedule A of the SEC prospectus, appears in an ICC document?

Mr. MATTRAS. In an ICC document?

Mr. LISHMAN. Yes, sir.

Mr. MATTRAS. All right, sir, we will look into that.

Mr. LISHMAN. We would like to have that supplied to the committee because it is our understanding that is not required to be filed in the prospectus that is left with the ICC.

(See app. A, p. 137.)

Mr. MATTRAS. Yes, we would have had to look at it and determine in different cases. Now we require prospectuses in public issues.

Mr. LISHMAN. Is that a requirement of a statute or is that a requirement of a regulation?

Mr. MATTRAS. It is in the nature of a regulation. We require that they supply the same prospectus as the SEC would be furnished.

Mr. LISHMAN. What is the reference to the regulation?

Mr. MATTRAS. We have—much of the information we develop is on a unique basis and we ask them for this, if it is not supplied. I do not know, I cannot say for sure, that it is in an actual regulation. But we do request the prospectus in all public issues.

Mr. LISHMAN. If it is not a public regulation available to the public generally, how was a prospective investor protected?

Mr. MATTRAS. Sir, a prospectus must be furnished to the investor in connection with any issue, the prospectus must be furnished to any prospective purchaser of a security.

Mr. ROGERS. Mr. Chairman, may I ask just one question? Do I understand you do not have a set form that you require of everyone?

Mr. MATTRAS. No, sir.

Mr. ROGERS. You kind of do it on an ad hoc basis?

Mr. MATTRAS. The requirement had been to furnish the same material as was furnished to the SEC.

Mr. ROGERS. So they write your regulations, is that what you are telling us?

Mr. MATTRAS. In this area, that is correct.

Mr. ROGERS. But you never published it to make this a set requirement?

Mr. MATTRAS. As I understand, sir, that is correct.

Mr. ROGERS. So, they might have to furnish it or they might not, depending on the attorney they deal with in the ICC.

Mr. MATTRAS. Well, they are required to furnish this prospectus and we, of course, look at the prospectus.

Mr. ROGERS. I know prospectus, but all of the material in the prospectus does not have to be the same for everybody; is that correct?

Mr. MATTRAS. It may vary with different people because of different carriers having different problems. Some may have to give more and others not as much, depending on what we see. But the basic information should be the same as with the SEC.

Mr. ROGERS. Hopefully so.

Mr. MATTRAS. Well, we look at them, sir.

Mr. ROGERS. But no set regulations are set forth.

Mr. MATTRAS. I believe that is correct.

Mr. ROGERS. It is amazing.
Thank you, Mr. Chairman.

Mr. MACDONALD. Mr. Lishman.

Mr. LISHMAN. Does the ICC require the same general accounting principles to be followed in connection with the prospectuses and the issuance of securities that are required by the SEC?

Mr. MATTRAS. We do have accounting principles, sir. I do not know that they are exactly the same as the SEC. Mr. Paolo could answer that better.

Mr. LISHMAN. Is there uniformity?

Mr. MACDONALD. Why don't you answer it, Mr. Paolo?

Mr. PAOLO. Yes, sir, I would like to make the record clear, the Interstate Commerce Commission promulgates accounting methods for the surface transportation industry. We do have a uniform system of accounts that is in general conformity with general accounting principles. There are one or two items in which we differ from the generally accepted accounting principles.

Mr. LISHMAN. Do you differ from the principles that are followed by the SEC?

Mr. PAOLO. I would suggest in probably one area, I do not know that the SEC has published a regulation in this regard. The general area of difference between the ICC and the generally accepted accounting principles is in the area of accounting for deferred taxes.

Other than that, generally speaking, the reports of stockholder reports of the companies under ICC jurisdiction are accepted by public accountants and certified accordingly.

Mr. MACDONALD. Could I ask you to explain why there is a difference at all? What is the purpose of having a difference?

Mr. PAOLO. Well, No. 1, we are in a regulatory field as opposed to the public accountants in the nonregulatory field.

Mr. MACDONALD. The SEC?

Mr. PAOLO. I do not know the SEC has particularly prescribed these particular regulations. SEC does not prescribe regulations in the sense that a regulatory agency prescribes regulations. We prescribe a complete uniform system of accounts.

Mr. MACDONALD. You are not suggesting the SEC is not a regulatory agency, are you?

Mr. PAOLO. Well, I am saying not in the sense of ratemaking and regulation in the same sense. They are in one area of brokers, as I understand, but in the general scheme they do not set rates or profits for any industry in that sense. They do not prescribe a system of accounts for industry in general.

Mr. MACDONALD. I am a little more confused than I was before and that was fairly confused.

What is the reason for having a difference? You say because it takes a different system in a regulatory agency and not for the SEC.

Mr. PAOLO. Well, certain matters can be treated differently by regulatory agencies because of ratemaking factors, for example, for deferred taxes. The situation for deferred taxes is setting up a liability and a charge to income for taxes that may be paid in the future. Now, from a regulatory standpoint if we allow that the ratepaying public would have to be providing these funds to the company that might not

be disbursed for another 20 or 30 years. So, there is a difference in the ratemaking aspect.

Mr. MACDONALD. Go ahead.

Mr. LISHMAN. Mr. Chairman, I would like to ask you to direct the SEC witnesses and the ICC witnesses to see if they could prepare for this committee an analysis of the similarities and differences between the methods of accounting pursued by each agency in connection with the issuance and marketing of securities.

Mr. MACDONALD. If that is possible, and I certainly hope it is, that you would also add the reason for the differences.

Mr. PAOLO. If I might add to that, I think similarities will encompass a whole uniform system of accounts. If we talk about differences I think we can narrow that down much more readily.

Mr. LISHMAN. Of course, I think the differences would serve the purpose.

Mr. MACDONALD. Is that possible without too much difficulty?

Mr. HARDIN. Are you asking insofar as investment companies are concerned or is this across-the-board now?

Mr. LISHMAN. I would say it is across-the-board.

Mr. MACDONALD. Before we go further than that, would it be possible without putting an intolerable burden on you to prepare it?

Mr. PAOLO. I would like to hear from a representative of the SEC. I am not certain.

Mr. MACDONALD. I am probably going to make the request anyway but I do not want to put a terrible burden on you, if it is something simple.

Mr. DINGELL. You only have transportation and holding companies, those are the only two kinds of things that you are going to go through, is that correct?

Mr. MACDONALD. When Mr. Lishman was asked the question he responded "across-the-board."

Mr. DINGELL. That is across-the-board transportation and holding companies, are all that are involved.

Mr. PAOLO. But general system of accounts covers a wide area.

Mr. MACDONALD. That has been covered but Mr. Lishman says the differences be outlined and explained so I will make the request. Is that satisfactory?

Mr. DINGELL. Mr. Chairman, I might just observe the accounting system of the ICC is so poor here that the Chairman of the ICC admitted before another subcommittee of this committee that the possibility of Penn Central bankruptcy came as a complete surprise to them.

Mr. MACDONALD. That was in the opening statement, Mr. Dingell. I renew my request.

Mr. SMITH. This could be a very formidable undertaking depending upon the depth with which you want to go into this. The accounting requirements of this Commission are to some extent relevant to the type of company reporting. In general there is a uniformity of accounting application among the various kinds of companies who file disclosure documents with the Commission. It might be more feasible to give a preliminary reply to you as to the feasibility of it.

Mr. MACDONALD. I would suggest that. We have an accountant, Mr. Druhan, on the staff, so I think if you work on it a little bit, it will be cleared up. We are not trying to impose a burden on you. We are just trying to get information.

(See p. 145 and p. 217.)

Mr. LISHMAN. I would like to return back to the SEC. I would like to go to the question of the Investment Company Act and the way it would have protected investors if the Pennsylvania Co., had registered under the act.

Now, it is correct, is it not, if the Pennsylvania Co., had been registered with the SEC as an investment company, transactions between affiliates, particularly transfers of assets, would have required the prior approval of the SEC?

Mr. SMITH. In general, that is correct, sir.

Mr. LISHMAN. If it had been registered, then the compensation of management could not have been excessive.

Mr. SMITH. Are you speaking of officers and directors of the investment company? There are no provisions in the Investment Company Act that go beyond the general corporate law in that respect. The provisions deal with investment advisory contracts with respect to compensation levels.

Mr. LISHMAN. On the investment advisory level, excessive compensation would not have been reported?

Mr. SMITH. There is an outside test on the amount of investment advisory compensation. It amounts to a gross abuse of trust.

Mr. LISHMAN. If it had been registered with the SEC would it have required a proper allocation of expenses between the Pennsylvania Co. and the parent?

Mr. SMITH. You mean as to the allocation of those expenses attributable to management of the investments in the investment company?

Mr. LISHMAN. Yes.

Mr. SMITH. It would be part of their statement filed with us, yes, sir.

Mr. LISHMAN. If it had been registered, loans by the Pennsylvania Co. to its parent would have required the prior approval of the SEC?

Mr. SMITH. Yes, sir.

Mr. LISHMAN. And if it had been registered, any guarantee by Pennsylvania Co. of a loan made by a third person to the Penn Central Transportation Co. would have required the prior approval of the SEC?

Mr. SMITH. Again that is true, sir.

Mr. LISHMAN. And if it had been registered, the Pennsylvania Co. would have been prohibited from creating an excessive debt structure, of creating interest obligation beyond its capacity to service?

Mr. SMITH. The investment company test is 300 percent of—any debt issued has to be covered three times.

Mr. LISHMAN. Finally—

Mr. SMITH. And only one category of debt issue is permitted.

Mr. LISHMAN. If it had been registered, it is correct that the majority of the board of directors could not have been persons affiliated with a bank?

Mr. SMITH. That is correct. Section 10(c) of the Investment Company Act provides that no registered investment company shall have the majority of its board consisting of persons who are officers or directors of any one bank.

Mr. LISHMAN. Now, I would like to point out that each of these items that I have raised about the applicability of the Investment Company Act was raised because the Pennsylvania Co. engaged in each of the practices described, and the evidence for this can be found in the prospectuses of the Pennsylvania Co. It speaks for itself.

Now coming back to the ICC, is it true that investment companies subject to the jurisdiction of the ICC are not prohibited from engaging in the practices just described, although they would be prohibited by the Investment Company Act of 1940?

Mr. KAHN. I think, Mr. Lishman, generally the answer would have to be yes except, I believe, there may have been one or two transactions that you included in your listing which would have amounted to a securities issue, and insofar as the holding company may have been designated a carrier under section 5(3) of the Interstate Commerce Act authorization of the Commission, advanced authorization of the Commission, would have been required before such security issue would have been lawful.

Mr. LISHMAN. Mr. Kahn, we would appreciate if you would supply for the record, a definitive answer to this.

Mr. KAHN. If you will give me the transactions that you read for the benefit of the SEC, I will attempt to indicate—

Mr. LISHMAN. We will send you a note, a letter indicating that.

Mr. KAHN. Fine.

Mr. LISHMAN. Thank you.

(See app. A, p. 137.)

Mr. LISHMAN. Now coming back, what steps has the ICC taken to insure investors in investment companies under its jurisdiction for protections similar to protections they would enjoy if the companies were subject to the jurisdiction of the SEC?

Mr. HARDIN. Subsequent to the previous hearings you have referred to, Mr. Lishman and Mr. Chairman, the Interstate Commerce Commission undertook to begin the drafting of legislation which would provide additional authority and jurisdiction for the Commission which would relate to, for example, situations where a nontransportation company acquires control of a single company. The legislation is still in draft form; it is now before the Commission. We are hopeful to have this submitted to the chairman of the committee within the next couple of weeks. This would also cover transactions as between subsidiaries. We believe that the legislation we are going to suggest will reach a number of the things which you are covering here.

Mr. LISHMAN. Now, in this no man's land, whereby innocent investors are misled by material failures to disclose in prospectuses filed with the ICC, did it not occur at any time to any officials in the SEC or the ICC that this was a situation requiring widespread publicity for the protection of widows and orphans, and this is not a rhetorical question—widows and orphans have been complaining to us about this situation.

Mr. MACDONALD. You addressed it to both?

Mr. LISHMAN. I addressed it to both. I will ask the SEC.

Mr. SMITH. In 1959, Mr. Lishman, I am sure you remember, the Commission proposed an amendment to the 1940 Act that would have

eliminated the 3(c)(9) exemption that railroad issuers previously have, and I believe the ICC concurred in that recommendation. That bill was not enacted, and we have abided since then by the statutory split that does exist.

Mr. MACDONALD. Does the ICC want to answer as well?

Mr. HARDIN. The bill to which Commissioner Smith refers, if my recollection serves me correctly, I am not certain of this, but I think was passed by the House. I may be in error on that, but there is a provision in the Interstate Commerce Act which, in section 20(a)(7), provides that the ICC jurisdiction shall be exclusive and plenary, that the ICC withdrew from that and agreed with the SEC that there should be concurrent jurisdiction in this area, and we joined with them in a position on that bill.

Mr. DINGELL. Mr. Chairman, could I request that the legislation referred to, be inserted in the record at this point?

Mr. MACDONALD. If it is available, without objection, so ordered.

(See app. C, p. 239.)

Mr. KAHN. May I respond further on behalf of the Interstate Commerce Commission to the question posed by Mr. Lishman? Clearly it is a criminal offense to submit to the Interstate Commerce Commission false and misleading data in applications for authorization of security issues.

Moreover, the Interstate Commerce Commission, under the law, is obliged and does indeed look at the purpose of that security issue, a matter which the SEC does not under the existing law require. The Commission has the power and does reject security issues which do not serve a lawful purpose under the act.

Mr. SMITH. Mr. Lishman, if I may, I would like to offer for the record, Mr. Chairman, copies of the portions of the hearings before the subcommittee of this committee back in 1959.

Mr. MACDONALD. Which subcommittee was that?

Mr. SMITH. The Commerce and Finance Subcommittee.

Mr. MACDONALD. I was chairman of that committee. I do not remember the hearings. [Laughter.]

Mr. SMITH. I am afraid it was before my time. This portion of the hearings does contain a comparative analysis of the 1940 act and the Interstate Commerce Act which, I believe, might be of some assistance to the committee and some benefit for the record.

Mr. MACDONALD. Without objection, so ordered.

(See app. C, p. 239.)

Mr. SMITH. I would also like to offer a copy of a memorandum that was delivered to Chairman Staggers in October, I believe, of 1969 on the dual regulatory status of investment companies and ICC regulated carriers which I again believe would be of some assistance to the committee.

Mr. MACDONALD. Without objection, so ordered.

(See app. C, p. 218.)

Mr. LISHMAN. Returning to the ICC, was the company successful in launching a \$100 million debenture offering?

Mr. KAHN. I believe they were unsuccessful, Mr. Lishman. They could not float it.

Mr. LISHMAN. Do you know why they were unable to float it?

Mr. KAHN. I believe the money market at that time, Mr. Lishman, was such that they could not float it without paying interest at a higher level than management thought was prudent.

Mr. LISHMAN. Now, according to exhibit E, which is a copy of page 4 of the prospectus of the Pennsylvania Co., the net proceeds from the sale of debentures were to be used to purchase from Pennsylvania Transportation Co. substantial amounts of its security holdings in nontransportation companies at book value. Is that correct?

Mr. KAHN. I would have to accept your statement.

Mr. LISHMAN. Well, you have that page 4 of the exhibit in front of you, and I think you will find that that is so stated.

Do you know how that book value was arrived at?

Mr. PAOLO. If I may, I would suggest, without having studied this thing, when net book value is discussed of a particular company, it is the net book value on the books of that particular company being the assets less the liabilities.

Mr. LISHMAN. Is it not reasonable to assume that current market value of the assets would be greater than their net book value?

Mr. PAOLO. Not necessarily. It could be much less or it could be greater, sir, or it could be equal.

Mr. LISHMAN. Was any attempt made to ascertain the current market value of these assets?

Mr. PAOLO. If I might answer, Mr. Lishman, we did not get into this particular—the Commission is looking at that now as part of its examination, but we never got into any analysis of this document of which you are speaking now. The application was filed; it was inadequate at the time, and my understanding is we did nothing with it at that point.

Mr. LISHMAN. Is it customary for ICC to make a comparison of the net book value figures and the current market value of assets proposed to be transferred?

Mr. PAOLO. We do that every time we examine a carrier's account, sir; yes, sir.

Mr. LISHMAN. Is it a fact that if the—this is to the SEC—if the Pennsylvania Co. had filed its prospectus with the SEC it would have been required to disclose the current actual market value of the assets?

Mr. SMITH. Where they are publicly held securities, yes, sir. Where they are not, the Investment Company Act provides that they are the value in good faith by the board of directors.

Mr. PAOLO. In this situation one of the companies that I noticed the name of here, of course, was not a marketable security. It was held in total by the transportation company.

Mr. LISHMAN. Is it true that the Pennsylvania Co. has outstanding a class of preferred stock which it not held by the railroad or its parent, the Penn Central Co., but by public investors?

Mr. PAOLO. I believe that is correct.

Mr. LISHMAN. It is a fact, is it not, that the transfer of assets from the railroad to the Pennsylvania Co. would have created a preference in favor of the preferred stockholders and would have diluted the equity and interest of the common stockholders of the Penn Central Co.?

Mr. PAOLO. I would have to analyze the transaction more so before I could respond to that.

Mr. LISHMAN. Could we receive such an analysis from you, please?

Mr. PAOLO. If you could repeat the question in a letter or so, so I understand it.

Mr. LISHMAN. Is it a fact that the transfer of assets from the railroad to the Pennsylvania Co. would have created a preference in favor of the preferred stockholders and would have diluted the equity and interest of the common stockholders of Penn Central Co.?

Mr. PAOLO. Well, it depends upon, again, what developed subsequent to the transfer. It depends upon whether the market value was greater than the net book. There are many intangibles here and it depends more on circumstances. I, at the moment, do not know what the preference of the preferred stockholders is.

Mr. LISHMAN. That is why I asked if you would supply us with your analysis of that.

Mr. PAOLO. I would be glad to; yes, sir.

(See app. A, p. 137.)

Mr. LISHMAN. What steps has the ICC taken to protect the interest of the Penn Central stockholders from suffering a possible diminution in value by reason of this shift of assets?

Mr. KAHN. Mr. Lishman, as you must know, the Interstate Commerce Commission under the presently worded statute, is without jurisdiction to in any way regulate the transfer of nontransportation assets. This is one of the areas where there is a need for additional legislation. It is among the areas being considered for remedial legislation by the Commission, and I would hope the Commission would be able to transmit appropriate draft legislation to the committee within the 2-week period that the vice chairman indicated.

Mr. LISHMAN. Thank you.

Now, you have in front of you a packet of exhibits, packet III, and included in it is a one-page chronology outlining the significant events leading up to the 1970 petition for bankruptcy filed in the U.S. district court in Philadelphia by the Penn Central Transportation Co.

Exhibit I in this packet is a letter dated July 2, 1970, addressed to the SEC Chairman by Chairman Staggers, requesting the SEC to conduct a study of trading in the securities of the Penn Central Co. and its subsidiaries for the period May 1 to June 28, 1970. Has the SEC instituted the study requested in that letter?

Mr. SMITH. Yes, it has, sir, underway at the present time.

Mr. LISHMAN. Who is conducting this study of it on behalf of the SEC?

Mr. SMITH. The Division of Trading and Markets.

Mr. LISHMAN. How many men have been assigned to do this work?

Mr. SMITH. I am advised by Mr. Pollack, the director of that division, four people plus a supervisor.

Mr. LISHMAN. When were these four people assigned?

Mr. POLLACK. Well, two people were working in the trading surveillance area on the questionnaires. Two other people were assigned from a branch of investigation, and I think that the people in the surveillance unit were in communication with the New York Stock Exchange shortly after the bankruptcy or reorganization petition was filed by Penn Central.

The people in the investigation unit shortly after that petition was filed began to collate information that was available to us concerning documents filed and releases made by the company system.

Mr. LISHMAN. Has the Commission itself or any of its supervisory personnel provided any guidelines orally or in writing for the conduct of this study?

Mr. POLLACK. Yes. There were two principal areas which we are inquiring to. One is the adequacy and accuracy of the publicly filed or publicly disseminated information and, two, whether trading by officials of the Penn Central system or persons associated with them or entities associated with them may have traded on the basis of inside information not available to the public or upon the basis of misleading information.

Mr. LISHMAN. Are these guidelines in writing?

Mr. POLLACK. No. They are guidelines that we would follow in any inquiry of this kind.

Mr. LISHMAN. When do you anticipate the study will be completed?

Mr. POLLACK. That, Mr. Lishman, is a difficult question. The securities of the Penn Central system are traded or were traded on, I believe, seven national exchanges as well as the major exchange, trading in a third market as well. The magnitude of the enterprise is going to require considerable time and effort on the part of our personnel, and just from the preliminary inquiry that we have made I would indicate that this is going to be one of the largest inquiries that we have made in the trading area in any specific instance, and it takes months, as you know, from the questionnaires which we have already supplied to you, to get the basic information that you need before you can commence doing the inquiry of persons or entities involved.

Mr. MACDONALD. If I can interject at that point, if that is so, and I am sure it is, why do you not put more people on it?

Mr. POLLACK. We do not have a staff of the kind that you would have in a large agency. What we do is, we assign people in this type of case to work full-time on it, and we permit them to develop the case in all of its aspects.

Mr. MACDONALD. That is not really an answer. If you said this was an emergency, and I think in an economic way it is as much of an emergency as the hijacking of airplanes, and the hijacking of the airplanes, just affected a very few people really, except the idea of it affects everybody, of course, but as I recall there was a whole special section being added to the Department of Justice to take care of that problem. If you said that you were in an economic emergency about this thing, that it needed to be stopped, too, I think you would find Congress rather receptive to giving you some more people. If you cannot transfer people within your own agency to help out in this emergency measure, I think perhaps the Congress would give you some temporary help. What would you think of that?

Mr. SMITH. There are a number of competing demands upon the Commission's time. Obviously, Mr. Chairman, and if it, in the course of the investigation, inquiry, develops that more manpower should be applied to it and we do not have the internal forces to do it, I am sure we would make the appropriate request.

Mr. MACDONALD. Mr. Commissioner, I am not chiding you but your division head has said he only has four people on it and one supervisor, I believe, and when I used the analogy of hijacking I am not going to say it was an economic hijack but, perhaps it was but, in any respect it goes to a fundamental issue in our economy and, of course, the fate of the stock market is reflected throughout our

economy, and I would think it was an emergency, and either transfer some people from other mundane jobs within the agency or ask for more, and I am in the unusual position of urging a bureaucracy to ask for more people.

Mr. SMITH. I wish there were more of you, sir.

Mr. MACDONALD. Well, you never can tell until you make a request how many there are of us. [Laughter.]

Mr. LISHMAN. Well, as part of the study did the SEC send out trading questionnaires to brokers throughout the country asking for information pertaining to trading in shares of Penn Central Co. and any of its subsidiaries?

Mr. POLLACK. Yes, sir.

Mr. LISHMAN. As I understand, the SEC has received responses from more than 200 brokers who represent the bulk of the total trading.

Mr. POLLACK. Correct.

Mr. LISHMAN. Now, we recognize a complete analysis is impossible at this time, but we would like to ascertain whether the SEC has made any preliminary analysis of the responses received to date.

Mr. POLLACK. We have, sir.

Mr. LISHMAN. Could you tell us briefly what the result of the analysis is?

Mr. POLLACK. The analysis indicates that there was a considerable amount of trading which causes us the same concern that the chairman referred to and that we will have to make an inquiry to develop all of the relevant facts concerning the circumstances surrounding the trading as well as the circumstances surrounding filings and dissemination of information by the enterprise.

Mr. LISHMAN. Now, in cooperation with the special subcommittee the SEC has made these responses available for inspection to members of the subcommittee staff. Now even in advance of a complete and detailed report there appears to be evidence indicating that a number of serious violations of law may have occurred by corporate insiders, by persons trading on the basis of inside information.

If you will look at exhibit J, for example, in packet III—is it packet III, yes.

Mr. DINGELL. Mr. Chairman, while that is taking place may I request that the exhibits alluded to as they are referred to by counsel be inserted in the record.

Mr. LISHMAN. They are already in the record.

Mr. DINGELL. They are already in the record. Very good.

Mr. LISHMAN. You will note that this exhibit J contains in the left-hand column the names of 12 brokers. These are a selection of 12 of 25 of the brokers who appeared to have traded most heavily in the Penn Central stock during the period involved. In the first column of exhibit J is shown what is called the normal trading by each of these brokers during a noncritical period of time, and the remaining columns indicate progressively the vast increases in trading in Penn Central stock by each of these 12 brokerage firms. The final column shows the total volume handled by each of the respective brokers from the period March 30 to June 26, 1970.

Now it will be seen from this exhibit that during a normal week the 12 selected brokers handled sales of approximately 30,000 shares.

But commencing in May when the directors of Penn Central Co. had insider knowledge of the precarious financial position of the company the 12 selected brokers' trading increased 10 times, from 30,000 shares to 298,400 shares. Do you see that figure?

Mr. SMITH. Yes, sir.

Mr. LISHMAN. That in the following week it further increased to 493,000 shares, and in the period May 25 to May 29 it hit a peak of 631,000 shares.

On May 28, public announcement was made of the inability to sell the 100 million debenture offering, and the public then became aware of the precarious cash position of the Penn Central Co. Thus the 12 selected brokers, who in the latter week of May sold 631,000 shares, in June since they apparently had unloaded the bulk of their holdings, sold 49,000 shares as shown on this exhibit. In contrast, the public, which had first learned of the true situation on May 28, increased its selling to 504,200 shares the next week.

Now the question I would like to ask is this: Do not these figures indicate a reasonable assumption that someone was trading on the basis of inside information?

Mr. SMITH. I don't believe, Mr. Lishman, from these figures alone that you can—that it would be appropriate for our agency, that is conducting an inquiry to draw any inferences at this time. We have to know a great deal more about who, in fact, was selling, what information there was at that time available to the public. There would be a great many more facts of various kinds that we would want to know before we reached any conclusion of possible violations.

Mr. MACDONALD. I can understand your reluctance to answer but I think I renew my suggestion that you either transfer people within the agency or get some more people. When I used the term economic hijack, I hadn't seen these figures. I am not going to draw any conclusions either because we are going just on the basis of the figures, and if you say there are 12 places, or whatever the figure was, that have to be checked out, you need some people and you need them quickly, and I urge you to do something about it.

Mr. LISHMAN. Does the SEC monitor trading in securities on a regular basis?

Mr. SMITH. We directly monitor the over-the-counter market. We rely on the exchanges to monitor trading on the exchanges and we have oversight and check on their conduct of that function.

Mr. PICKLE. Mr. Chairman, might we get from the ICC an answer to the same question which Mr. Lishman has addressed to Commissioner Smith, namely, if he felt this abnormal trading could have resulted from any inside information.

Mr. MACDONALD. Indeed, Mr. Pickle, we will address the question to the ICC right now.

Mr. HARDIN. I think that is a matter in which the ICC would not be involved, Mr. Chairman. I don't—the inside sales or trading is something that the ICC would not have information on insofar as our—

Mr. PICKLE. My question is not so much your legal obligation or whether you are held administratively responsible in any way.

Mr. HARDIN. I understand.

Mr. PICKLE. What is the opinion of the ICC, if you have one, whether in your judgment, based on these figures, there could or probably was inside information?

Mr. HARDIN. Well, the figures grow and I just am not willing to say that this would be the reason for it, Mr. Pickle. I am just not that certain.

Mr. PICKLE. Would either of you indicate that there is a strong indication that there might have been this possibility?

Mr. SMITH. There is enough for us to continue our study of it.

Mr. MACDONALD. Mr. Dingell. Excuse me, have you finished?

Mr. DINGELL. Mr. Chairman, I would like to have the same question directed to our guests from the ICC that was raised, what monitoring do you do of stock sales that would, and information of that sort that would, lead to your conclusion that there may or may not be insider trading.

Mr. KAHN. None.

Mr. DINGELL. None at all?

Well, we are in this very strange position where you folks receive the reports but you do no monitoring to find out whether there is inside trading.

Mr. KAHN. We receive no reports from the officers, directors of the railroads or the holding companies designated as railroads.

Mr. DINGELL. But under the exemption the ICC on most sections relating to trading in stocks and relating to reports on financial activities inside the company, you receive the report which would give you the information, yet you do no monitoring of the activities that would lead you to a judgment as to whether or not there were violations of the SEC Act or violations of the insider trading regulations of the statute.

Mr. KAHN. I respectfully submit, Congressman Dingell, that if the requirements of the Securities and Exchange Act in that regard are fully applicable, and if there were violations of the provisions prohibiting insider dealing on the basis of insider information, there would be a complete remedy pursuable by the Securities and Exchange Commission.

Mr. DINGELL. And yet you receive the bulk of the reports under the exemptions that are afforded the companies under ICC, that is, common carriers by rail and motor vehicle.

Mr. KAHN. That is like comparing apples and oranges, if I may say so.

Mr. DINGELL. Well, I don't see it that way.

Mr. SMITH. I believe, Mr. Dingell, the requirements for reporting by officers and directors of transactions in their securities on a monthly basis is a provision of the 1934 act, and there is no exemption for publicly held ICC regulated carriers from that requirement. They file those reports with the SEC, sir.

Mr. DINGELL. I see, thank you, Mr. Chairman.

Mr. LISHMAN. Returning to the SEC, is it a fact that you receive every day a report in connection with monitoring which includes a list of the five most active stocks on the New York Stock Exchange?

Mr. SMITH. We do, sir.

Mr. LISHMAN. Was the Penn Central ever included on that list?

Mr. POLLACK. I will have to supply it for the record. Offhand I can't tell you.

(See app. B, p. 169.)

Mr. LISHMAN. In the normal case what steps would the Commission take when activity in a widely held stock issue increased threefold in 1 week and five- and sevenfold in the two succeeding weeks?

Mr. POLLACK. The Exchange, in this case the New York Stock Exchange, has a program similar to the one that we have in the over-the-counter market, which kicks out any trading that varies from parameters that are built into the particular system, and if so they then undertake a preliminary inquiry to determine whether there is some explanation for the particular volume.

Mr. LISHMAN. Did you monitor the trading in the Penn Central Co. during the period March 30 to June 26, 1970?

Mr. POLLACK. It would have been monitored by the New York Stock Exchange. I cannot tell you, Mr. Lishman, whether the volume was such under their parameters to print out this particular stock.

Mr. LISHMAN. Were any steps taken to ascertain the causes of the increased trading?

Mr. POLLACK. They were taken after the filing of the petition for re-organization.

Mr. LISHMAN. Did the SEC consider a suspension of trading?

Mr. POLLACK. No.

Mr. LISHMAN. Why not?

Mr. POLLACK. Because I think at that point the information concerning the filing of the petition in bankruptcy was publicly known. There had been during the early part of 1969 and continuing to the filing of the petition, a release of information indicating a deterioration in the financial condition of Penn Central. For example, there had been a release, as I recall, of the first quarter's earnings which was rather disastrous, sometime in April.

Mr. LISHMAN. Isn't it true that if you had suspended trading for 10 days, you could have ascertained these causes, made them public through a Commission announcement and prevented the insiders from continuing to dump their stock holdings?

Mr. POLLACK. I don't know what dumping you are referring to or whether—

Mr. LISHMAN. I am referring to the volume of trading that is shown in our exhibit J which we have just gone over.

Mr. POLLACK. Well, I think Commissioner Smith has really given you the response to the comment you made, Mr. Lishman.

Mr. SMITH. I believe, Mr. Lishman, that would assume the conclusion of the inquiry.

Mr. MACDONALD. Well, no, it wouldn't, if I could interrupt. It wouldn't. The question isn't whether or not there was this dumping, the question is how come all this trading didn't get the SEC's more vigorous attention, and I am rather curious about that myself.

Mr. POLLACK. Mr. Chairman, where you have a situation such as this, where there is publicly available material indicating a change in the company's financial condition, and where you have information indicating that there have been losses of substantial amounts in the public filings that they are making, you may well find an increase in the volume. That would have been, had you looked at it at the time, a possible explanation for the increase in volume. Now that they have filed a petition in bankruptcy, the question that you ask is was all of

the adverse information out sufficiently so that the investing public had sufficient information or coequal information with those who may have sold stock during this period.

Mr. MACDONALD. I think the main thing is, one of the points of our inquiry into the SEC this morning is, was the SEC diligent enough, was it really bird-dogging the stock. We heard all kinds of rumors here on the Hill, I know I did, I don't happen to trade in the market but we heard all kinds of rumors, so, if we heard them, you must have heard them. What did you do about it, if anything? Just say "Well, the public has been put on notice"?

Mr. POLLACK. I don't know what rumors you have heard.

Mr. MACDONALD. I don't think this was any real surprise to anyone except, I guess it was, the Chairman of the ICC who said he was surprised. [Laughter.]

That they were in financial trouble, but nobody else was. I have known they were in trouble for over a year and I am not an insider.

Mr. POLLACK. What I am saying is, if that was so and the public was aware as a result of the information that you obtained that they were in trouble, that might account for your increasing volume as the situation deteriorated.

Mr. MACDONALD. In other words, you are saying that the insiders just were smarter than the outsiders.

Mr. POLLACK. I can't answer that question.

Mr. MACDONALD. It is not a fair one. I will withdraw it.

Mr. POLLACK. At this point that is the purpose of our inquiry.

Mr. MACDONALD. All right.

Mr. SMITH. The possibility is——

Mr. DINGELL. Could I ask a question here?

Mr. POLLACK. Yes, sir.

Mr. DINGELL. Do you have any coordination, or program for coordinating, with the stock exchange to find out what circumstances that they are monitoring would lead the SEC to think that there might be an excessive amount of trading in a particular stock?

Mr. POLLACK. Yes, sir. Our surveillance——

Mr. DINGELL. All right, what are they?

Mr. POLLACK. Our surveillance section is in daily communication with the New York Stock Exchange. Indeed, they file with us reports, I don't recall the exact period, but they file a report indicating issues that they have looked into. They have, under our division of responsibility, been given the initial responsibility for this. And after the petition in bankruptcy was filed, and after they began to pull the clearing sheets, and after it appeared that, as this committee started its inquiry, this would require an intensive investigation, we used that basic information to send out the questionnaires which Mr. Lishman has referred to. Before you get that information you can't really do this kind of an inquiry, and it takes time to get it.

Mr. DINGELL. Well, all right. What you are telling me here is that really you get the information after the bankruptcy has occurred and the innocents in the market have been fleeced.

Mr. POLLACK. We get information, sir, wherever we get some firm indication that there is something that requires inquiry.

Mr. DINGELL. All right.

Mr. POLLACK. So that sometimes you get it after a bankruptcy because you are not that smart to be able to see in a particular trading pattern that there may be some problem that you ought to look into.

Mr. DINGELL. Well, did you get any notice from the New York Stock Exchange that there was an excessive amount of trading going on in Penn Central stock?

Mr. POLLACK. I can't answer that. I don't believe we did but I would have to check it and furnish it for the record.

(See app. B, p. 170.)

Mr. DINGELL. All right, I would like to have that presented for the record with great clarity and precision. What you are really saying here is you finally got the word about excessive trading in Penn Central stock after the bankruptcy was filed. When did you begin to go into this question of excessive trading in Penn Central stock and begin coordinating with the New York Stock Exchange on this point to find out?

Mr. POLLACK. Our people were working with the New York Stock Exchange shortly after the petition for reorganization had been filed and I understand that the New York Stock Exchange had begun collecting the clearing sheets which are necessary for the obtaining of the brokers who had done the trading that you are interested in inquiring into.

Mr. DINGELL. All right, now——

Mr. POLLACK. If I could just add one thing, Mr. Dingell, you refer to excessive trading.

Mr. DINGELL. Let's not say excessive but extraordinary.

Mr. POLLACK. Whether the chart shows excessive, what they were looking into I don't know, but as you look back on the chart you can see an increase in the trading and some of it is concomitant with the deterioration of the condition of the Penn Central system.

Mr. DINGELL. I want to yield to my friend, but just one question. But what you are saying here really is you have an admirable system of finding out when the horse has been stolen so you can run in and lock the barn door. I am asking you to tell us what information or what devices you have to find out that these companies are in trouble and there might be insider trading going on that ought to be stopped before it takes place. Tell me one thing that you are doing in this particular area.

Mr. POLLACK. Well you can't find it out, sir, before it takes place. What you can see——

Mr. DINGELL. Well you had——

Mr. POLLACK (continuing). Is an increase in trading. When you find there has been an increase in trading and you don't find any public explanation for it which satisfies you, then you will make an inquiry. When you go and you inquire, you will then find out whether and who has done the trading.

Mr. DINGELL. Well you had between March 30——

Mr. POLLACK. Let me tell you one thing.

Mr. DINGELL (continuing). And April 3, and May 28-29, a tremendous upswing in trading. Didn't the SEC have any information as to this upswing in the volume of shares traded during that period? You got your first information as to upswing in trading in June after the petition in bankruptcy was filed, is that what you are telling the committee?

Mr. POLLACK. That information as to trading was not necessarily—I don't know whether we had it. It would be available in the exchange doing the monitoring. If I can just finish, sir, but what I want to say to you is that on April 22, for example, to just pick one item, the Penn Central Transportation Co. announced that its operating results for the first quarter of 1970, I understand, showed an operating loss for the quarter of some \$62 million.

What I am saying is that after that you may find that there was an increase in trading. The person who is doing the surveillance, if the machine showed the increase in volume because of the parameters that had been set, would have made some sort of an inquiry. Now they may have determined, I don't know—

Mr. DINGELL. I want you to tell this committee or to find out or the SEC to find out for this committee or the staff director to find out, what the New York Stock Exchange's rules are on this and what steps were taken by the New York Stock Exchange and when they first found out about this upswing in trading and whether they expressed any concern and what the level of action by them was in both taking disciplinary action internally and also in advising the SEC.

Mr. Chairman, I yield back the time and I hope the staff will go into the question later.

Mr. MACDONALD. Mr. Rogers.

Mr. ROGERS. I understood you to say you didn't know what the criteria were that the stock market used to decide whether they should watch stock sales, when they report to you; is that correct?

Mr. POLLACK. They have standards which they have set which will be established on the basis of the price of the stock with certain variables. When the stocks exceed those variables they will be reported out to the people who are doing the surveillance. They will then look at them to see whether there is some public information which they think is adequate to explain what has happened in the market. If there isn't they may make an inquiry. For example—

Mr. ROGERS. I understand that. I don't need to go any further, thank you on that.

What I am saying is, I understood you to say you didn't know what those were.

Mr. POLLACK. I don't have them in my mind, sir.

Mr. ROGERS. Have they been approved by the Commission?

Mr. POLLACK. I don't know whether we have officially approved them, sir. But they have similar standards to the standards that we use in the over-the-counter market.

Mr. ROGERS. Well, similar—are they the same as what you use on the over-the-counter market?

Mr. SMITH. Mr. Rogers, the standards that are used are different depending upon the market, and depending upon the volume of activity, the volatility in both volume and price of the particular security, and in none of the stock watch programs that I am familiar with do we announce and let people know what our parameters are.

Mr. ROGERS. I think this would be common knowledge, wouldn't it—

Mr. SMITH. No, no.

Mr. ROGERS (continuing). Pretty much as to when you would trigger an investigation. You mean on the market they don't know?

Mr. SMITH. The self-regulatory groups themselves know the parameters that are programed in but they are not known to the general investing market.

Mr. ROGERS. Well, have you approved these parameters that the stock market uses?

Mr. SMITH. Specific parameters the stock market has used in the Penn Central, I don't know that.

Mr. ROGERS. I think they ought to be put in the record if you know them or not, and if you don't approve these, how do you know that they are sufficient to alert you and you, in turn, to alert the public? You don't know what they are?

Mr. SMITH. We know what they are. We have not announced what they are.

Mr. ROGERS. I understood you didn't know. You say they are theirs; well, submit it for the record if you would, then, please.

Mr. POLLACK. If we would submit it for the record you would subject the whole objective of the program—

Mr. MACDONALD. Let's get an answer to the question, it is a good question. Can it be supplied for the record or if it can't how does it embarrass you to do so. If you would explain it to us, we don't mean to be unfair. If there is some practical reason why you don't either OK or not OK standards, just tell us. We are not going to be unreasonable about it.

Mr. SMITH. The reason we don't permit people to know our parameters in surveillance of the over-the-counter market is it lets people who would otherwise intend to manipulate the market know how far they can go without being picked up.

Mr. ROGERS. I understand that and I won't ask you.

Mr. SMITH. And the same thing is true for the New York and AMEX and other markets.

Mr. ROGERS. What I am saying, from the testimony, you don't even know what the stock market standards are, from the testimony I understood. Do you or don't you, and I would like that for the record?

Mr. POLLACK. We undoubtedly have those standards, sir. I don't have those in my mind to discuss them.

Mr. ROGERS. I understand that. I would like that for the record, Mr. Chairman, and how often you review those and if you think they are sufficient and, if so, when you analyze this, why wasn't this triggered in time for you to do something on this Penn Central case. Let me pursue this.

Mr. SMITH. We will supply for the record a description of the stock watch activity in this security.

(See app. B, p. 170.)

Mr. ROGERS. And how often you revise it and if you give approval or you don't, and if you did approve the present standards they are using, the parameters, and if they are sufficient, and why, if they are sufficient, wasn't this Penn Central case triggered and given to you if, in your inquiry, you find there was this excessive selling.

Let me just ask one more question, if you would supply that for the record.

I also would like for the record the names of the employees doing this investigation, when they were assigned, and if they are continuing on this. It is my information, at least we had heard, you only had one man assigned until just recently; is that true?

Mr. POLLACK. I have the people here. My understanding, sir, is that we have had people in the surveillance section collecting those questionnaires since July 6, and that we have two people, plus a supervisor in the investigation section working on this.

Mr. ROGERS. Devoting their full time to this.

Mr. POLLACK. I have the gentleman here, I can find out.

Mr. ROGERS. That is all I want to know.

Mr. MACDONALD. First of all, would you identify yourself for the record.

STATEMENT OF WILLIAM KUEHNLE, SECURITIES AND EXCHANGE COMMISSION

Mr. KUEHNLE. William K-u-e-h-n-l-e, I have been devoting substantially my full time but you have to understand in the logistics of this you really have to have the trading questionnaires first to find out who has been selling. Then you can pursue that and it has taken us considerable time in getting these questionnaires back because of enormous trading, something like 7 million shares over a 3-month period.

Mr. MACDONALD. How many people have you had working with you?

Mr. KUEHNLE. There is one other working with me.

Mr. MACDONALD. That is one.

Mr. KUEHNLE. Also two people from our market surveillance.

Mr. ROGERS. Have all of you been devoting full time or not? Would you say substantially?

Mr. KUEHNLE. I would say substantially full time.

Mr. ROGERS. Have all of you been doing that?

Mr. POLLACK. Two in the market surveillance section on the questionnaires.

Mr. ROGERS. Have all of you been devoting full time or just you?

Mr. KUEHNLE. All substantially, I would say.

Mr. ROGERS. I would like to have it more specific. If you would supply for the record what substantial means, in your language, I don't know what it means, and how long you have been working.

Mr. MACDONALD. Percentagewise, can you do it percentagewise, 80 percent of your time, 90, 20?

Mr. KUEHNLE. I think logistics have to be taken into consideration.

Mr. ROGERS. I just want to know the time you are spending and how many of you are doing it.

Mr. SMITH. We will supply it for the record.

(See app. B, p. 173.)

Mr. PICKLE. I would like to ask a question of the SEC relative to the parameters or guidelines that the stock exchanges furnished. Have there been instances based on information given by the New York Stock Exchange, given to the Surveillance Committee that the SEC has taken action to stop the sale, curtail the sale of securities over the market?

Mr. POLLACK. Yes, sir.

Mr. SMITH. Yes, there have been.

Mr. PICKLE. Many instances?

Mr. POLLACK. We have had one that is similar to this in the Westec case where we took both civil action and we took criminal action.

Mr. PICKLE. Were you able to take action within a period of 30 or 60 days? What was the time interval from the time the information was given to you until the action was taken?

Mr. POLLACK. That was a lengthy investigation. It took a long period of time from the time we made the investigation until we took injunctive action. But what will happen, sir, if there is something that the exchange is aware of, they have the power to suspend trading and we have the power to suspend trading and so you will find from time-to-time that they may suspend securities that are traded on the exchange. We will suspend securities both that may be on the exchange and that are over-the-counter markets.

Mr. PICKLE. So there have been instances of curtailments.

Mr. POLLACK. Yes, sir.

Mr. PICKLE. Were they in volumes larger than the Penn Central?

Mr. POLLACK. I think the volume is only meaningful in terms of the particular events that are occurring, sir, plus the fact that at this point, as we say, we have concern that we are making an inquiry, but whether when we get finished with this investigation what we will be able to do would be foolhardy for me to attempt to tell you at this time. All that we have seen is that there is a large volume of trading, there were a series of events here that took place in a fairly concise period of a deterioration in the company. Whether the people on the inside or people associated with them had the benefit of information that should have been publicly disclosed is something that we intend to inquire into.

Mr. MACDONALD. As you gentlemen can tell, I think, the subcommittee is a little, not upset particularly, but perhaps confused about the relationship between the SEC and the stock exchanges and I, for one, and you don't have to reveal what is in the rules of either or how you differ, but do you approve the rules of the various stock exchanges, either by gentlemen's agreement or by regulation?

Mr. SMITH. Under section 19(b) of the Securities and Exchange Act we do have review authority over certain specified rules and regulations of the exchange.

Mr. DINGELL. Mr. Chairman, that is not a responsive answer.

Mr. MACDONALD. I will yield to you in a minute, John. About that, if you do have the right to approve, and you don't publish whether or not you have approved it but the stock exchange has set up its rules and if they are not revoked, and everyone, you know, the speculators know that you have approved it, so I really don't understand under those circumstances why you are so reluctant to let people know how far they can go, because they do know the rules of the stock exchanges, don't they and, therefore, if you haven't objected to the stock exchanges then they know how far they can go?

Mr. SMITH. I think we are talking about two things, two different things.

The rules of the stock exchange are known. We were talking about stock watch kickout parameters. They are not rules.

Mr. MACDONALD. Would you put that into layman's English for me?

Mr. SMITH. Well, if there is a certain amount of activity in a stock, if volume goes above a certain amount, perhaps associated with a price change of a certain amount, the thousand or so securities traded

on the New York Stock Exchange where behavior goes beyond a certain standard that is programed into the computer, they are reported out and then inquiries are made in their stock watch program and something comparable to what we do in the over-the-counter market although we have no volume information for that market, we have to go solely on price. Then inquiries are made to attempt to find out whether there is an explanation of the activity in the stock. And many stocks have high degrees of volatility both in price and in trading amounts. Many inquiries don't result in suspensions or injunctive actions because there is some apparent explanation for the increased activity.

It is not a matter, I think, of unpublicized rules. The rules are clear, in the sense that you cannot manipulate the market, insiders cannot trade on the basis of material information known only to them, those are the rules.

Mr. MACDONALD. That is why we are holding the hearing today. We thought maybe the rules were better.

Mr. SMITH. And we are conducting a study.

Mr. MACDONALD. On that point what is the relationship between the SEC's ability to prevent trading and that of the stock exchange? You operate in two separate spheres completely or do you coordinate?

Mr. SMITH. My understanding is there is a high degree of coordination between their stock watch programs, both the New York and AMEX, and the SEC's on trading in the markets.

Mr. MACDONALD. What form does the comity take?

Mr. POLLACK. They will take primary responsibility for stocks listed on their exchange and they will conduct inquiries. In some instances, recently, for example, one of the exchanges, on the basis of its surveillance, determined that it could not complete the inquiry because of the absence of the investigatory jurisdiction that it had, and it would then turn that over to us and we would endeavor to complete it.

Mr. MACDONALD. How quickly would the thing occur and how quickly could you get an action on it?

Mr. POLLACK. It would depend. If they could come—for example, we could suspend a trading in a stock in 24 hours time if that were necessary. In some cases it may take a couple of weeks or a month to do an inquiry. It all depends upon the scope.

Mr. MACDONALD. How many people do you have in your division doing the monitoring of the fluctuations?

Mr. POLLACK. Let me get the exact number, if I can—eight people.

Mr. MACDONALD. Eight people, and they monitor all the stock exchanges in the United States.

Mr. POLLACK. Well, as I said—

Mr. MACDONALD. What was the volume last year in the exchange of stocks and bonds?

Mr. POLLACK. I can supply that for the record but first it may be helpful to you, Mr. Chairman—

Mr. MACDONALD. Please supply it for the record but for purpose of conversation give a rough guess.

Mr. POLLACK. I don't know. I can't give you the figure off hand.

Mr. MACDONALD. Mr. Commissioner, can you give a guess, gestimate, I should say.

Mr. SMITH. The volume of trading on the New York Stock Exchange?

Mr. MACDONALD. No, all stock exchanges in your jurisdiction.

Mr. SMITH. New York would be perhaps 75, 80 percent of all.

Mr. MACDONALD. Yes.

Mr. SMITH. It would be well over a billion shares.

Mr. MACDONALD. That is just in New York. And you have got eight people to check all that out.

Mr. POLLACK. No, sir. May I explain under the system of the statute, the exchanges are given fairly comprehensive self-regulatory functions. Indeed, to avoid duplication they do the surveillance on listed stocks. We do it over-the-counter because there isn't a self-regulatory organization that can do that type of surveillance in the over-the-counter market. In the coming year we hope the National Association of Securities Dealers as a result of the automated quotation system they are putting in can take part of this load, but the exchanges regulate their markets under the statute the way it has been set up so that they have primarily responsibility to insure that the trading on their markets is done in a fair and orderly fashion.

Mr. MACDONALD. Right. But you still have jurisdiction over them so you have got the ultimate responsibility, right?

Mr. POLLACK. Correct.

Mr. MACDONALD. You use them as the Congress uses you as a regulatory arm, right?

Mr. POLLACK. That is right, sir.

Mr. MACDONALD. Roughly, but isn't that analogous?

Mr. POLLACK. That is right, sir.

Mr. MACDONALD. But the Congress seems to stay on the regulatory agency more than you do on the stock exchanges.

Mr. POLLACK. If you talk to the stock exchanges, sir, I think they might dispute that with you.

Mr. MACDONALD. Maybe it wouldn't be a bad idea to get someone from the New York Stock Exchange down here.

Mr. POLLACK. I think they are very proud of the program they do in the market surveillance and they would feel, as I have just expressed to you, sir, that we, perhaps are sometimes too pushy. But this will often happen where people have oversight functions, as you well know.

Mr. MACDONALD. It always happens.

Mr. Dingell, do you have any questions?

Mr. DINGELL. Mr. Chairman, I simply wanted to observe here that we still have not been told what device they have between the Commission and the exchange to tip them off as to when a large burst of trading is taking place that needs a look at by the Commission, and what the tools are to suspend trading and how the suspension of trading would have been achieved in this case, and why it was not, why there was not a suspension of trading achieved at an earlier time through this device. And I think it would be very well for us to have the New York Stock Exchange before us to get some answers to them. I would like to get some further answers but I am going to request the staff be instructed to pursue this further by correspondence and the correspondence be incorporated in the record.

(See app. B, p. 178.)

Mr. MACDONALD. It is 10 past the hour and Congress is in session. I would like to ask if you can keep yourself available for a reopening of the hearing next week sometime. It is not within my power to set a fixed date but it will be next week sometime.

Mr. SMITH. I would like to explain that the chairman of our commission was not present today because he was attending a conference of the State Securities Administrators in San Diego and was unable to be present.

Mr. MACDONALD. We know you did a good job representing him.

In the closing statement—I guess we had better hold on to it.

Thank you very much, gentlemen. The hearing is adjourned subject to the call of the Chair.

(Whereupon, at 12:10 p.m., the hearing was adjourned, subject to the call of the Chair.)

APPENDIX A

October 1, 1970

Honorable Dale W. Hardin
Vice Chairman
Interstate Commerce Commission
Washington, D. C.

Dear Mr. Hardin:

During your testimony at the public hearing held by this Subcommittee on September 24, 1970, it was determined that certain additional information, as listed below, would be supplied for the record. The Subcommittee would appreciate being supplied with this material at your earliest convenience.

The material to be supplied for the record is as follows:

1. A statement of the date on which the ICC first obtained a copy of the offering circular dated May 12, 1970. If this circular was not filed with your agency, please indicate whether it should have been filed (Transcript p. 17).
2. A statement whether the offering circulars dated April 27 and May 12, 1970 are substantially identical with the exception of the addition of the names of the members of the underwriting groups in the May 12 circular (Tr. p. 18).
3. Copies of five offering circulars filed with your agency which include all the information required of prospectuses filed with the SEC as set forth in Schedule A of the Securities Act of 1933 (Tr. p. 30).
4. A statement of the requirements for registration as an investment company with the ICC and the requirements for issuance of securities by such a company (Tr. pp 41-42).
5. A list of activities prohibited to investment companies registered with the ICC and a statement whether transactions between affiliates of an ICC investment company

Hon. Dale W. Hardin
October 1, 1970
Page 2

are prohibited or delimited in any way (Tr. p. 42).

6. A clarification of the limitations on the debt issuances of ICC investment companies (Tr. p. 40).
7. An indication whether ICC investment companies are permitted to loan money to their parent companies or to guarantee the obligations of their parents (Tr. p. 40).
8. A statement whether the proposed transfer of assets from the Penn Central Transportation Company to the Pennsylvania Company could have created a preference in favor of the preferred stockholders of the Pennsylvania Company and thereby have diluted the equity and interests of the common stockholders of Penn Central Company (Tr. p. 51).

Although not specifically requested for the record, please also furnish the Subcommittee copies of the five most recent offering circulars filed with the ICC prior to September 24, 1970, if not included in item 3, above.

The Subcommittee also requested an analysis of the differences in accounting treatment by the ICC and SEC with respect to the issuance and marketing of securities. We understand that this will require additional time to prepare because of the coordination necessary. Your report on this particular item can follow your responses to the other items requested.

Your continued cooperation with the Subcommittee will be appreciated.

Sincerely,

HARLEY O. STAGGERS
CHAIRMAN

Interstate Commerce Commission

Washington, D.C. 20423

OFFICE OF THE CHAIRMAN

October 15, 1970

The Honorable Harley O. Stagers
Chairman
Special Subcommittee on Investigations
Committee on Interstate and Foreign Commerce
House of Representatives
Washington, D. C. 20515

Dear Mr. Chairman:

This has further reference to your letter of October 1, 1970, addressed to Vice Chairman Hardin, listing the material to be supplied for the record as determined during the course of the Special Subcommittee on Investigations hearing on September 24, 1970.

The responses enumerated herein correspond to the numbered questions in your letter as follows:

1. The ICC first obtained a copy of the offering circular dated May 12, 1970, on May 19, 1970. It was never officially filed with the ICC but was acquired by the Bureau of Accounts audit staff at the company's offices in Philadelphia. An application to issue the \$100 million debentures had been filed with the Commission in April but was incomplete, e.g., missing from the application were the price, underwriting discounts, interest rate, and redemption price. When these amounts were determined they would have been filed with the Commission together with any amendments such as the revised circular. The missing data never was filed. It cannot be said that the company was delinquent in filing the revised circular since they may have been waiting until all of the missing data could be supplied. The applicant has now requested withdrawal of the application.

2. The offering circulars dated April 27 and May 12, 1970, are substantially identical aside from the addition of the names of the members of the underwriting groups and certain updating in the May 12 circular. The only substantive changes (1) add an option that the holder of each debenture shall

have the right, to be exercised within the 45-day period ending on March 1, 1975, to have the principal of his debentures or any portion thereof which is a multiple of \$1,000, mature on June 1, 1975, and (2) amend the mandatory sinking fund provisions to provide for an annual payment beginning in 1976 of 5% of principal amount of debentures outstanding instead of an amount sufficient to redeem \$5 million principal amount of debentures.

3. Sections 20a and 214 of the Interstate Commerce Act (Act) require that interstate railroad and motor carriers obtain this Commission's authorization to issue securities, with certain exemptions. Section 5(3) of the Act provides, in essence, that whenever a person which is not a carrier is authorized by order of the Commission to acquire control of more than one carrier, such person shall to the extent provided by the Commission in such order be considered a carrier subject to the reporting, accounting and securities provisions of the Act. In general the Commission has subjected holding companies to the said provisions of the Act if their major interest was in transportation and has not subjected holding companies whose major interest was in non-transportation activities. In marginal cases holding companies were subjected to the reporting and/or the accounting provisions of the Act but not to the securities provisions.

In the early sixties there were relatively few non-carrier holding companies in control of carriers but in the last five years the number has increased. In recent times there have also been relatively few applications for authority to issue securities to the general public by either carriers or holding companies subject to the Act, the emphasis being on private placement, borrowings through banks and other institutions, financing without use of securities such as open account advances, credit agreements, security agreements, etc., and in the case of railroads equipment trust agreements. The latter is in form public financing but is generally limited in practice to institutions, and is a popular means of raising funds since title to the equipment is placed in a trustee, thus insulating it from inclusion in the railroad's assets in the event of reorganization. Certain railroads that otherwise would not be able to obtain financing are thus able to finance equipment purchases at reasonable terms.

In all applications for authority to issue securities by carriers or holding companies to the general public a prospectus is required in connection with the application, which prospectus is reviewed along with the

application and changes in the prospectus are required if deemed necessary. There is no statutory or regulatory requirement that the prospectus conform in all respects to that required by the Securities and Exchange Commission. As the basis for a preliminary prospectus, however, the Commission has required that such prospectus include information required in Form S-1 or Form S-2 registration statements under the Securities Act of 1933 issued by the Securities and Exchange Commission (copies attached). The prospectus is then subject to further revision on review by this Commission when deemed desirable.

Attached are five of the most recent prospectus filed with the Commission involving proposed issuance of securities to the general public, as well as three recent circulars relating to proposed issuance of equipment trust certificates.

4. As indicated in our answer to Question 3, holding companies may be subjected to reporting, accounting, and securities provisions of the Act in a proceeding under Section 5 of the Act. There is no requirement as such for registration as an investment company. Holding companies thus subjected are considered for such purposes to be carriers. Attached are rules and regulation governing securities provisions of the Act. The Commission does not have statutory authority to regulate holding companies in control of one carrier or a single integrated system of carriers, and holding companies subjected under Section 5 to the Commission's jurisdiction for reporting, accounting, and securities issuance are limited in number.

5. Holding companies made subject to the Act are required to comply with the reporting, accounting and securities provisions prescribed by the Commission. This Commission lacks statutory authority to regulate transactions between carriers and holding companies unless such transactions involve the issuance of securities. In addition, where carriers or holding companies have a proceeding pending before the Commission, restrictions may be imposed as a condition of approval of such transaction, which conditions may limit inter-company dealings if there is a sound basis for imposing such conditions.

The Commission's lack of statutory authority to regulate carrier financing which does not involve the issuance of securities is a gap long recognized by the Commission, and legislative recommendations to correct this gap were made by the Commission in its annual report to Congress in 1952, 1953, 1954, 1955 and particularly in 1959. If the Commission had authority to regulate all financing of carriers, a certain number of intercompany transactions involving carriers and their holding companies could have been regulated. Legislative proposals requesting authority to regulate intercompany transactions between holding companies and carriers under their control have recently been submitted to Congress on October 6, 1970.

While recognizing the need for general statutory authority the Commission has imposed restrictions quite frequently on carriers with respect to dividends, use of proceeds, etc., in instances where carriers were overcapitalized or were in some other manner failing to maintain what the Commission regards as good standards. Such restrictions necessarily were always done in the form of conditions relating to some pending proceeding such as applications under section 5, 20a or 214 of the Act. More recently such restrictions were imposed in certain cases involving holding companies. In Finance Docket No. 26056, The Greyhound Corporation Securities, decided May 14, 1970, the Commission imposed the condition that without the express approval of the Commission no carrier controlled by The Greyhound Corporation, a holding company, shall (1) make any advances to affiliated companies, (2) encumber any of its assets for noncarrier purposes, or (3) engage in any other intercompany property transaction. In a proceeding in No. MC-F-10486, Matlack, Inc. - Control & Purchase - Baggett Bulk Transport, Inc., decided April 7, 1970, the Commission imposed a condition that Matlack, Inc., and any carrier subsidiary thereof shall not without the express approval of the Commission (1) declare or pay any dividends, (2) make any advances to affiliated companies, (3) encumber any of its assets for noncarrier purposes or (4) engage in any other intercompany property transactions. In other proceedings the Commission reserved authority to issue further orders if such should seem necessary and section 5(9) of the Act provides that the Commission may from time to time, for good cause shown, make such orders, supplemental to any order made under paragraph (1), (2), or (7) of that section as it may deem necessary.

6. There is nothing in the act or in the Commission's security regulations concerning limitations of debt securities for holding companies which have been subjected to the securities provisions of the Interstate Commerce Act. However, debt limitations have been imposed in a long line of Commission decisions going all the way back to Securities of Louisville & Nashville R.R. 76 ICC 718, decided 1923, based on the concept that the capitalization of a corporation should not exceed its capitalizable assets. Capitalization is defined as the sum of capital stock, premium on capital stock and outstanding long term debt, while capitalizable assets are primarily working capital, operating property and investment securities at current value. Accordingly, an applicant will not ordinarily be permitted to increase its capitalization by the issuance of bonds or other debt securities unless it has sufficient capitalizable assets to support the issue. However, security issues have been approved when overcapitalization exists in cases where the Commission found that the overcapitalization was a temporary situation and would be overcome by favorable earnings. Conditions to such an approval have usually been imposed such as restricting the payment of dividends or requiring an infusion of additional equity capital.

7. As indicated in the reply to Question 5, carriers and holding companies may make loans to each other without Commission authorization unless such loans involve the issuance of securities or the assumption of obligation and liability in respect to securities, in which event authorization would be required from this Commission under section 20a or 214. The only exception to the above would be in instances where in an appropriate proceeding filed before the Commission, restrictions on intercompany transactions were imposed. The legislative proposals submitted to Congress on October 6, 1970, were designed in large part to obtain statutory authority to control such transactions.

8. The proposed transfer of assets consisting of stock held in affiliated companies by Penn Central Transportation Company to Pennsylvania Company (Penna. Co.) could have created a preference in favor of preferred stockholders under certain circumstances; for example upon dissolution of Penna. Co. where the assets that were passed down were valued at amounts considerably below their fair market value and the assets of Penna. Co. were not otherwise sufficient to retire preferred stock at par value. However, it can also be argued that the transfer could be detrimental to the preferred shareholders if the assets were valued at amounts in excess of their fair market value since the new debentures would have a prior claim over the preferred stockholders.

But in this instance the question is moot because the preferred stockholders of the Penna. Co. were all former owners of Buckeye Pipe Line Company (Buckeye) common stock who had conversion privileges to exchange their Penna. Co. preferred stock for common stock of Norfolk & Western (N&W), and upon dissolution would have exercised their conversion privilege.

Stockholders of Buckeye exchanged their common shares for \$100-par-value 4 5/8 percent cumulative preferred stock as part of the transaction where Penna. Co. acquired control. Penna. Co. issued 705,898 shares on July 24, 1964.

The merger agreement with Buckeye provided that the holders of preferred stock could exchange their stock for N&W common stock. The initial optional redemption price was also subject to adjustments to protect the holders of preferred stock against dilution of their rights.

The agreement also provided that the Penna. Co. would deposit in escrow pursuant to an escrow agreement with the Chemical Bank New York Trust Company of New York, New York, N&W common stock (shares) as will be necessary to meet the demands of the preferred stockholders.

An analysis of the preferred stockholders at September 30, 1970, who have converted their Penna. Co. preferred stock to N&W common stock is as follows:

Number of Penna. Co. preferred shares issued at July 24, 1964		705,898
Conversions to N&W common stock		
year 1968	73	
year 1969	39	
January 1, 1970 to		
September 30, 1970	<u>225,871</u>	
TOTAL CONVERTED		<u>225,983</u>
Number of shares outstanding at September 30, 1970		<u>479,915</u>

From the above analysis it is clear that there was considerable activity in 1970 and that there will be a considerable number of preferred shareholders of Penna. Co. who will also exercise this conversion privilege in the near future. The primary reasons for the conversion are that because of the interruption of dividend payments by the Penna. Co. and the subsequent loss of income to these preferred stockholders, and the financial problems of Penna. Co.'s parent, the Penn Central Transportation Company.

In conclusion, the question of dilution of equity of the common stockholders because of an intercompany transfer of assets which may benefit the preferred stockholders is not a material factor in this transaction, principally because of the conversion privilege to N&W common stock which we presume will eventually be exercised by the majority of the preferred stockholders. Therefore, the transfer of assets between the two corporations at other than fair market value would have no effect on the stockholders' rights, primarily because of the conversion option to N&W common stock.

Our concern in intercompany transactions are where assets are being transferred from the carrier at amounts substantially below fair market which will result in a dissipation of these assets.

We are also concerned where assets are transferred between companies to show profits, particularly where the carrier is filing an unconsolidated report which could mislead investors and others as to the profit performance of the carrier. This is particularly important when the assets of the carrier are a major investment in a holding company structure, and where a misstatement of earnings could be a factor in evaluating the overall performance of the holding company by financial analysts and investors.

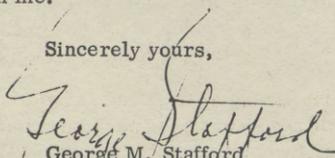
The company representatives claim that the net book value at which the stock was being transferred was very close to fair market value. Although the proposed transfer of common stock of Manor Real Estate Company and Despatch Shops Inc. did not take place, there was a transfer of the common

stock of Clearfield Coal Company on March 31, 1970. In our investigation into the Penn Central Transportation Company and its affiliates, we are reviewing all major intercompany transfers of assets between the various companies affiliated with Penn Central Transportation Company and the transfer of the assets and resulting reporting of profits on the Clearfield Coal Company transaction will be thoroughly analyzed.

The requested analysis of the difference in accounting treatment by the ICC and SEC with respect to the issuance and marketing of securities is in process and will be submitted to you at the earliest practicable date.

If there are further questions on any of the matters discussed herein please do not hesitate to call upon me.

Sincerely yours,


George M. Stafford
Chairman

Enclosures

Interstate Commerce Commission

Washington, D.C. 20423

OFFICE OF THE CHAIRMAN

November 25, 1970

Honorable Harley O. Staggars
Chairman
Special Subcommittee on Investigations
Committee on Interstate and Foreign Commerce
House of Representatives
Washington, D. C. 20515

Dear Chairman Staggars:

This has further reference to your letter of October 1, 1970, addressed to Vice Chairman Hardin, particularly to the penultimate paragraph regarding the submission of an analysis of the differences in accounting treatment of certain material items by this Commission and the Securities and Exchange Commission.

As stated in the testimony of Mr. Matthew Paolo, Director of our Bureau of Accounts, before the Subcommittee, there are a few items in which our accounting rules differ from generally accepted accounting principles adhered to by SEC. These items, hereinafter discussed, are: (a) Deferred Income Taxes, (b) Material Prior Period Items, and (c) Consolidation of Subsidiaries.

(a) Deferred Income Taxes. The matter of accounting for deferred income taxes has been the subject of several ICC proceedings. The Twelfth Report by the Committee on Government Operations, on the report from its Subcommittee on Legal and Monetary Affairs, entitled "Railroad Accounting Procedures," submitted to the House of Representatives, 85th Congress, 1st Session (House Report No. 1167) on August 14, 1957, recommended that the ICC consider institution of rulemaking procedures with a view (1) to conforming financial statements submitted to stockholders and investors to generally accepted accounting principles, and (2) to establishing reserves for deferred Federal income taxes.

By Notice dated February 9, 1959, copy enclosed, the ICC issued a statement setting forth its policy with respect to Accounting for Federal Income Taxes. This Notice provided that the amount of reduction in Federal income tax payments realized for each year and the accumulated sum for the current and prior years due to use of accelerated depreciation in tax returns will not be recorded in the accounts, but will be disclosed by explanatory notes in reports filed with the ICC. Carriers were urged to disclose the same information in reports to stockholders and others. On February 1, 1963, as a culmination of a proposed rulemaking procedure, the ICC issued a report and order in docket No. 34178, Accounting for Federal Income Taxes Under New Depreciation Guideline Lives and Investment Tax Credit (copy enclosed). For reasons stated therein it concluded no change in the accounting rules was necessary and affirmed its policy statement set forth in the Notice of February 9, 1959.

In 1960 the ICC instituted rulemaking procedure relating to the applicability of its accounting rules to financial statements of carriers contained in reports to stockholders or otherwise released to the public. By report and order dated January 25, 1962, in docket No. 33581, Financial Statements Released by Carriers (copy enclosed), it found that, "Carriers desiring to do so may prepare and publish financial statements in reports to stockholders and others, except in reports to this Commission, based on generally accepted accounting principles for which there is authoritative support, provided that any variance from this Commission's prescribed accounting rules contained in such statements is clearly disclosed in footnotes to the statements."

From the foregoing it can be seen that, although the ICC does not permit carriers to record provision for deferred income taxes in its accounts, the effect of the various accounting methods permitted for income tax purposes is clearly disclosed in annual reports filed with us and in reports to stockholders and others. Of course, the basis of the ICC ruling is "The present day shipper should not be required to provide from current freight rates for possible increased tax rates of the indefinite future."

(b) Material Prior Period Items. The Commission is continually striving to conform its accounting rules to generally accepted accounting principles as promulgated by the Accounting Principles Board of the American Institute of Certified Public Accountants, whenever possible in the light of its responsibilities under the provisions of the Interstate Commerce Act.

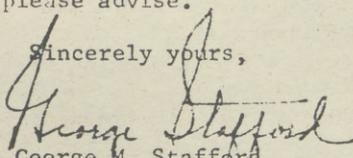
In December 1966, the Accounting Principles Board issued an opinion with respect to accounting and reporting of Extraordinary Items and Prior Period Adjustments. After considerable study, review and consultation with other regulatory agencies, including SEC, we issued on May 25, 1967 a Notice of Proposed Rulemaking relating to this matter. Final order prescribing amendments to the Uniform System of Accounts was issued on September 1, 1967. The rules prescribed conformed generally to the Opinion except that we provided for inclusion of material prior period items in the income statement, whereas under generally accepted accounting principles they are treated as adjustments of the beginning balance of surplus or retained income. We should bear in mind that such items, using the Board's language, are "rare." The effect of either procedure is the same on a company's financial position at the end of any given year. The ICC requires full disclosure and explanation of such items. We were unable to follow the method prescribed by the Board since our rules provide that carriers' reports must be in accordance with its books of account and we allow no adjustment in the accounts once they have been closed for the year and the annual report filed.

(c) Consolidation of Subsidiaries. The ICC requires companies subject to its jurisdiction to file unconsolidated financial statements and to carry their investments in other companies at cost. The parent company's equity in the income of such companies is not accounted for until received through payment of dividends. However, railroads have been instructed to disclose by explanatory notes in their annual reports to the ICC their share of accumulated undistributed earnings and losses since acquisition of unconsolidated affiliated companies. At the present time, ICC is reviewing this matter to determine whether or not a rulemaking proceeding should be initiated to require equity accounting for investments in unconsolidated affiliated companies.

In general, the SEC requires that consolidated financial statements be prepared and that any subsidiaries not consolidated be carried at cost plus equity in earnings (losses) since acquisition. Most railroads include consolidated financial statements in their reports to shareholders.

I believe this completes the information requested in your letter of October 1, 1970, for inclusion in the record of the hearing on September 24, 1970, of the Special Subcommittee on Investigations. If I can furnish any other information on this matter, please advise.

Sincerely yours,


George M. Stafford
Chairman

Enclosures

cc: Honorable Hamer H. Budge
Chairman
Securities and Exchange Commission
500 North Capitol Street, N. W.
Washington, D. C. 20549

21684

INTERSTATE COMMERCE COMMISSION

No. 33581**FINANCIAL STATEMENTS RELEASED BY CARRIERS**

Decided January 25, 1962

Adherence to the Commission's accounting rules by carriers in preparing financial statements other than those filed with the Commission found not necessary, provided divergencies are disclosed in footnotes.

REPORT OF THE COMMISSION**DIVISION 2, COMMISSIONERS FREAS, GOFF, AND HERRING****By DIVISION 2:**

By notice of proposed rulemaking published in the Federal Register on October 15, 1960 (49 CFR 25), the Commission, division 2, initiated an investigation as to the applicability, pursuant to provisions of the Interstate Commerce Act, of the rules in the Commission's uniform system of accounts to financial statements of carriers contained in their reports to stockholders or otherwise released to the public. The investigation was instituted as a result of a petition filed by Arthur Andersen & Co., a firm of certified public accountants, requesting that the Commission issue a rule or decision on this point. The petitioner's position is that carriers should be free to prepare and publish financial statements for release to stockholders and others, except reports filed with us pursuant to our orders, in accordance with what is described as "generally accepted accounting principles"; and that the Commission should decide that such procedure would not be considered as a violation of our regulations and the Interstate Commerce Act.

The notice contained a proposed rule which would prohibit carriers subject to our accounting regulations from including in their annual reports to stockholders or otherwise released to the public, financial statements which are inconsistent with the corporate books of accounts, which are maintained in conformity with our uniform systems of accounts, and with reports filed with us by or on behalf of such carriers. Interested parties were invited to submit in writing their views and comments for our consideration.

Many responses have been received from carriers and others, including the American Institute of Certified Public Accountants and individual firms of certified public accountants, who audit financial statements of carriers, expressing opposition to the proposed rule. The substance of these objections is that the Commission should not

as a matter of policy deny carriers the right to furnish their stockholders or to otherwise publish financial statements based on accounting methods for which there is substantial authoritative support under generally accepted accounting principles. The certified public accountants point out that they are called upon to express their professional opinions concerning financial statements contained in reports prepared for stockholders and in other situations; and that adoption of the proposed rule would unduly interfere with the orderly performance of their duty and obligation in certifying financial statements for their clients. The response filed by the American Institute of Certified Public Accountants contains the following statements:

We respectfully suggest that, as a matter of policy, the Commission should not deny to the investing public, as the proposed rule would do, the presentation of significant financial information upon a basis which has substantial authoritative support and as to which the investing public ought reasonably to be informed.

The managements of private enterprises have a responsibility and the freedom to report financial information to investors and creditors in a manner designed to best serve the needs of such investors and creditors. There would seem to be no good reason why the managements of companies subject to the Commission's jurisdiction should not have the same responsibility and freedom to make such reports as do the managements of other private enterprises.

The American Trucking Associations, Inc., American Waterways Operations, Inc., Investment Bankers Associations of America, numerous individual motor carriers of property and motor carriers of passengers, certain railroad companies and pipe line companies, and others filed responses opposing the proposed rule basically supporting these reasons of the certified public accountants; namely, that they should be free to publish financial statements in reports to stockholders and others in accordance with generally accepted accounting principles.

The American Institute of Certified Public Accountants, in opposing adoption of the proposed rule, suggests that any variance between financial statements prepared and certified by public accountants, based on generally accepted accounting principles, and statements prepared and filed with us in accordance with the uniform accounting requirements of this Commission could be disclosed in reports certified by public accountants. The New York Stock Exchange expresses interest in this matter, which affects financial statements of carriers whose stock is traded on the exchange, and makes the same suggestion with respect to disclosure of any variance that may occur.

The term "generally accepted accounting principles" is commonly used to denote broad basic principles which have received general business acceptance, with considerable tolerance for variation among different industries because of special conditions or long established

usage. The Commission's accounting rules are in accordance with generally accepted accounting principles. Nevertheless, disagreement has been expressed by Arthur Andersen & Co., the petitioner, and others filing responses in this proceeding, to our rules because these rules do not provide for including in financial statements as a current tax expense and under liabilities so-called deferred income taxes. Deferred taxes are said to exist as a result of accelerated depreciation allowed by the Internal Revenue Service in computing Federal income taxes on purchases of new property, such deferred taxes being the amount that may be payable in later years because of accelerated, or increased, depreciation allowances early in the life of property and corresponding decreased depreciation allowances in later years.

There is considerable diversity of opinion among accounting authorities with respect to the matter of the proper method of accounting for so-called deferred taxes. Showing deferred taxes in financial statements, and also various optional methods of depreciation authorized in the tax regulations, commonly are recognized in nonregulated industries as being in accord with "generally accepted accounting principles"; other tax regulations also have had an important impact on generally acceptable accounting principles. On the other hand, this Commission and other governmental agencies, for regulating purposes, have placed emphasis on the necessity of industry-wide uniformity in accounting and have not sanctioned the same degree of flexibility in accounting concepts that prevails among nonregulated companies.

There is considerable support for the position taken by the petitioner and others in this proceeding for an accounting procedure of providing for deferred Federal income taxes, resulting from accelerated depreciation, in computing net income in financial statements, as well as for the procedure prescribed by this Commission's uniform rules which requires that income taxes are to be recorded as tax expenses in the year when the tax becomes payable and not in an earlier year. However, after carefully considering this matter, we believe that the treatment of tax deferrals in financial statements in reports to stockholders and otherwise published by carriers need not be made in strict accordance with the proposed rule herein and that such rule should be modified. In our opinion, the following rule is reasonable: Carriers desiring to do so may prepare and publish financial statements in reports to stockholders and others, except in reports to this Commission, based on generally accepted accounting principles for which there is authoritative support, provided that any variance from this Commission's prescribed accounting rules contained in such statements is clearly disclosed in footnotes to the statements. This rule,

in our opinion, will not cause any undue burden on the carriers, is in accordance with the public interest, and should be adopted, and we so find. We further find that such rule should be made effective as provided for in the order.

An appropriate order reflecting this action will be entered.

INTERSTATE COMMERCE COMMISSION
Washington, D.C.

February 9, 1959

NOTICE TO ALL CARRIERS SUBJECT
TO PRESCRIBED ACCOUNTING RULES

Accounting for Federal Income Taxes

The Commission has given consideration to provisions of section 167 of the Internal Revenue Code of 1954, which permit allowances for depreciation to be computed by accelerated methods. The election to use such allowances reduces Federal income taxes thereby increasing net income during the early life of property newly acquired but, by decreasing depreciation deductions in later years, permits no more to be deducted for any unit of property than would be available under straight-line depreciation.

This optional income tax treatment presents a problem in administering prescribed accounting regulations. It has been studied by other Federal agencies which regulate accounts, by State commissions in connection with the rate making function, and by the accounting profession. One approach has been to charge to operating expenses the same amounts that are claimed as depreciation allowances for income tax purposes. This has the advantage that depreciation charges within net income are comparable to the basis on which income taxes are computed. Another view has been that income should be normalized by including therein the amount by which taxes are reduced when depreciation allowances are high to create a reserve which would be reversed as depreciation allowances diminish.

The Commission has repeatedly held that depreciation by the straight-line method best serves the purpose of assigning the service loss on transportation property to income of the years in which the property is in revenue service. The use of other depreciation methods for income tax purposes is not an acceptable reason for changing our depreciation accounting requirements. Accelerated depreciation allowances available under the revenue code provide an earlier recovery of an investment with resultant tax advantages, and are not intended to be a standard for measuring the rate at which service loss is incurred.

When an available depreciation allowance produces a reduction in Federal income taxes, no matter how temporary the benefit may be the effect on net income should be the same as a reduction in taxes produced by lower tax rates. Possible income taxes to be

assessed in the future are not an element of tax expense for the current year. As to depreciable property with an expected life of thirty years, or even less, it is illogical to expect that tax reductions resulting from accelerated depreciation allowances can be matched with tax increases of the future. New property units acquired in the future will provide increased depreciation allowances to offset decreasing allowances for older units. Furthermore, income tax rates and tax procedures are subject to change from year to year, and the computation of income taxes differs as between carriers, and for any carrier differs as between years, in too many respects to justify special provision for a fluctuation in taxes resulting only from depreciation allowances.

After consideration of the views for and against normal income taxes, different in amount from the income taxes actually payable, it has been decided that the charge to income each year for that year's Federal income taxes should be the amount produced by application of the effective tax regulations to transactions within the year. The present day shipper should not be required to provide from current freight rates for possible increased taxes of the indefinite future.

The amount of reduction in Federal income tax payments realized for each year and the accumulated sum for the current and prior years due to the use of accelerated depreciation in tax returns will be disclosed by explanatory notes in reports filed with this Commission. Carriers are urged to disclose this information in their reports to stockholders and in financial statements released to the press.

As a statement of policy this notice will be served on all carriers subject to prescribed accounting regulations, and notice will be given to the general public by depositing a copy in the office of the Secretary of the Commission in Washington, D.C., and by filing it with the Federal Register.

By the Commission, division 2.

HAROLD D. McCOY
Secretary

INTERSTATE COMMERCE COMMISSION

No. 34173

SERVICE DATE
FEBRUARY 13, 1963ACCOUNTING FOR FEDERAL INCOME TAXES UNDER NEW
DEPRECIATION GUIDELINE LIVES AND INVESTMENT TAX CREDIT

Decided February 1, 1963

In the application of uniform systems of accounts, actual Federal income taxes payable for each year, based on the effective tax regulation for the year, shall be recorded in the tax accounts. Change in present accounting regulations in respect of tax reductions resulting from tax-depreciation guideline lives and investment tax credit, found to be not necessary. Appropriate order entered.

REPORT OF THE COMMISSION

DIVISION 2, COMMISSIONERS FREAS, WEBB, AND HERRING

BY DIVISION 2:

By notice of proposed rule-making published in the Federal Register on November 3, 1962 (27 F.R. 10909), we initiated an investigation with respect to carriers in all modes of transportation subject to the Interstate Commerce Act concerning the matter of accounting rules to be applied for Federal income taxes in connection with (1) the new shortened tax-depreciation guideline lives authorized by the Internal Revenue Service in Revenue Procedure No. 62-21, July 1962, and (2) the investment tax credit authorized in the Revenue Act of 1962.

The material facts bearing on the issue here presented are not in dispute, and a public hearing or oral argument would serve no useful purpose. In view of the close proximity to the closing of the carriers' books for the year 1962, a preliminary notice, dated December 17, 1962, to all carriers subject to the Commission's accounting rules, embodying our ultimate findings on the issue before us, was served on December 20, 1962.

The new tax-depreciation guideline lives authorized in Revenue Procedure No. 62-21 is a significant development in income tax methods and procedures. This tax revenue procedure authorizes substantial reductions in the lives of depreciable property effective with tax returns for the year 1962. For example, the tax regulation specifies depreciation guideline lives for railroad locomotives, freight and passenger cars, and other similar equipment as 14 years, compared with presently-used service lives averaging 15 to 25 years for locomotives, and 25 to 30 years for other equipment; for bridges, trestles and culverts, elevated structures, shops and engine houses, and similar structures, the guideline life is 30 years, compared with presently-used service lives averaging about 50 to 70 years, depending upon the structural material. Similar substantially-shortened guideline lives are specified for many other classes of property.

The tax-depreciation guideline lives so authorized may be used by taxpayers for three years without being questioned by Internal Revenue Service, regardless of the taxpayers' past experience with respect to life-of-service performance in replacing property. The guideline lives so used for tax-depreciation deductions are subject to adjustment in later years if conditions prescribed in the tax regulations as to replacement performance and formula for depreciation reserve ratios prescribed in life adjustment tables are not met. After the expiration of the three-year period prescribed in the tax regulations, ending with the year 1964, the shortened guideline lives must be justified by demonstrating a replacement performance policy through the reserve ratio tests. If the prescribed tax guideline ratio tests are not met, the service lives used for tax depreciation will be lengthened percentage-wise annually.

The Revenue Act of 1962 contains an important provision known as the "Investment Tax Credit." Under this provision the taxpayer is allowed a credit against taxable net income equal to 7 per cent of the cost of new property acquired during the taxable year, provided the property has a life of 3 years or more. The credit for property with a life between 4 and 8 years is somewhat less than 7 per cent. This tax credit is to be applied to offset tax liability up to a specified amount and a percentage of tax liability in excess thereof. The investment tax credit is to be deducted from the base upon which tax-depreciation deductions are to be allowed. For example, a taxpayer purchasing new property for \$100,000 becomes entitled to a tax credit of \$7,000 against his tax liability for the current year; this credit is then applied to reduce the base to \$93,000, upon which current and future tax-depreciation deductions are allowed.

In recording depreciation in the corporate books of account under our accounting rules, as distinguished from Federal income tax returns, carriers are required to use the straight-line method of depreciation applied to the estimated useful life, based on past experience and informed judgment as to probable future service, for each class of property. The initial estimated useful life is revised and rates of depreciation are adjusted as may be found necessary from time to time as a result of changes in conditions. Depreciation procedures are so prescribed by us in uniform systems of accounts for financial accounting of carriers, notwithstanding unlike depreciation methods and other special provisions authorized by the Internal Revenue Service for tax purposes.^{1/}

Tax-depreciation deductions, based on the tax-depreciation guideline lives, will be much larger in amount than book depreciation computed under this Commission's accounting rules in

^{1/} Uniform systems of accounts for carriers in the several modes of transportation, Code of Federal Regulations, Title 49. The rules for motor carriers provide that the straight-line method of computing depreciation shall be employed, except that the mileage method may be used for automotive equipment, in which event the rate per mile shall be applied to the number of miles traveled each year.

the early years of the service lives of facilities. Question therefore arises, (1) should the actual Federal income tax expense of each year, based on taxable income reported in the tax return for the year, be recorded in the corporate books of account and in financial statements to the Commission; or (2) should the tax reduction realized because of tax depreciation in excess of book depreciation be treated as tax deferment and included in a suspense or reserve account to provide for taxes that may have to be paid in later years to offset the earlier tax reductions, under a continuing procedure for year-by-year equalization of tax charges in computing net income, without regard to actual tax liability in each year's tax return.

Essentially the same question arises as to whether tax reduction realized from the investment tax credit should be included in the corporate income reports and financial statements each year or be treated as tax deferment under a continuing procedure for year-by-year equalization of tax charges. Such income equalization procedure could be accomplished in the same manner as tax reduction realized through use of the tax-depreciation guideline lives, or by regarding the investment tax credit as a reduction in the cost of property and the depreciation base.

Carriers in the several modes of transportation, public accountants, and others filed responses in this proceeding pursuant to our Notice of Proposed Rule Making inviting views and comments. The responses contained divergent views on the question of proper accounting for the tax reductions hereinbefore discussed. Respondents expressing views in favor of treating the reduction in tax payments resulting from use of depreciation guideline lives and the investment tax credit as tax deferment and then equalizing the distribution of such payments to income by a process of interperiod tax allocation, assert that this procedure is essential for a proper matching of revenues and expenses for each year, and would result in equitable allocation of income taxes to expenses each year in relation to earnings for the year even though the amount so allocated is different from actual tax payment for the year. Some respondents assert that the investment tax credit is a true reduction in cost of property, the purchase of which gives rise to the credit. These respondents declare that unless allocation or equalization of tax payments in the accounts is authorized in order to compensate for the differences between tax depreciation and book depreciation, and also for the investment tax credit, the reported net income from year to year will be distorted and unrealistic.

These proponents of deferred-tax accounting propose that, accounting-wise, the excess of normal income taxes (taxes that would have been payable without the benefit of depreciation guideline lives and investment tax credit) over actual tax payments should be placed in a suspense or equalization account for later year-by-year allocations, so that taxes reported in financial statements each year would agree with the taxes that would otherwise be payable each year on the basis of the straight-line depreciation recorded in the corporate accounts.^{2/}

^{2/} Of the investment tax credit realized, some of the respondents would treat 52 per cent of the amount as deferred taxes and the remaining 48 per cent as a true reduction of taxes for the year in which the tax credit is obtained.

In advocating this tax-deferral or tax-equalization accounting procedure, they point out that such method of accounting has the approval of public accountants as being in accordance with "generally accepted accounting principles," and request us to modify our rules and authorize that procedure. The term "generally accepted accounting principles" is commonly used to denote broad basic principles which have received general business acceptance, with considerable tolerance for variation among different industries because of special conditions or long-established usage.

On the other hand, most of the responses filed by respondents are in opposition to tax-deferment or tax-equalization procedure. They express the view that actual taxes payable for each year, based on the effective tax regulations of the year, is the only liability to the Government and the true amount to be recorded in the corporate accounts and financial statements each year for tax expenses; and that when taxes so computed are reported in the tax return for a year no deferred-tax liability remains unpaid for the year and no amount should be recorded in the accounts and financial statements for unpaid taxes or for tax-liability contingency. These respondents assert that tax-deferment or tax-equalization procedure, whereby payments would be allocated over a period of years and not recorded as tax expenses in the year for which the payment is made, would obscure the true tax expense for each year and obliterate the tax consequences of transactions and events within each year.

In opposing tax-deferral or tax-equalization accounting procedures the opponents declare that the ever-changing tax system does not lend itself to interperiod tax allocation because of uncertainties associated with such allocation; and that tax reductions resulting from tax-depreciation guideline lives and investment tax credit are just as real as though statutory tax rates were decreased.

The question presented in this proceeding with respect to accounting for the tax effect of tax-depreciation guideline lives and the investment tax credit is essentially an extension of the matter of accounting for tax consequences of accelerated depreciation pursuant to provisions of section 167 of the Internal Revenue Code of 1954, previously considered by us, and which resulted in our statement of policy dated February 9, 1959, wherein we stated that the actual Federal income tax expense of each year, based on taxable income reported in tax returns, shall be recorded in carrier's books of account and in financial statements to the Commission. Accounting for Federal Income Taxes, 24 F.R. 1401.3/ That statement of policy contains the following conclusions:

When an available depreciation allowance produces a reduction in Federal income taxes, no matter how temporary the benefit may be, the effect on net income should be the same as a reduction in taxes produced by lower tax rates. Possible income taxes to be assessed in the future are not an element of

3/ Reproduced as appendix A to this report.

tax expense for the current year. As to depreciable property with an expected life of thirty years, or even less, it is illogical to expect that tax reductions resulting from accelerated depreciation allowance can be matched with tax increases of the future. New property units acquired in the future will provide increased depreciation allowances to offset decreasing allowances for older units. Furthermore, income tax rates and tax procedures are subject to change from year to year, and the computation of income taxes differs as between carriers, and for any carrier differs as between years, in too many respects to justify special provision for a fluctuation in taxes resulting only from depreciation allowances.

After consideration of the views for and against normal income taxes, different in amount from the income taxes actually payable, it has been decided that the charge to income each year for that year's Federal income taxes should be the amount produced by application of the effective tax regulations to transactions within the year. The present-day shipper should not be required to provide from current freight rates for possible increased taxes of the indefinite future.

We have carefully considered the divergent views and all of the arguments presented by the respondents in this proceeding and affirm the ultimate findings contained in our preliminary notice herein that no sufficient justification has been presented to warrant a change in our present accounting rules and the statement of policy previously announced under date of February 9, 1959. We reach the same conclusions set forth in that statement of policy, that actual Federal income taxes payable for each year, based on the effective tax regulations for the year, shall be recorded in the tax accounts of the carriers' books of account, and in financial statements.

Carriers are presently required to disclose, in explanatory notes in their annual reports to us, reductions in income taxes because of accelerated depreciation pursuant to section 167 of the Internal Revenue Code. The requirement for disclosure will be extended to apply to tax reductions attributable to tax-depreciation guideline lives, as well as the investment tax credit, and appropriate procedural rules will be issued to implement this requirement.

An appropriate order will be entered discontinuing the proceeding.

APPENDIX A

INTERSTATE COMMERCE COMMISSION
Washington, D.C.

February 9, 1959

NOTICE TO ALL CARRIERS SUBJECT
TO PRESCRIBED ACCOUNTING RULES

Accounting for Federal Income Taxes

The Commission has given consideration to provisions of section 167 of the Internal Revenue Code of 1954, which permit allowances for depreciation to be computed by accelerated methods. The election to use such allowances reduces Federal income taxes thereby increasing net income during the early life of property newly acquired but, by decreasing depreciation deductions in later years, permits no more to be deducted for any unit of property than would be available under straight-line depreciation.

This optional income tax treatment presents a problem in administering prescribed accounting regulations. It has been studied by other Federal agencies which regulate accounts, by State commissions in connection with the rate making function, and by the accounting profession. One approach has been to charge to operating expenses the same amounts that are claimed as depreciation allowances for income tax purposes. This has the advantage that depreciation charges within net income are comparable to the basis on which income taxes are computed. Another view has been that income should be normalized by including therein the amount by which taxes are reduced when depreciation allowances are high to create a reserve which would be reversed as depreciation allowances diminish.

The Commission has repeatedly held that depreciation by the straight-line method best serves the purpose of assigning the service loss on transportation property to income of the years in which the property is in revenue service. The use of other depreciation methods for income tax purposes is not an acceptable reason for changing our depreciation accounting requirements. Accelerated depreciation allowances available under the revenue code provide an earlier recovery of an investment with resultant tax advantages, and are not intended to be a standard for measuring the rate at which service loss is incurred.

When an available depreciation allowance produces a reduction in Federal income taxes, no matter how temporary the benefit may be the effect on net income should be the same as a reduction in taxes produced by lower tax rates. Possible income taxes to be assessed in the future are not an element of tax expense for the current year. As to depreciable property with an expected life of thirty years, or even less, it is illogical to expect that tax reductions resulting from accelerated depreciation allowances can be matched with tax increases

of the future. New property units acquired in the future will provide increased depreciation allowances to offset decreasing allowances for older units. Furthermore, income tax rates and tax procedures are subject to change from year to year, and the computation of income taxes differs as between carriers, and for any carrier differs as between years, in too many respects to justify special provision for a fluctuation in taxes resulting only from depreciation allowances.

After consideration of the views for and against normal income taxes, different in amount from the income taxes actually payable, it has been decided that the charge to income each year for that year's Federal income taxes should be the amount produced by application of the effective tax regulations to transactions within the year. The present-day shipper should not be required to provide from current freight rates for possible increased taxes of the indefinite future.

The amount of reduction in Federal income tax payments realized for each year and the accumulated sum for the current and prior years due to the use of accelerated depreciation in tax returns will be disclosed by explanatory notes in reports filed with this Commission. Carriers are urged to disclose this information in their reports to stockholders and in financial statements released to the press.

As a statement of policy this notice will be served on all carriers subject to prescribed accounting regulations, and notice will be given to the general public by depositing a copy in the office of the Secretary of the Commission in Washington, D. C., and by filing it with the Federal Register.

By the Commission, division 2.

HAROLD D. McCOY,
Secretary.

No. 34178

ACCOUNTING FOR FEDERAL INCOME TAXES UNDER
NEW DEPRECIATION GUIDELINE LIVES AND
INVESTMENT TAX CREDITO R D E R

At a Session of the Interstate Commerce Commission, Division 2, held at its office in Washington, D. C. on the 1st day of February, 1963.

The Commission having under consideration a notice of proposed rule-making in this proceeding published in the Federal Register of November 8, 1962 (27 F.R. 10909) pertaining to the above referred to accounting matter and responses to said notice; and

It appearing, That a preliminary notice, dated December 17, 1962, announcing the ultimate findings of Division 2 was served on December 20, 1962;

And it further appearing, That investigation of the matters and things involved in this rulemaking proceeding has been made, and said Division, on the date hereof, having made and filed a report containing its findings of fact and conclusions thereon:

It is ordered, That this proceeding be, and it is hereby, discontinued.

By the Commission, Division 2.

(SEAL)

HAROLD D. McCOY,
Secretary.

APPENDIX B

October 1, 1970

Honorable Richard B. Smith
Commissioner
Securities and Exchange Commission
Washington, D. C.

Dear Mr. Smith:

During your testimony at the public hearing held by this Subcommittee on September 24, 1970, it was determined that certain additional information, as listed below, would be supplied for the record. The Subcommittee would appreciate this material being supplied at your earliest convenience.

The material to be supplied for the record includes:

1. A statement whether, pursuant to Schedule A to the Securities Act of 1933 or appropriate forms for registration of securities, interest payments should be disclosed in a prospectus when paid to a bank which is represented on the board of directors of the issuer. These interest payments would include, but not be limited to, interest on commercial paper, conditional sales agreements, loan commitments and debentures held by a bank for investment as opposed to being held as nominee (Transcript p. 25).
2. A similar statement with respect to legal fees paid to a law firm represented on the board of directors of the issuer (Tr. p. 27).
3. A statement whether Penn Central's common stock was among the five most active on the New York Stock Exchange between March 30 and June 26, 1970, and, if so, on what dates (Tr. p. 63).
4. A statement whether the New York Stock Exchange notified your Commission of possible excessive trading activity in Penn Central's common stock between March 30 and June 26, 1970 (Tr. p. 68).

5. A statement whether the SEC is aware of the criteria used by the New York Stock Exchange in particular and by all exchanges in general in their stock watch procedures. This should include an indication of how often such criteria are reviewed by the SEC and whether, in the opinion of the Commission, such criteria are adequate. If the criteria with respect to Penn Central are considered adequate, an explanation of the reasons for no action being taken by the Exchange would be helpful to the Subcommittee. It is understood that the Subcommittee is not requesting disclosure of any specific criteria used by the exchanges or the Commission (Tr. pp. 74-75).
6. A report showing the names of the Commission personnel conducting the inquiry into Penn Central, the dates of their assignment to the inquiry, the amount of time expended on a daily basis by each individual and an indication whether additional personnel will be assigned. The earliest date should be indicated by which the Commission feels it will be in a position to report on the results of its inquiry (Tr. pp. 75-77).
7. A description of the mechanism presently existing by which the stock exchanges alert the SEC of any unusual increase in the volume of trading in a particular security (Tr. p. 85).
8. An outline of the procedure involved in the suspension of trading by the exchanges and the SEC and a statement of the reasons suspension was not invoked in the Penn Central matter (Tr. p. 85).

The Subcommittee also requested an analysis of the differences in accounting treatment by the ICC and the SEC with respect to the issuance and marketing of securities. We understand that this will require additional time to prepare, in view of the coordination necessary. Your report on this particular item can follow your responses to the other items requested.

Your continued cooperation with the Subcommittee will be appreciated.

Sincerely,

HARLEY O. STAGGERS
CHAIRMAN

MEMORANDUM OF THE SECURITIES AND EXCHANGE COMMISSION PREPARED IN RESPONSE TO THE REQUEST OF OCTOBER 1, 1970 FROM CHAIRMAN HARLEY O. STAGGERS OF THE SPECIAL SUBCOMMITTEE ON INVESTIGATIONS OF THE COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE OF THE HOUSE OF REPRESENTATIVES, FOR ADDITIONAL INFORMATION SUPPLEMENTING COMMISSIONER RICHARD B. SMITH'S TESTIMONY ON SEPTEMBER 24, 1970 DURING THE SUBCOMMITTEE'S HEARINGS ON PENN-CENTRAL.

The following replies are submitted in response to the letter dated October 1, 1970 from Chairman Harley O. Staggers of the Committee on Interstate and Foreign Commerce requesting certain additional information in connection with the testimony of Commissioner Smith during the Subcommittee hearings on Penn-Central. For convenience, the questions are repeated at the beginning of each of the responses.

Question No. 1 A statement whether, pursuant to Schedule A to the Securities Act of 1933 or appropriate forms for registration of securities, interest payments should be disclosed in a prospectus when paid to a bank which is represented on the board of directors of the issuer. These interest payments would include, but not be limited to, interest on commercial paper, conditional sales agreements, loan commitments and debentures held by a bank for investment as opposed to being held as nominee (Tr. p. 25).

This question relates to the disclosure which would have been required if the offering circular of the Pennsylvania Company, dated May 12, 1970, had been filed as part of a registration statement under the Securities Act of 1933. The offering circular related to a proposed offer of sinking fund debentures in the principal amount of \$100 million. The securities were not sold. The debentures in question were not registered under the Securities Act of 1933 because of reliance upon the exemption from the registration and prospectus requirements of the Act which is afforded under

Section 3(a)(6) of the Act to security offerings of common or contract carriers which are subject to Section 20(a) of the Interstate Commerce Act.

As explained in more detail below, in certain circumstances such interest payment disclosures would have been required, while in certain other circumstances they would not. The response to this question is accordingly given under alternative assumptions: (A) That the Pennsylvania Company is an investment company registered under the Investment Company Act of 1940, and (B) that it is not an investment company registered under the Investment Company Act of 1940 and that the securities which it offered were not exempt under Section 3(a)(6) of the Securities Act of 1933.

(A) If it is assumed that the Pennsylvania Company was an investment company registered under the Investment Company Act, it would have been required to file a registration statement for the offering of securities under the Securities Act of 1933 on Form S-4, the form prescribed for registered closed-end investment companies. For convenience, a copy of Form S-4 is attached together with a copy of Form N-8B-1, since portions of the latter are incorporated by reference in Form S-4. Form N-8B-1 is the appropriate form for registering a closed-end company under the Investment Company Act of 1940, as distinguished from registering its securities under the Securities Act of 1933.

Ordinarily disclosure would not be required in the prospectus of a registered investment company of interest payments made by registrant to a bank represented on its board of directors. Item 25 of Form N-8B-1 requires, insofar as may be pertinent here, disclosure of aggregate

remuneration in excess of \$30,000 paid by registrant during its last fiscal year to any director or to any affiliated person of any director for services in all capacities. Form S-4 also requires that such information be included in a registration statement filed under the Securities Act of 1933. Disclosure of interest payments to a bank by a registered closed-end company having a common director with the bank would not be required because, absent facts showing the contrary, they would not constitute remuneration for services paid to the director or to an affiliated person of a director. It should be noted that under the Investment Company Act, while a bank director is an affiliate of the bank, the bank is not an affiliate of the director unless some other specified relationship exists.

(B) If it is assumed that the Pennsylvania Company was not an investment company and that its offering of securities was not exempt under Section 3(a)(6) of the Securities Act of 1933, the company would have been required to file a registration statement on Form S-1, the general form for registration of securities under the Securities Act of 1933. For convenience, a copy of this form is attached. It will be noted that Item 20 of the form, entitled "Interest of Management and Others in Certain Transactions," requires disclosure of the interest of directors of the issuer in material transactions during the preceding three years, or in any proposed material transactions to which the registrant or any of its subsidiaries was or is about to be a party. Such material transactions might include the payment of interest to a bank or the payment of legal fees to a law firm unless permitted to be excluded by specific provisions of the instructions to Item 20. While we do not have sufficient information

to determine whether such exclusions would have been available to the Pennsylvania Company, it should be noted that disclosure would be required when a director is a partner in the law firm. In particular, Instruction 6 to Item 20 permits certain information to be excluded from the response thereto. Section (ii) of Instruction 6 provides an exclusion where the interest of the specified persons in the transactions is solely that of a director of another corporation which is a party to the transaction. Section (iv) of Instruction 6 provides an exclusion where the interest of the specified persons, as defined therein, does not exceed \$30,000. Instructions 3, 4 and 8 to Item 20 also provide for omissions of information but in areas which do not appear pertinent to Question 1.

Item 20 of Form S-1 also requires disclosure of the interest of any associate of specified persons in transactions specified in the item. The term "associate" is defined in Rule 405 of the Commission's General Rules and Regulations under the Securities Act of 1933 (17 CFR 230.405(b-1)) as follows:

The term "associate" used to indicate a relationship with any person means (1) any corporation or organization (other than the registrant or a majority-owned subsidiary of the registrant) of which such person is an officer or partner or is, directly or indirectly, the beneficial owner of 10 percent or more of any class of equity securities, (2) any trust or other estate in which such person has a substantial beneficial interest or as to which such person serves as trustee or in a similar capacity, and (3) any relative or spouse of such person, or any relative of such spouse, who has the same home as such person or who is a director or officer of the registrant or any of its parents or subsidiaries.

Question No. 2 A similar statement with respect to legal fees paid to a law firm represented on the board of directors of the issuer (Tr. p. 27).

The responses to this question will be made under assumptions similar to those in the response to Question No. 1, and will refer to such responses to Question No. 1 where pertinent to avoid unnecessary duplication.

(A) If it is assumed that the Pennsylvania Company was an investment company registered under the Investment Company Act of 1940, disclosure would be required in the prospectus included in the Registration Statement on Form S-4 of legal fees exceeding \$30,000 and paid by the registrant during its preceding fiscal year to a law firm having as a partner a person who is a director of the registrant. As noted in the response to the previous question, Item 25 of Form N-8B-1 requires disclosure of remuneration for services paid by registrant to an affiliated person of a director. Copartners are defined as affiliates of each other.

(B) If it is assumed that the Pennsylvania Company was not an investment company registered under the Investment Company Act of 1940 and if it is assumed further that the securities which it offered were not exempt under Section 3(a)(6) of the Securities Act of 1933, disclosure of legal fees would be required in response to Item 20 of Form S-1 whenever the director is a partner of the law firm, as discussed in Part (B) of the response to Question No. 1 above.

Question No. 3 A statement whether Penn Central's common stock was among the five most active on the New York Stock Exchange between March 30 and June 26, 1970, and, if so, on what dates (Tr. p. 63).

The common stock of Penn Central Company was among the five most actively traded securities on the New York Stock Exchange on the following

days during the period from March 30, 1970 to June 26, 1970: May 12, 19, 22, 25, 27 through 29, June 9 through 12, 15, 17 and 22 through 26.

Question No. 4 A statement whether the New York Stock Exchange notified your Commission of possible excessive trading in Penn Central's common stock between March 30 and June 26, 1970 (Tr. p. 68).

The Commission did not receive notification from the New York Stock Exchange of possible excessive trading in Penn Central's common stock during the period in question. As more fully set forth in the response to Question No. 5, the Exchange was satisfied that the trading activity and price movements of this stock were explained adequately by general business news, market conditions, and specific news items appearing in the financial press regarding Penn Central.

Question No. 5 A statement whether the SEC is aware of the criteria used by the New York Stock Exchange in particular and by all exchanges in general in their stock watch procedures. This should include an indication of how often such criteria are reviewed by the SEC and whether, in the opinion of the Commission, such criteria are adequate. If the criteria with respect to Penn Central are considered adequate, an explanation of the reasons for no action being taken by the Exchange would be helpful to the Subcommittee. It is understood that the Subcommittee is not requesting disclosure of any specific criteria used by the exchanges or the Commission (Tr. pp. 74-75).

As stated in testimony before the Subcommittee, the New York Stock Exchange and all exchanges have the primary responsibility, subject to Commission oversight, for surveillance over trading on the exchanges in their listed securities. Pursuant to this responsibility the exchanges have instituted a number of programs to detect questionable trading activity and possible violations of exchange rules. One program employed by the

New York Stock Exchange involves a daily computer print-out of those securities in which trading has exceeded pre-established parameters which have been programmed into the computer. The computer evaluates certain data, such as the high-low range of prices during the trading day, the change in closing prices compared with the closing prices of the preceding day, and the movement in a leading market index, and identifies a large number of issues for possible review each day.^{1/} A determination is then made by the Exchange as to what further inquiry will be made with respect to those securities listed on the print-out. In making this determination, consideration is given to such factors as published news concerning the issuer, brokerage firm recommendations, general market trends, trading activity in securities of other issues within the same industry and the number and type of holders of the securities.

The Commission is fully aware of the specific criteria used by the exchanges, and the New York Stock Exchange in particular, in their stock watch procedures since the Commission's staff is advised by all exchanges of changes in procedures employed by their market surveillance units. In addition, the Commission, as part of its oversight responsibility over exchange functions, conducts a program of inspections and engages in frequent meetings and communications with exchange staff on a continuing basis. Commission

^{1/} As more fully described below, the common stock of Penn-Central Company was listed on a daily computer print-out on six separate days during the period from March 30 to June 19, 1970.

inspections, although performed periodically, are not regularly scheduled, but are conducted when the Commission deems them necessary. ^{2/} When an inspection indicates deficiencies in any area, these deficiencies are brought immediately to the attention of the appropriate officials of the organization involved. These Commission oversight activities insure that the Commission is kept fully advised of the market surveillance functions of the exchanges and subject these functions to continuous review by the Commission. Based upon information provided by the exchanges, and review of market surveillance procedures, the Commission believes that the criteria used are sufficiently stringent to identify securities in which there have been inordinate price movements and that the parameters employed are adequate.

As previously stated, the Penn Central Company was listed on the computer print-out of the New York Stock Exchange on six days during the period from March 30 to June 19, 1970 (May 12, 19, 22, June 9, 10 and 12). The Exchange, however, did not conduct any inquiry into the trading with respect to any of these particular days because it was satisfied that the price movements in Penn Central's common stock were explained adequately by general news, market conditions and specific news appearing in the financial press regarding Penn Central. Since no inquiry by the Exchange was conducted during the period in question, no information was available

^{2/} The most recent Commission inspections of the New York Stock Exchange and the Midwest Stock Exchange were conducted in October 1969 and March 1970 respectively.

to forward to the Commission. The Exchange has, however, reported to the Commission that, some time in June, 1970, it had made a decision, because of the frequency of Penn Central's appearance on the computer list and the volume of trading in its securities, to initiate an inquiry into the trading activity in Penn Central stock, and requested the clearing sheets in Penn Central for the purpose of ascertaining the names of Exchange clearing members buying or selling during the period. According to the Exchange, this inquiry was discontinued shortly after it was instituted when it was informed that the Commission had undertaken its own inquiry into trading in Penn Central. Under these circumstances, the Exchange forwarded to the Commission's staff the copies of the clearing sheets which it had requested and obtained.

Question No. 6 A report showing the names of the Commission personnel conducting the inquiry into Penn Central, the dates of their assignment to the inquiry, the amount of time expended on a daily basis by each individual and an indication whether additional personnel will be assigned. The earliest date should be indicated by which the Commission feels it will be in a position to report on the results of its inquiry (Tr. pp. 75-77).

Immediately after the filing by Penn Central Transportation Company, on June 21, 1970, under the railroad reorganization provisions of the Bankruptcy Act, Stanley Sporkin, Associate Director of the Commission's Division of Trading and Markets, directed the staff of the Office of Enforcement to begin an inquiry into the Penn Central matter. The Market Surveillance Branch, under the supervision of Robert Bretz, was assigned to conduct a study of the trading in Penn Central's securities during the

period preceding the company's filing under the Bankruptcy Act. In addition, the Branch of Enforcement, under Branch Chief Irwin M. Borowski, was assigned to perform the overall inquiry in coordination with the regional offices of the Commission.

The trading study is the initial step in an inquiry of this type since it is only through such a study that the Commission can determine whether and to what extent there has been trading activity which might indicate an abuse of information concerning the company. The trading survey being conducted is one of the most extensive performed by the staff of the Division of Trading and Markets in an individual case.^{3/}

A trading study is a time-consuming task, which initially requires, among other things, obtaining the clearing sheets from each of the stock exchanges, reviewing the "pink sheets" and collecting information from put and call brokers. Thereafter, a selection is made of those brokers to whom questionnaires were mailed who show significant activity. This involves numerous hours of clerical work. It is then necessary to follow up and

^{3/} The trading study, which surveys the three-month period immediately preceding the filing in reorganization, covers trading in the common stock and a collateral trust bond of the Penn Central Company and the preferred stock of Penn Central Transportation Company, and encompasses trading not only on the New York Stock Exchange and most of the regional exchanges, but also trading in the third market and the option market. Because of the number of securities involved and the trading volume (over 7 million shares of Penn Central common on the New York Stock Exchange alone) it was necessary to circularize more than 250 broker-dealers with questionnaires. At this time, approximately four-fifths of the questionnaires have been returned and the Commission is continuing to receive questionnaires from the remaining firms.

contact brokers personally in order to expedite compliance with the request. The returned questionnaires reflect thousands of trades. Each of these is being analyzed in terms of size, whether the persons or entity involved had any relationship to Penn Central, the nature of the transaction (i.e., was it a long or short sale) and the timing of the activity with respect to specific corporate events. This analysis is still continuing as the questionnaires are being received.

The table below, sets forth the names of the staff members in the Market Surveillance Branch who have been assigned to conduct the trading study (excluding clerical personnel), and the percentage of time devoted by each to this matter.

<u>Staff</u>	<u>Position</u>	<u>Period of Time</u>	<u>Percentage</u>
Robert Bretz	Supervisor	6/22/70-9/24/70 9/25/70-11/12/70	10% 15%
James Mann	Financial Analyst	6/22/70-9/24/70 9/25/70-11/12/70	75% 50%
Herbert Mayer	Financial Analyst	6/22/70-8/14/70 8/15/70-11/12/70	40% 25%

These individuals have been assisted, as necessary, by staff members in the Branch of Enforcement in the review and analysis of trading information received.^{4/}

Because of the unusual significance of the Penn Central situation, four members of the eight-man staff of the Branch of Enforcement were

^{4/} Because of the nature of a study of this type and the unavoidable time lag in receiving responses to the questionnaires, a commitment of more personnel than those who were assigned to the task would not appreciably expedite completion of the trading study.

assigned at the inception of the inquiry.^{5/} The table below indicates the members of the staff of the Branch of Enforcement assigned to the inquiry and the percentage of time devoted by each to this matter.^{6/}

<u>Staff</u>	<u>Position</u>	<u>Period of Time</u>	<u>Percentage</u>
Irwin Borowski	Branch Chief	Approx. beginning of July 1970 to Sept. 24, 1970 9/25/70 to 11/12/70	10% 25%
William Kuehnle	Staff Attorney	Approx. beginning of July 1970 to Aug. 18, 1970 8/19/70 to 9/24/70 9/25/70 to 11/12/70	25% 80% 90%
James Birchby	Staff Attorney	7/8/70 to 8/18/70 8/19/70 to 11/12/70	70% 90%
John Murray	Summer Law Clerk	7/8/70 to 8/14/70	80%

These individuals, in addition to assisting the Market Surveillance Branch, have commenced a broad review and analysis of the news items and magazine articles about the company going back to the time of the merger, the company's public releases, the filings of the company with the Commission and other regulatory agencies and the gathering and review of investment advisory and brokerage recommendations regarding the company.

Moreover, as a result of coordination at any early stage in the inquiry, the Washington and New York regional offices of the Commission,

^{5/} In most cases involving issues similar to the Penn Central matter, only one attorney in the Branch of Enforcement usually is assigned to the case at its inception and it will be only one of a number of cases on which he is working. The commitment of more staff personnel and time to a case will usually occur after the trading survey has been substantially completed and the field inquiry commences.

^{6/} A fifth member of the staff, Daniel Glickman, was originally assigned to the case, but left the Commission's employ without having become significantly involved.

the offices thought to be directly concerned with the inquiry, are prepared to provide staff personnel for and to participate in the inquiry as it involves their regions at the appropriate time. In fact, the Washington Regional Office has been participating in a part of the inquiry since early in July. The table below sets forth the staff members of the Washington Regional Office assigned to this matter and the time devoted by each.

<u>Staff</u>	<u>Position</u>	<u>Period of Time</u>	<u>Percentage</u>
William Schief	Associate Regional Administrator	Approx. beginning of July 1970 to Sept. 15, 1970 9/16/70 to 11/12/70	5% 15%
Lionel Pashkoff	Staff Attorney	Approx. beginning of July 1970 to Sept. 15, 1970 9/15/70 to 11/1/70 11/1/70 to 11/12/70	15% 50% 75%
Jay Franz	Staff Attorney	10/15/70 to 11/12/70	60%
Edward Griffin	Staff Attorney <i>Investigator</i>	10/15/70 to 11/12/70	50%

Murray Garson, an accountant in the Division of Trading and Markets, was also assigned to the inquiry in the first week of October 1970 and has from that date devoted approximately 70% of his time to the matter.

As described above, the application of manpower to an inquiry such as this varies upon the stage of the inquiry. Assignment of additional personnel will be made by the Commission as necessary while the staff presently assigned to the inquiry will continue to draw upon the expertise of various members of the Commission's staff as circumstances require.

Although it is difficult to state at this time when a report on this inquiry can be submitted, it is anticipated that the staff may be able to

provide a progress report in early 1971. The timing of such a report, however, is contingent upon the extent to which the inquiry uncovers areas which necessitate further in-depth treatment. The Commission considers this inquiry a matter of the highest priority, and it is being conducted accordingly.

Question No. 7 A description of the mechanism presently existing by which the stock exchanges alert the SEC of any unusual increase in the volume of trading in a particular security (Tr. p. 85).

There are a number of mechanisms utilized by the exchanges to alert the Commission to any unusual increase in the volume of trading in a particular security. In keeping with the concept that a continuous flow of information between the exchanges and the Commission is desirable, reliance is placed upon informal as well as formal mechanisms of communication. Thus, the Commission may be alerted to matters involving trading volume in a security through telephone conversations with exchange staff, case referrals and periodic reports of exchange activity. In addition, the Commission's staff coordinates its own market surveillance activities with those of the New York Stock Exchange and American Stock Exchange through receipt from these exchanges of daily and weekly stock watch reports. These reports contain information relating to inquiries made by the exchange staff into trading in particular securities.

Question No. 8 An outline of the procedure involved in the suspension of trading by the exchanges and the SEC and a statement of the reasons suspension was not invoked in the Penn Central matter (Tr. p. 85).

The Commission is authorized under Sections 15(c)5 and 19(a)(4) of the Securities Exchange Act to suspend summarily trading in securities in

exchange and over-the-counter markets for ten-day periods. In determining whether a suspension of trading is appropriate, the Commission has been guided by the express Congressional intent in granting this power. In this regard, the Report of the Senate Banking and Currency Committee, in reporting out S. 1642, which was ultimately enacted in 1964 and which authorized the Commission to suspend trading in the over-the-counter market, stated:

New paragraph (5) of Section 15(c) would permit the Commission temporarily to suspend trading when fraudulent or manipulative practices of the issuer or other persons have deprived an over-the-counter security of a fair and orderly market, or when some corporate event has made informed trading impossible and has created conditions in which investors are likely to be deceived. Trading would be allowed to resume as soon as there has been adequate disclosure and dissemination of the facts material to investment decisions . . . S. Rep. No. 379, p. 26, 88th Cong., 1st Sess. (1963).

Although the suspension power can be exercised summarily and rapidly by the Commission, we recognize that a trading suspension can work a serious hardship and, therefore, we attempt to exercise this power with careful consideration for the rights of all interested parties, including existing and prospective security holders and the issuer itself. The procedure for instituting a trading suspension is a relatively simple one. When the staff of the Commission becomes aware of information which indicates that a suspension might be appropriate, it transmits this information to the Commission for its consideration and determination. The information upon which the staff's recommendation is based may originate from our market surveillance program, a staff investigation or information furnished by another government agency or self-regulatory body or from a public complaint.

The Commission has exercised its suspension powers primarily in the over-the-counter market and has relied in the first instance on the securities exchanges to halt and suspend trading in exchange listed securities where the circumstances warrant. The Commission's initial reliance upon the exchanges to suspend or halt trading is not only in accord with the self regulatory scheme for the exchanges embodied in the Securities Exchange Act, but is desirable as a practical matter, since the exchanges become immediately aware, through their continuous surveillance of trading, of unusual activity in a listed security and have the ability to act instantaneously to suspend trading. The New York Stock Exchange has established procedures for halting trading promptly in instances where significant corporate developments or imbalances in security orders disrupt the making of an orderly market. Similar procedures are employed by the American Stock Exchange and the regional securities exchanges.

The Exchange did not suspend or halt trading in Penn Central common stock either prior or subsequent to the filing in bankruptcy on June 21, 1970. According to the Exchange, it did not suspend trading prior to June 21, 1970 because it believed that the increased market activity in Penn Central was adequately explained by specific news events. Similarly, the Commission did not suspend trading since no factors indicated that a suspension would be appropriate. Neither the Commission nor the Exchange deemed it necessary to suspend or halt trading in Penn Central common stock subsequent to the filing in bankruptcy since the bankruptcy petition and the publicity it received in the financial press disclosed the financial condition of the company to the investing public.

Although trading in Penn-Central stock was not suspended, we note that on June 22, 23 and 24, the opening of trading in that stock was significantly delayed due to the heavy imbalance of orders. In addition, on June 24, 1970, the Exchange did suspend trading in 21 debt obligations of rail lines leased by the Penn Central Transportation Company and trading in these obligations is still suspended.

SUPPLEMENTARY INFORMATION:

In addition to the foregoing responses to the questions presented, we would like to take this opportunity to supplement and clarify several of the replies which were given at the hearing before the Subcommittee on September 24, 1970 in the following manner: (References are to the transcript.)

Page 24, line 8:

In the case of a registered investment company, stock options are prohibited by the Investment Company Act of 1940. (See Sections 18(d) and 23(a) of that Act.)

Page 24, line 14, and page 28, line 5:

These responses were also given under the assumption that we were talking about a company not registered and not required to register under the Investment Company Act of 1940. If the company were required to so register, and if it were a closed-end investment company, it would be required to file a registration statement on Form S-4 as described in the response to Question No. 1 above.

Sections 7 and 10 of the Securities Act of 1933 grant to the Commission authority to require certain specified information in registration statements

and prospectuses. Those sections also authorize the Commission to provide for the omission, by rules and regulations, of any information otherwise required which the Commission designates as not necessary or appropriate in the public interest or for the protection of investors. The term "rules and regulations" includes the forms for registration of securities under the Securities Act of 1933 and the related instructions thereto.

It is under this authority, as well as that contained in Section 24(a) of the Investment Company Act of 1940, that the Commission has not required in a registration statement filed on Form S-4 certain disclosures ordinarily required by Form S-1. Exercising this discretion, the Commission has not required disclosure of interest payments to banks represented on the board of a registered investment company to be included in the prospectus.

Such disclosure has not been considered necessary in the past because of the protections afforded by a combination of other regulatory provisions of the Investment Company Act which require that the investment company receive at least net asset value for its common stock, which limit the amount of its indebtedness in relation to its asset size, and which limit the number of the company's directors who may be officers or directors of any one bank.

In any event, the Commission is now considering whether to amend Form S-4 to require such disclosure in the future.

As in effect
4/15/59

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM S-4

REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

(Exact name of registrant as specified in charter)

(Address of principal executive offices)

(Name and address of agent for service)

Approximate date of commencement of
proposed sale to the public _____

CALCULATION OF REGISTRATION FEE

<u>Title of securities being registered</u>	<u>Amount being registered</u>	<u>Proposed maximum offering price per unit</u>	<u>Proposed maximum aggregate offering price</u>	<u>Amount of registration fee</u>
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GENERAL INSTRUCTIONSA. Rule as to Use of Form S-4.

Form S-4 shall be used for registration under the Securities Act of 1933 of securities of all closed-end management investment companies registered under the Investment Company Act of 1940 on Form N-8B-1.

B. Application of General Rules and Regulations.

Attention is directed to the General Rules and Regulations under the Act, particularly those comprising Regulation C. That regulation contains general requirements regarding the preparation and filing of the registration statement.

C. Documents Comprising Registration Statement.

The registration statement shall consist of the facing sheet of the form, the prospectus containing the information specified in Part I, the information called for by Part II, the undertaking to file reports, the required signatures, consents of experts, financial statements and exhibits and any other prospectus, information, undertaking or documents which are required or which the registrant may file as a part of the registration statement.

D. Form and Content of Prospectus.

(a) The purpose of the prospectus is to inform investors. Hence, the information set forth in the prospectus should be presented in clear, concise, understandable fashion. Avoid unnecessary and irrelevant details, repetition or the use of unnecessary technical language. The prospectus shall contain the information called for by all of the items of Part I of the form, except that no reference need be made to inapplicable items, and negative answers to any item may be omitted.

(b) Unless clearly indicated otherwise, information set forth in any part of the prospectus need not be duplicated elsewhere in the prospectus. Where it is deemed necessary or desirable to call attention to such information in more than one part of the prospectus, this may be accomplished by appropriate cross reference. In lieu of restating information in the form of notes to the financial statements, references should be made to other parts of the prospectus where such information is set forth.

E. Cross Reference Sheet.

The cross reference sheet required by Rule 404(c) shall show the location in the prospectus of the information called for by the items of Part I of this form and by the items of Form N-8B-1 enumerated in Item 5 of this form.

F. Preparation of Part II.

Part II of the registration statement shall contain the numbers and captions of the items in Part II of the form, but the text of the items may be omitted provided the answers are so prepared as to indicate to the reader the coverage of the items without the necessity of referring to the text of the items or the instructions thereto. If the information required by any item of Part II is completely disclosed in the prospectus, reference may be made to the specific page or caption of the prospectus which contains such information.

PART I. INFORMATION REQUIRED IN PROSPECTUSItem 1. Distribution Spread.

The information called for by the following table shall be given, in substantially the tabular form indicated, on the outside front cover page of the prospectus as to all securities being registered which are to be offered for cash (estimate, if necessary).

	<u>Price to public</u>	<u>Underwriting discounts and commissions</u>	<u>Proceeds to registrant or other persons</u>
Per Unit _____	_____	_____	_____
Total _____	_____	_____	_____

Instructions. 1. The term "commissions" has the meaning given in paragraph (17) of Schedule A of the Act. Only commissions paid by the registrant or selling security holders in cash are to be included in the table. Commissions paid by other persons, and other considerations to the underwriters, shall be set forth following the table with a reference thereto in the second column of the table. Any finder's fees or similar payments shall be appropriately disclosed.

2. If it is impracticable to state the price to the public, the method by which it is to be determined shall be explained. In addition, if the securities are to be offered at the market, or if the offering price is to be determined by a formula related to market prices, indicate the market involved and the market price as of the latest practicable date.

3. If any of the securities being registered are to be offered for the account of security holders, the name of each holder, the amount held by him and the amount offered for his account should be stated either on the first page of the prospectus or elsewhere in the prospectus with an appropriate cross-reference on the first page.

Item 2. Plan of Distribution.

(a) If the securities being registered are to be offered through underwriters, give the names of the principal underwriters, and state the respective amounts underwritten. Identify each such underwriter having a material relationship to the registrant and state the nature of the relationship. State briefly the nature of the underwriters' obligation to take the securities.

Instruction. All that is required as to the nature of the underwriters' obligation is whether the underwriters are or will be committed to take and to pay for all of the securities if any are taken, or whether it is merely an agency or "best efforts" arrangement under which the underwriters are required to take and pay for only such securities as they may sell to the public. Conditions precedent to the underwriters' taking the securities, including "market outs", need not be described except in the case of an agency or "best efforts" arrangements.

(b) State briefly the discounts and commissions to be allowed or paid to dealers, including all cash, securities, contracts or other consideration to be received by any dealer in connection with the sale of the securities.

Instruction. If any dealers are to act in the capacity of sub-underwriters and are to be allowed or paid any additional discounts or commissions for acting in such capacity, a general statement to that effect will suffice without giving the additional amounts to be so paid.

(c) Outline briefly the plan of distribution of any securities being registered which are to be offered otherwise than through underwriters.

Item 3. Use of Proceeds to Registrant.

State the principal purposes for which the net proceeds to the registrant from the securities to be offered are intended to be used, and the approximate amount intended to be used for each such purpose.

Instructions. 1. Details of proposed expenditures are not to be given. If any substantial portion of the proceeds has not been allocated for particular purposes, a statement to that effect shall be made together with a statement of the amount of proceeds not so allocated.

2. If any material part of the proceeds is to be used to discharge a loan, the item is to be answered as to the use of the proceeds of the loan if the loan was made within one year; otherwise, it will suffice to state that the proceeds are to be used to discharge the indebtedness created by the loan.

3. If any material amount of the proceeds is to be used to acquire assets, otherwise than in the ordinary course of business, briefly describe the assets and give the names of the persons from whom they are to be acquired. State the cost of the assets to the registrant and the principle followed in determining such cost.

Item 4. Sales Otherwise than for Cash.

If any of the securities being registered are to be offered otherwise than for cash, state briefly the general purposes of the distribution, the basis upon which the securities are to be offered, the amount of compensation and other expenses of distribution, and by whom they are to be borne.

Instruction. If the distribution is to be made pursuant to a plan of acquisition, reorganization, readjustment or succession, describe briefly the general effect of the plan and state when it became or is to become operative. As to any material amount of assets to be acquired under the plan, furnish information corresponding to that required by Instruction 3 to Item 3.

Item 5. Information Required by Items of Form N-8B-1.

The prospectus shall contain the information which would be required by the following items of Form N-8B-1 if a registration statement on that form were currently being filed:

Items 1, 2, 3, 4, 5, 8 and 9;

Item 10, as of a date within 90 days;

Items 11 and 12;

Item 13 as to persons controlling the registrant;

Items 14, 16, 17, 18, 21(a), 22 and 25;

Items 26, 27 or 28 as to securities being registered.

Instructions. 1. Subject to Rule 407, the information called for by the foregoing items of Form N-8B-1 shall be given as of the effective date of the registration statement on this form.

2. The information called for by Item 12 of Form N-8B-1 shall be set forth not further back in the prospectus than the fifth page thereof and shall not be preceded by any chart or table other than the table required by Item 1 of this form.

Item 6. Financial Statements.

The prospectus shall contain the following financial statements:

(a) The statements which would be required by Form N-8B-1 if a registration statement on that form were currently being filed.

(b) If any balance sheet or statement of assets and liabilities filed pursuant to (a) is not as of a date within 90 days prior to the date of filing the registration statement on this form, there shall also be included in the prospectus a corresponding balance sheet or statement of assets and liabilities as of a date within 90 days prior to the date of filing and the related statements prescribed by Article 6 of Regulation S-X from the close of the latest fiscal year for which such statements are included pursuant to (a) up to the date of the balance sheet or statement of assets and liabilities required by this paragraph. The statements required by this paragraph need not be certified, but if they are certified, the balance sheet or statement of assets and liabilities as of the end of the last fiscal year, may be omitted.

(c) Notwithstanding paragraphs (a) and (b) above, the following may be omitted from the prospectus:

(1) The statements of any subsidiary which is not a majority-owned subsidiary;

(2) All schedules in support of the most recent balance sheet or statement of assets and liabilities filed except the following: Schedule I; columns A, E, F and G of Schedule II; and columns A, B, C and D of Schedule III, omitting the information called for by paragraph (b) of footnote 1 to Column A;

(3) The historical financial information called for by Part E of the Instructions as to Financial Statements in Form N-8B-1.

(d) If the registrant has only one class of outstanding capital securities, then it may, at its option, furnish all financial statements specified in (a) and (b) above in Part II of the registrant statement and include only the following statements in the prospectus:

(1) A statement of Assets and Liabilities in which the details of Schedules I, II, and III prescribed by (b) and (c) above may be substituted for the summaries of these items as prescribed by Rule 6-03 of Regulation S-X. If this option is elected, the statement required by Rule 6-09 may be omitted from the prospectus.

(2) An Income Statement for the latest fiscal year in the form specified in Rule 6-04 of Regulation S-X, including, on the same page, (i) the items specified in caption 5 of Rule 6-05 and caption 2 of Rule 6-06, and (ii) the ratio of total operating and management ex-

penses to total investment income. "Total operating and management expenses" means the aggregate of the expenses described in captions 2 and 3 of Rule 6-04 of Regulation S-X. "Total investment income" does not include equalization adjustments.

(3) Statement of Changes in Net Assets for the three full fiscal years prior to the date of filing (or for the life of the registrant, if less) as prescribed by Rule 6-08.

Except that the statement prescribed by (2) above is required for only one fiscal year and an interim period, if any, to within 90 days of filing, the instructions as to dates and certification prescribed in (a) and (b) above shall be applicable to the optional statements permitted by this paragraph (d)

PART II. INFORMATION NOT REQUIRED IN PROSPECTUS

Item 7. Marketing Arrangements.

Briefly describe any arrangement known to the registrant or to any person named in answer to Item 2, or to any person specified in Item 14(a) or (b) of Form N-8B-1, made for any of the following purposes:

- (a) To limit or restrict the sale of other securities of the same class as those to be offered for the period of distribution.
- (b) To stabilize the market for any of the securities to be offered.
- (c) For withholding commissions, or otherwise to hold each underwriter or dealer responsible for the distribution of his participation.

Instruction. If the answer to this item is contained in an exhibit, the item may be answered by cross-reference to the relevant paragraphs of the exhibit.

Item 8. Other Expenses of Issuance and Distribution.

Furnish a reasonably itemized statement of all expenses in connection with the issuance and distribution of the securities being registered, other than underwriting discounts and commissions. If any of the securities being registered are to be offered for the account of security holders, indicate the portion of such expenses to be borne by such security holders.

Instruction. Insofar as practicable, registration fees, Federal taxes, States taxes and fees, trustees' and transfer agents' fees, cost of printing and engraving, and legal, ac-

counting and engineering fees shall be separately itemized. The information may be given as subject to future contingencies. If the amounts of any items are not known, estimates designated as such shall be given.

Item 9. Indemnification of Directors and Officers.

State the general effect of any charter provision, by law, contract, arrangement or statute under which any director or officer of the registrant is insured or indemnified in any manner against any liability which he may incur in his capacity as such.

Item 10. Financial Statements and Exhibits.

List all financial statements and exhibits filed as a part of the registration statement:

- (a) Financial statements, indicating those included in the prospectus.
- (b) Exhibits.

UNDERTAKINGS

A. The following undertaking shall be included in every registration statement:

"Subject to the terms and conditions of Section 15(d) of the Securities Exchange Act of 1934, the undersigned registrant hereby undertakes to file with the Securities and Exchange Commission such supplementary and periodic information, documents and reports as may be prescribed by any rule or regulation of the Commission heretofore or hereafter duly adopted pursuant to authority conferred in that section."

B. The following undertaking, with appropriate modifications to suit the particular case, shall be included in the registration statement if the securities being registered are to be offered to existing security holders pursuant to warrants or rights and any securities not taken by security holders are to be reoffered to the public:

"The undersigned registrant hereby undertakes to supplement the prospectus, after the expiration of the subscription period, to set forth the results of the subscription offer, the transactions by the underwriters during the subscription period, the amount of unsubscribed securities to be purchased by the underwriters and the terms of any subsequent reoffering thereof. If any public offering by the underwriters is to be made on terms differing from those set forth on the cover page of the prospectus, a post-effective amendment will be filed to set forth the terms of such offering."

SIGNATURES

Pursuant to the requirements of the Securities Act of 1933, the registrant has duly caused this registration statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of _____, and State of _____, on the _____ day of _____, 19__.

(Registrant)

By _____
(Signature and Title)

Pursuant to the requirements of the Securities Act of 1933, this registration statement has been signed below by the following persons in the capacities and on the dates indicated.

(Signature)

(Title)

(Date)

Instructions. 1. The registration statement shall be signed by the registrant, its principal executive officer or officers, its principal financial officer, its controller or principal accounting officer and by at least the majority of the board of directors or persons performing similar functions. If the registrant is a foreign person, the registration statement shall also be signed by its authorized representative in the United States.

2. The name of each person who signs the registration statement shall be typed or printed beneath his signature. Any person who occupies more than one of the specified positions shall indicate each capacity in which he signs the registration statement.

INSTRUCTIONS AS TO EXHIBITS

Subject to the rules regarding incorporation by reference, the following exhibits shall be filed as a part of the registration statement. Exhibits shall be appropriately lettered or numbered for convenient reference. Exhibits incorporated by reference may bear the designation given the previous filing. Where exhibits are incorporated by reference, the reference shall be made in the list of exhibits called for by Item 10(b).

1. Copies of all exhibits which would be required by Form N-8B-1 if a registration statement on that form were currently being filed.
2. A specimen or copy of each security being registered.
3. A copy of each underwriting contract with a principal underwriter, each syndicate agreement and each purchase, sub-underwriting or selling group agreement or letter pursuant to which the securities being registered are to be distributed or, if the terms of such documents are not determined, the proposed forms thereof.
4. An opinion of counsel as to the legality of the securities being registered, indicating whether they will when sold be legally issued, fully paid and non-assessable.
5. All financial statements omitted from the prospectus pursuant to Item 6(c) or (d).

As in effect 5/1/65

SECURITIES AND EXCHANGE COMMISSION
Washington, D. C.

FORM N-8B-1

REGISTRATION STATEMENT OF MANAGEMENT INVESTMENT COMPANY

Pursant to Section 8 of

THE INVESTMENT COMPANY ACT OF 1940

(Name of registrant)

(Address of principal executive office)

GENERAL INSTRUCTIONSA. Rule as to Use of Form N-8B-1.

This form shall be used for registration statements filed pursuant to Section 8(b) of the Investment Company Act of 1940 by all management investment companies except those which issue periodic payment plan certificates.

B. Application of General Rules and Regulations.

(a) The General Rules and Regulations under the Act contain certain general requirements which are applicable to registration on any form. These general requirements should be carefully read and observed in the preparation and filing of registration statements on this form.

(b) Particular attention is directed to Regulation 8B which contains general requirements regarding matters such as the kind and size of paper to be used, the legibility of the registration statement, the information to be given whenever the title of securities is required to be stated, and the filing of the registration statement. The definitions contained in Rule 8b-2 should be especially noted.

C. Preparation of Registration Statement.

(a) This form is not to be used as a blank form to be filled in, but only as a guide in the preparation of the registration statement on paper meeting the requirements of Rule 8b-12. The registration statement shall contain the item numbers and captions, but the text of the items may be omitted provided the answers thereto are prepared in the manner specified in Rule 8b-13.

(b) Unless otherwise stated, the information required shall be given as of the date of filing the registration statement.

Item 1. General Information.

Give the date and form of organization of the registrant and the name of the state or other sovereign power under the laws of which it was organized.

Instruction. As to the form of organization, only a statement such as the following is required: "a corporation," "an unincorporated association," "a common law trust," or other appropriate statement.

Item 2. Development of Business.

(a) If the registrant has engaged in any business other than that of an investment company during the past five years, state the nature of such other business and give the approximate date on which the registrant originally commenced business as an investment company. If the registrant's name was changed during the period, state its former name and the approximate date on which it was changed. Indicate briefly the nature and results of any bankruptcy, receivership or similar proceedings or any other materially important reorganization, readjustment or succession during the period.

(b) If during the past three years any affiliated person of the registrant had any material interest, direct or indirect, in any transaction involving the purchase of any substantial amount of assets presently held by the registrant or any of its subsidiaries, otherwise than in the ordinary course of business, describe the interest of the affiliated person in such transaction and state the cost of such assets to the purchaser and to the seller.

Instruction. No information need be given under paragraph (b) as to the interest of any affiliated person in any transaction exempted from section 17 of the Act.

Item 3. Subclassification of Registrant.

(a) State whether registrant is a closed-end or open-end investment company.

(b) State whether registrant proposes to operate as a diversified or non-diversified investment company.

Instruction. Registrant may reserve freedom of action to change from a non-diversified to a diversified investment company.

Item 4. Fundamental Policies of the Registrant.

Describe the policy or proposed policy of the registrant with respect to each of the following types of activities, and outline the extent, if any, to which the registrant has engaged in such activities during its

last three fiscal years.

(a) The issuance of senior securities (if registrant is a closed-end company.)

(b) The borrowing of money.

(c) The underwriting of securities of other issuers.

(d) The concentration of investments in particular industries.

(e) The purchase and sale of real estate.

(f) The purchase and sale of commodities or commodity contracts.

(g) The making of loans to other persons.

(h) Any other policy which the registrant deems a matter of fundamental policy and elects to treat as such pursuant to Sections 8(b)(2) and 13(a)(3) of the Act.

Instruction. 1. The registrant may reserve freedom of action with respect to any of the foregoing activities, but in such cases shall express definitively, in terms of a reasonable percentage of assets to be devoted to the particular activity, or otherwise, the maximum extent to which the registrant intends to engage therein. See Release No. 167 under the Act.

2. For the purposes of (g) the purchase of a portion of an issue of publicly distributed bonds, debentures or other securities, whether or not the purchase was made upon the original issuance of the securities, is not to be considered the making of a loan by the registrant.

Item 5. Policies with Respect to Security Investments.

Describe the investment policy of the registrant with respect to each of the following matters which is not described as a fundamental policy of the registrant under Item 4, indicating which of such investment policies may not be changed without stockholder action:

(a) The type of securities (for example, bonds, preferred stocks, common stocks) in which it may invest, indicating the proportion of the assets which may be invested in each such type of security.

(b) The percentage of assets which it may invest in the securities of any one issuer.

(c) The percentage of voting securities of any one issuer which it may acquire.

(d) Investment in companies for the purpose of exercising control or management.

(e) Investment in securities of other investment companies.

(f) The policy with respect to portfolio turnover.

(g) Any other investment policy not specified above or in Item 4, which is set forth in the registrant's charter, by-laws or prospectus.

Item 6. Diversification of Assets.

Furnish the following information as of the date of registration pursuant to Section 8(a) of the Act and also as of the end of the latest fiscal year of the registrant covered by the financial statements filed herewith:

(a) With respect to the following classes of assets of the registrant--

<u>Class of Assets</u>	<u>Date of Registration</u>	<u>End of Fiscal Year</u>
	<u>Value of : Percent</u>	<u>Value of : Percent</u>
	<u>class : of total</u>	<u>class : of total</u>
Cash and cash items, including receivables		
Government securities		
Securities of other investment companies		
Other securities		
Other assets		
Total assets		

(b) With respect to each company in which the registrant had invested in all classes of such company's securities more than 5 percent of the value of the registrant's total assets --

<u>Name and address of company</u>	<u>Nature of its principal business</u>	<u>Percentage of value of registrant's assets invested therein</u>	
		<u>At date of : At end of</u>	<u>registration : fiscal year</u>

(c) With respect to each company, 5 percent or more of whose voting securities are directly or indirectly owned, controlled, or held with power to vote, by the registrant --

<u>Name and address of company</u>	<u>Nature of its principal business</u>	<u>Percentage of its voting securities owned by registrant</u>	
		<u>At date of registration</u>	<u>: At end of fiscal year</u>

Instructions. 1. Attention is directed to Section 5(b) and (c) of the Act. The term "value" is defined in Section 2(a)(39) of the Act.

2. If the registrant's latest fiscal year ended prior to the date of registration, the information need be given only as of the date of registration.

Item 7. Underwriting Commitments.

If the registrant is a diversified company, furnish the following information for the period from the date of registration to the close of the latest fiscal year covered by the financial statements filed herewith with respect to each commitment as underwriter made by the registrant:

(a) The value of the registrant's total assets immediately after each such commitment as underwriter.

(b) The dollar amount of all outstanding commitments as underwriters at such time.

(c) The value at such time of registrant's investments in all securities of issuers (other than investment companies) of which the registrant owned more than 10 percent of the outstanding voting securities.

Instruction. Instruction 2 to Item 6 shall also apply to this item.

Item 8. Tax Status.

State whether the registrant during the last taxable year met the requirements of Subchapter M of the Internal Revenue Code, and state its present intention with respect to meeting such requirements during the current taxable year.

Item 9. Pending Legal Proceedings.

Briefly describe any material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the registrant or any of its subsidiaries is a party. Include the name of the court in which the proceedings are pending, the date instituted, and the principal parties thereto. Include similar information as to any such proceedings known to be contemplated by governmental authorities.

Item 10. Capitalization.

Furnish the following information, in substantially the tabular form indicated as to each class of authorized securities of the registrant. The information is to be furnished as of the end of the registrant's latest fiscal year.

(1)	(2)	(3)	(4)
<u>Title of class</u>	<u>Amount authorized</u>	<u>Amount held by registrant or for its account</u>	<u>Amount outstanding exclusive of amount shown under (3)</u>

Item 11. Defaults and Arrears on Senior Securities.

(a) State, as to each issue of long-term debt of the registrant which is in default, on the date of filing, with respect to the payment of principal, interest or amortization: (1) Nature of default; (2) date of default; (3) amount of default per \$1,000 face amount; and (4) total amount of default.

(b) State as to each issue of capital stock of the registrant on which any accumulated dividend is in arrears at the date of filing: (1) Title of issue; (2) amount per share in arrears.

Item 12. Condensed Financial Information.

(a) Furnish the following information for the registrant, or for the registrant and its subsidiaries consolidated as prescribed by caption 3 of Rule 6-02 of Regulation S-X, for each of the last ten fiscal years of the registrant (or for the life of the registrant and its immediate predecessors, if less) and for the period between the end of the latest fiscal year and the date of the latest balance sheet or statement of assets and liabilities furnished:

PER SHARE INCOME AND CAPITAL CHANGES
(For a share outstanding throughout the year)

Income and Expense

19-- 19-- Etc

1. Income
2. Operating expenses
3. Net income
4. Dividends from net income

Capital Changes

5. Net asset value at beginning of period
6. Net realized and unrealized profits
(or losses) on securities
7. Distributions from realized capital gains

8. Net asset value at end of period
9. Ratio of operating expenses to average net assets
10. Ratio of net income to average net assets
11. Number of shares outstanding at end of period

Instructions. 1. The information shall be given in comparative columnar form, by years, in the order indicated by the captions of the item.

2. The information shall be given as to the shares of all open-end companies and, where practicable, as to the common shares of closed-end companies.

3. Per-share figures may be given to the nearest cent in all columns.

4. Appropriate adjustments shall be made to reflect any stock split-ups or stock dividends during the period.

5. "Operating expenses", as used in caption 2 above, include the expenses described in captions 2 and 3 of Rule 6-04 of Regulation S-X. If there were income deductions such as those described in captions 4 and 6 of that rule, compute the per-share amounts thereof in accordance with instructions 8(b) below and state them separately immediately after caption 2 above.

6. Distributions not exceeding the capital gains computed on the federal tax basis may be treated as distributions from capital gains for purposes of the above table, even though they exceed capital gains on a book basis.

7. If any distributions were made from capital sources other than capital gains, change caption 7 to: "Distributions from realized capital gains and other capital sources" and in a footnote indicate the amounts and nature of distributions from such other sources.

8. For open-end companies having continuous transactions in their own shares:

(a) The amount to be shown at caption 3 is derived by adding to, or deducting from, dividends paid from net income per share for the year (caption 4) the increase or decrease per share in undistributed net income for the year. Such increase or decrease may be derived from a comparison of the per-share figures obtained by dividing the undistributed net income at the beginning and end of the year by the number of shares outstanding on those respective dates.

(b) The amounts to be shown at captions 1 and 2 are derived by applying to the net income on a per-share basis the ratio of such items, as shown in the financial statements prepared under Rule 6-04 of Regulation S-X, to the net income as shown in such statements.

9. The amount to be shown at caption 6, while mathematically determinable by the summation of amounts computed for as many periods during the year as shares were sold or repurchased (which could be as often as twice daily) is also the balancing figure derived from the other figures in the statement and may be so computed. The amount shown at this caption for a share outstanding throughout the year may not accord with the change in the aggregate gains and losses in the portfolio securities for the year because of the timing of sales and repurchase of registrant's shares in relation to fluctuating market values for the portfolio.

10. The "average net assets", as used in captions 9 and 10 shall be computed upon the basis of the value of the net assets determined no less frequently than as of the end of each month, except that the average value of securities for which market quotations are not available may be based upon the value of such securities as of the end of the preceding quarter.

11. The number of shares outstanding at the end of each period may be shown to the nearest thousand (000 omitted), provided it is indicated that such has been done, or may be shown in a footnote.

(b) Furnish the following information as of the end of each of the registrant's last ten fiscal years with respect to each class of senior securities (including bank loans) of the registrant. If consolidated statements were prepared as of any of the dates specified, the information shall be furnished on a consolidated basis:

(1)	(2)	(3)	(4)	(5)
<u>Year</u>	Total amount outstanding, exclusive of treasury securities	Asset coverage per share or other unit	Involuntary liquidating preference per share of senior stock	Approximate market value per share or other unit (Exclude bank loans)

Instructions. 1. Instruction 2 to paragraph (b) shall also apply to this paragraph.

2. In lieu of the method described in Section 18(h) of the Act, asset coverage called for in Column (3) shall be expressed in terms of dollar amounts per unit of each class of senior securities. If the registrant has outstanding more than one class of securities, indicate the method used in computing the asset coverage.

Item 13. Persons in Control Relationship with Registrant.

Furnish a list or diagram of all persons directly or indirectly controlling, controlled by or under common control with the registrant and as to each such person indicate (1) if a company, the State or other sovereign power under the laws of which it was organized, and (2) the percentage of voting securities owned or other basis of control by the person, if any, immediately controlling it.

Instructions. 1. The list or diagram shall include the registrant and shall be so prepared as to show clearly the relationship of each company named to the registrant and to the other companies named. If any company is controlled by means of the direct ownership of its securities by two or more persons, so indicate by appropriate cross reference.

2. Designate by appropriate symbols (a) subsidiaries for which separate financial statements are filed; (b) subsidiaries included in the respective consolidated financial statements; (c) subsidiaries included in the respective group financial statements filed for unconsolidated subsidiaries; (d) other subsidiaries, indicating briefly why statements of such subsidiaries are not filed.

3. The names of particular subsidiaries may be omitted if the unnamed subsidiaries considered in the aggregate as a single subsidiary would not constitute a significant subsidiary.

Item 14. Persons Owning Equity Securities of Registrant.

Furnish the following information as to all equity securities of the registrant owned by the following persons as of a specified date within 90 days prior to the date of filing:

(a) Each person who directly or indirectly owns, controls or holds with power to vote, 5 percent or more of the outstanding voting securities of the registrant.

(b) Each person who owns of record or is known by the registrant to own beneficially more than 10 percent of any other class of equity securities of the registrant.

(c) All officers, directors and members of the advisory board of the registrant as a group, without naming them.

(1)	(2)	(3)	(4)	(5)
Name and address	Title of class	Type of ownership	Amount owned	Percent of class

Instructions. 1. Indicate in the third column whether the securities are owned both of record and beneficially, of record only, or beneficially only, and show separately in the fourth and fifth

columns the respective amounts and percentages owned in each such manner.

2. The percentages are to be calculated on the basis of the amount of outstanding securities of the class. In any case where the amount owned by all officers, directors and members of the advisory board as a group is less than 1 percent of the class, a statement to that effect will suffice as an answer to paragraph (c).

Item 15. Number of Holders of Equity Securities.

State, in substantially the tabular form indicated, as of a specified date within 90 days prior to the date of filing, the approximate number of holders of record of each class of equity securities of the registrant.

(1)	(2)
<u>Title of class</u>	<u>Number of holders</u>

Item 16. Directors and Executive Officers.

Furnish the information required by the following table as to all directors and executive officers of the registrant.

<u>Name and address</u>	<u>Positions and offices with registrant</u>	<u>Principal occupations during past five years</u>
-------------------------	--	---

Instruction. For the purposes of this item, the term "executive officer" means the president, vice-president, secretary and treasurer, and any other officer who performs policy-making functions for the registrant.

Item 17. Members of Advisory Board of Registrant.

If the registrant has an advisory board, furnish the information specified in the following table as to each member of such board.

(1)	(2)
<u>Name and address</u>	<u>Positions and offices held with other affiliated persons</u>

Instruction. List under Column (2) the name of each affiliated person of the registrant, other than members of the advisory board, with which any member of the advisory board is connected in any capacity and show all positions and offices held with such person.

Item 18. Remuneration of Directors, Officers and Members of Advisory Board.

(a) Furnish the information required by the following table as to all remuneration paid by the registrant and its subsidiaries during the registrant's last fiscal year to the following persons for services in all capacities:

(1) Each director, each of the three highest-paid officers, and each member of the advisory board of the registrant whose aggregate remuneration exceeded \$30,000, naming each such person.

(2) All directors, officers and members of the advisory board of the registrant as a group, without naming them.

(A)	(B)	(C)
Name of individual or identify of group	Capacities in which remuneration was received	Aggregate remuneration

Instructions. 1. This item applies to any person who was a director, officer or member of the advisory board of the registrant at any time during the fiscal year. However, information need not be given for any portion of the year during which any such person did not occupy one of the positions indicated.

2. The information is to be given on an accrual basis if practicable. The tables required by this paragraph and paragraph (b) may be combined if the registrant so desires.

3. Do not include remuneration paid to a partnership in which any director, officer or member of the advisory board was a partner, but see item 25.

4. If the registrant has not completed a full fiscal year since its organization, the information shall be given for the current fiscal year, estimating future payments if necessary.

(b) Furnish the following information, in substantially the tabular form indicated below, as to all pension or retirement benefits proposed to be paid under any existing plan in the event of retirement at normal retirement date, directly or indirectly, by the registrant or any of its subsidiaries to each person named in answer to paragraph (a)(1) of this item:

(A)	(B)	(C)
Name of individual	Amount set aside or accrued during issuer's last fiscal year	Estimated annual benefits upon retirement

Instructions. 1. Column (B) need not be answered with respect to payments computed on an actuarial basis pursuant to any plan which provides for fixed benefits in the event of retirement at a specified age or after a specified number of years of service.

2. The information called for by Column (C) may be given in a table showing the annual benefits payable upon retirement to persons in specified salary classifications.

3. In the case of any plan (other than those specified in instruction 1.) where the amount set aside each year depends upon the amount of earnings of the issuer or its subsidiaries for such year or a prior year, or where it is otherwise impracticable to state the estimated annual benefits upon retirement, there shall be set forth, in lieu of the information called for by Column (C), the aggregate amount set aside or accrued to date, unless it is impracticable to do so, in which case there shall be stated the method of computing such benefits.

Item 19. Indemnification of Directors and Officers.

State the general effect of any contract, arrangements or statute under which any director or officer of the registrant is insured or indemnified in any manner against any liability which he may incur in his capacity as such.

Instruction. No information need be given as to insurance provided by any director or officer for his own protection.

Item 20. Employees of Registrant.

Furnish the information required by the following table as of a specified date within 90 days with respect to the employees of (1) registrant and (2) any company of the character specified in Section 2(a)(19)(iii) of the Act.

<u>Class of employees</u>	<u>Number of full-time employees</u>	<u>Number of part-time employees</u>
Executive and research		
All other employees		

Item 21. Custodians of Portfolio Securities.

(a) State the name, principal business address and, if other than a commercial bank or trust company, the nature of the business of each person holding portfolio securities of the registrant as custodian.

(b) Describe the arrangements under which such securities are held, including the basis upon which the remuneration for such services is determined.

Item 22. Investment Advisers.

Furnish the following information as to each investment adviser of the registrant:

(a) Name and principal business address.

(b) Name and address of any affiliated person of the registrant who is also an affiliated person of the investment adviser and the nature of the affiliation.

(c) A brief description of the investment advisory contract with the registrant, including the basis for determining the remuneration of the investment adviser.

Item 23. Business and Other Connections of Investment Advisers and Their Managements.

Describe briefly any other business, profession, vocation or employment of a substantial nature in which each investment adviser of the registrant and each director, officer or partner of such investment adviser is engaged for his own account or in the capacity of director, officer, employee, partner or trustee.

Instructions. 1. State the name and principal business of any company with which any person specified is connected in the capacity of director, officer, employee, partner or trustee, and the nature of such connection.

2. The names of investment advisory clients need not be given in answering this item.

Item 24. Personnel of Investment Advisers.

Furnish the information required by the following table, in substantially the tabular form indicated, as of a specified date within 90 days with respect to all personnel (other than directors, officers, partners or proprietors) of each investment adviser of the registrant:

<u>Class of personnel</u>	<u>Number of full-time employees</u>	<u>Number of part-time employees</u>
Account supervisors, counsellors and executives		
Economists, statisticians and research personnel		
All other personnel		

Item 25. Remuneration of Certain Affiliated Persons.

Furnish the information required by the following table as to each of the persons specified below who received from the registrant and its subsidiaries during the last fiscal year of the registrant aggregate remuneration in excess of \$30,000 for services in all capacities. Indicate the nature of the relationship by reason of which the remuneration of each such person named is required to be given.

(a) Each affiliated person of the registrant other than its directors, officers, employees and members of its advisory board.

(b) Each affiliated person of any of the following: Its directors or officers, any member of its advisory board, any company named in answer to item 6(c), any security holder named in answer to item 14(a) or (b), any investment adviser, or any underwriter named in answer to Item 31.

<u>Name of person</u>	<u>Capacities in which services were rendered</u>	<u>Aggregate remuneration</u>
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Item 26. Capital Stock.

State the title of each class of capital stock of the registrant and furnish the following information:

(a) Outline briefly (1) dividend rights; (2) voting rights; (3) liquidation rights; (4) pre-emptive rights; (5) conversion rights; (6) redemption provisions; (7) sinking fund provisions; and (8) liability to further calls or to assessment by the registrant.

(b) If the rights of holders of such stock may be modified otherwise than by a vote of a majority or more of the shares outstanding, voting as a class, so state and explain briefly.

(c) Outline briefly any restriction on the repurchase or redemption of shares by the registrant while there is an arrearage in the payment of dividends or sinking fund installments. If there is no such restriction, so state.

Instructions. 1. Only a brief summary of the pertinent provisions from an investment standpoint is required. A complete legal description of the provisions referred to is not required and should not be given. Do not set forth the provisions of the governing instruments verbatim; only a succinct resume is required.

2. If the rights evidenced by any class of securities being described are materially limited or qualified by the rights of any other class of securities, include such information regarding such other securities as will enable investors to understand the rights evidenced by the securities being described.

Item 27. Long-Term Debt.

State the title of each class of long term debt of the registrant and outline such of the following provisions as are relevant.

(a) Provisions with respect to interest, maturity, conversion, redemption, amortization, sinking fund or retirement;

(b) Provisions with respect to the kind and priority of any lien,

restricting the declaration of dividends or requiring the maintenance of any ratio of assets, the creation or maintenance of reserves or the maintenance of properties;

(c) Provisions permitting or restricting the issuance of additional securities, the incurring of additional debt, the release or substitution of assets securing the issue, the modification of the terms of the security, and similar provisions.

(d) The name of the trustee and the nature of any material relationship with the registrant or any of its affiliates, the percentage of securities of the class necessary to require the trustee to take action, and what indemnification the trustee may require before proceeding to enforce the lien.

Instruction. The instructions to Item 26 shall also apply to this item.

Item 28. Other Securities.

If the registrant has any authorized securities other than capital stock or long-term debt, outline briefly the rights evidenced thereby. If the securities are subscription warrants or rights, state the title and amount of securities called for, the period during which and the prices at which the warrants or rights are exercisable.

Instruction. The instructions to Item 26 shall also apply to this item.

ITEMS 29 TO 33 APPLY ONLY TO OPEN-END INVESTMENT COMPANIES

Item 29. General Information as to Distribution of Securities.

(a) State whether the registrant is currently offering its securities for sale.

(b) List all States and other jurisdictions in which securities of the registrant may lawfully be sold by the registrant, its underwriters or dealers.

Item 30. Pricing of Securities for Sale, Redemption or Repurchase.

(a) Describe briefly the method followed or to be followed by the registrant in determining the price at which its securities will be offered to the public, redeemed or repurchased, and furnish a specimen price make-up sheet showing the method of computing the offering, redemption or repurchase price per unit, using as a basis the value of the registrant's portfolio securities and other assets and its outstanding securities as of the date of the balance sheet filed for the registrant.

Instructions. 1. State the number of times each day the offering,

redemption or repurchase price is determined, the time when such price becomes effective and the length of time it remains in effect.

2. Explain fully any difference in the price at which securities are offered to the public and the redemption or repurchase price.

(b) State the sales load expressed as a percentage of the public offering price and indicate the portion thereof to be received by dealers and the portion to be retained by the principal underwriter.

Instructions. 1. If the sales load varies on a quantity basis, indicate the quantities and the respective loads applicable thereto. However, the allocation between underwriters and dealers need be given only with respect to the maximum load.

2. Indicate briefly any difference in the sales load charged upon the sale of securities in connection with the conversion or exchange of securities or the reinvestment of dividends and similar distributions.

(c) Describe briefly any provision in the registrant's charter or in any subscription agreement or other instrument which specifically authorizes or requires the reinvestment in the registrant's securities of the proceeds of dividends or similar distributions made thereon.

Item 31. Principal Underwriters.

Furnish the following information with respect to each principal underwriter currently distributing securities of the registrant:

(a) Name and principal business address and nature of any material relationship with the registrant (other than that of principal underwriter).

(b) The name of each investment company (other than the registrant and closed-end companies) for which such underwriter also acts as a principal underwriter, depositor or investment adviser.

Item 32. Management of Principal Underwriters.

Furnish the information required by the following table with respect to each director, officer or partner of each principal underwriter named in answer to Item 31.

<u>Name and principal business address</u>	<u>Positions and offices with underwriter</u>	<u>Positions and offices with registrant</u>
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Item 33. Compensation of Underwriters.

Furnish the information required by the following table with respect

to all commissions and other compensation and profits received by each principal underwriter named in answer to Item 31 directly or indirectly from the registrant during the registrant's last fiscal year:

(1)	(2)	(3)	(4)	(5)
Name of principal underwriter	Underwriting Net discounts and commissions	Compensation or profit on redemptions and repurchases	Brokerage commissions	Other compensation

Instruction. Indicate in a note, or otherwise, the nature of the services rendered in consideration of the compensation set forth under Column (5). Include under this column any compensation received by an underwriter for keeping the registrant's securities outstanding in the hands of the public.

Item 34. Financial Statements and Exhibits.

List all financial statements and exhibits filed as a part of the registration statement.

- (a) Financial statements.
- (b) Exhibits.

SIGNATURE

Pursuant to the requirements of the Investment Company Act of 1940, the undersigned registrant (or depositor or trustee) has caused this registration statement to be signed on its behalf in the City of _____ and State of _____ on the _____ day of _____, 19____.

(Name of registrant, depositor or trustee)

By _____
(Name and title of person signing on behalf of registrant, depositor or trustee)

Witness: _____
(Name and title)

INSTRUCTIONS AS TO FINANCIAL STATEMENTS

These instructions specify the financial statements required to be filed as a part of a registration statement on this form. Regulation S-X governs the certification, form and content of the statements required, including the basis of consolidation, and prescribes the statements of surplus and schedules to be filed in support thereof.

A. STATEMENTS OF THE REGISTRANT1. Balance Sheets and Statements of Assets and Liabilities.

(a) The registrant shall file a certified balance sheet or statement of assets and liabilities as of the close of its latest fiscal year unless such fiscal year has ended within 90 days prior to the date of filing, in which case the statements may be as of the close of the preceding fiscal year.

(b) If the latest fiscal year of the registrant has ended within 90 days prior to the date of filing and the statement required by paragraph (a) is filed as of the end of the preceding fiscal year, there shall be filed as an amendment to the registration statement, within 120 days after the date of filing, a certified statement of the registrant as of the end of its latest fiscal year.

2. Statements of Income and Expense, Realized and Unrealized Gain or Loss on Investments.

The statements specified in Rules 6-04, 6-05 and 6-06 of Regulation S-X shall be filed for the registrant for each of its last three fiscal years preceding the date of the statement required by Instruction 1(a) and for the fiscal year immediately preceding the date of each statement filed pursuant to Instruction 1(b). Such statements shall be certified.

B. CONSOLIDATED STATEMENTS3. Consolidated Balance Sheets and Statements of Assets and Liabilities.

(a) There shall be filed a certified consolidated balance sheet or statement of assets and liabilities of the registrant and its subsidiaries as of the close of the latest fiscal year of the registrant, unless such fiscal year has ended within 90 days prior to the date of filing, in which case this statement may be as of the close of the preceding fiscal year.

(b) If the latest fiscal year of the registrant has ended within 90 days prior to the date of filing and the statement required by paragraph (a) is filed as of the end of the preceding fiscal year, there shall be filed as an amendment to the registration statement, within 120 days after the date of filing, a certified consolidated balance sheet or statement of assets and liabilities of the registrant and its subsidiaries as of the end of the latest fiscal year.

4. Consolidated Statements of Income and Expense, Realized and Unrealized Gain or Loss on Investments.

The statements specified in Rules 6-04, 6-05 and 6-06 of Regulation S-X shall be filed for the registrant and its subsidiaries consolidated for each of the last three fiscal years preceding the date of the consolidated statement required by Instruction 3(a) and for the fiscal year immediately preceding the date of each consolidated statement filed pursuant to Instruction

3(b). Such statements shall be certified.

C. UNCONSOLIDATED SUBSIDIARIES

5. Unconsolidated Subsidiaries.

(a) Subject to Rules 4-03 and 6-02-3 of Regulation S-X regarding group statements of unconsolidated subsidiaries, there shall be filed for each subsidiary of the registrant not consolidated, the financial statements which would be required if the subsidiary were itself a registrant. However, the profit and loss statements or statements of income and expense, realized and unrealized gain or loss on investments filed for any subsidiary which is less than majority-owned need cover only the last fiscal year immediately preceding the date of the balance sheet or statement of assets and liabilities filed for such subsidiary.

(b) If the fiscal year of any unconsolidated subsidiary ends within 90 days before the date of filing the registration statement, or ends after the date of filing, the financial statements of the subsidiary may be filed as an amendment to the registration statement within 120 days after the end of the subsidiary's fiscal year.

6. Omission of Statements Required by Instruction 5.

Notwithstanding Instruction 5, there may be omitted from the registration statement all financial statements of any one or more unconsolidated subsidiaries if all such subsidiaries for which statements are so omitted, considered in the aggregate as a single subsidiary, would not constitute a significant subsidiary.

D. GENERAL PROVISIONS

7. Reorganization or Succession.

(a) If, during the period for which statements of income and expense, realized and unrealized gain or loss on investments are required to be filed with the registration statement, the registrant has emerged from a reorganization in which substantial changes occurred in its asset, liability, capital share, surplus or reserve accounts, a brief explanation of such changes shall be set forth in a note or supporting schedule to the balance sheets or statements of assets and liabilities filed.

(b) If, during such period, the registrant has acquired by merger, consolidation or other succession one or more businesses representing, in the aggregate, assets valued in excess of 15% of the value of the registrant's assets at the time of filing, the additions, eliminations and other changes effected in the succession shall be appropriately set forth in a note or supporting schedule to the balance sheets or statements of assets and liabilities filed. In addition, profit and loss or income statements for each business so acquired, or combined statements if appropriate, shall be filed for such period prior to the succession as may be necessary when added to the time, if any, for which profit and loss or income statements after the succession are

filed to cover the equivalent of three full fiscal years.

8. Filing of Other Statements in Certain Cases.

The Commission may, upon the informal written request of the registrant, and where consistent with the protection of investors, permit the omission of one or more of the statements herein required or the filing in substitution thereof of appropriate statements of comparable character. The Commission may also by informal written notice require the filing of other statements in addition to, or in substitution for, the statements herein required in any case where such statements are necessary for an adequate presentation of the financial condition of any person whose financial statements are required, or whose statements are otherwise necessary for the protection of investors.

E. HISTORICAL FINANCIAL INFORMATION

9. Scope of Part E.

The information required by Part E shall be furnished for the seven-year period preceding the period for which profit and loss statements or statements of income and expense, realized and unrealized gain or loss on investments are filed, as to the accounts of each person whose balance sheet or statement of assets and liabilities is filed. The information is to be given as to all of the accounts specified whether they are presently carried on the books or not. Part E does not call for an audit, but only for a survey or review of the accounts specified. It should not be detailed beyond a point material to an investor. Information may be omitted, however, as to any person for whom equivalent information for the period has been filed with the Commission pursuant to the Securities Act of 1933 or the Securities Exchange Act of 1934.

10. Revaluation of Assets.

(a) If there were any material increases or decreases in investments, in property, plant and equipment, or in intangible assets, state (1) in which year or years such revaluations were made; (2) the amounts of such increases or decreases, and the accounts affected, including all related entries; and (3) if in connection with such revaluations any related adjustments were made in reserve accounts and amounts with explanations.

(b) Information is not required as to adjustments made in the ordinary course of business, but only as to major revaluations made for the purpose of entering in the books current values, reproduction cost, or any values other than original cost.

(c) No information need be furnished with respect to any revaluation entry which was subsequently reversed or with respect to the reversal of a revaluation entry recorded prior to the period if a statement as to the reversal is made.

11. Capital Shares.

(a) If there were any material restatements of capital shares which resulted in transfers from capital share liability to surplus or reserve, state the amount of each such restatement and all related entries. No statement need be made as to restatements resulting from the declaration of share dividends.

(b) If there was an original issue of capital shares, any part of the proceeds of which was credited to accounts other than capital share accounts, state the title of the class, the accounts and the respective amounts credited thereto.

12. Debt Discount and Expense Written Off.

If any material amount of debt discount and expense, on long-term debt still outstanding, was written off earlier than as required under any periodic amortization plan, give the following information: (1) title of the securities, (2) date of the write-off, (3) amount written off, and (4) to what account charged.

13. Premiums and Discount and Expense on Securities Retired.

(a) If any material amount of long-term debt or preferred shares was retired and if either the retirement was made at a premium or there remained, at the time of retirement, a material amount of unamortized discount and expense applicable to the securities retired, state for each class (1) title of the securities retired, (2) date of retirement, (3) amount of premium paid and of unamortized discount and expense, (4) to what account charged, and (5) whether being amortized and, if so, the plan of amortization.

(b) In the case of preferred shares, the premium or discount shall be measured by the difference between the price paid and the involuntary liquidating preference of the shares. This Instruction 13 does not apply to open-end investment companies.

14. Discount on Securities Retired.

If any material amount of long-term debt or preferred shares was retired and if such retirement was made at a discount, state for each year and with respect to each such class of securities (1) the title of the class retired, (2) the amount of discount, and (3) to what account credited. Instruction 13(b) above shall also apply here.

15. Other Changes in Surplus.

If there were any material increases or decreases in surplus, other than those resulting from transactions specified above, the closing of the income and profit and loss accounts or the declaration or payment of dividends, state (1) the year or years in which such increases or decreases

were made; (2) the nature and amounts thereof; and (3) the accounts effected, including all material related entries. Instruction 10(c) above shall also apply here.

16. Predecessors.

The information shall be furnished, to the extent it is material, as to any predecessor of the registrant from the beginning of the period to the date of succession, not only as to the entries made respectively in the books of the predecessor or the successor, but also as to the changes effected in the transfer of the assets from the predecessor. However, no information need be furnished as to any one or more predecessors which, considered in the aggregate, would not constitute a significant predecessor.

17. Omission of Certain Information.

(a) No information need be furnished as to any subsidiary, whether consolidated or unconsolidated, for the period prior to the date on which it became a subsidiary of the registrant or a predecessor for which information is required above.

(b) No information need be furnished hereunder as to any one or more unconsolidated subsidiaries for which separate financial statements are filed if all subsidiaries for which the information is so omitted, considered in the aggregate as a single subsidiary, would not constitute a significant subsidiary.

(c) Only the information specified in Instruction 10 need be given as to any predecessor or any subsidiary thereof if immediately prior to the date of succession thereto by a person for which information is required, the predecessor or subsidiary was in insolvency proceedings.

INSTRUCTIONS AS TO EXHIBITS

Subject to the rules regarding incorporation by reference, the following exhibits shall be filed as a part of the registration statement. Exhibits shall be appropriately lettered or numbered for convenient reference. Exhibits incorporated by reference may bear the designation given in the previous filing. Where exhibits are incorporated by reference, the reference shall be made in the list of exhibits called for by Item 35.

1. Copies of the charter as now in effect.
2. Copies of the existing by-laws or instruments corresponding thereto.
3. Copies of any voting trust agreement with respect to more than ten percent of any class of equity securities of the registrant.
4. (a) Specimens or copies of each security issued by the registrant, including copies of all constituent instruments, defining the rights of the

holders of such securities.

(b) Copies of the constituent instruments defining the rights of holders of long-term debt of all subsidiaries for which consolidated or unconsolidated financial statements are required to be filed.

(c) The instruments relating to any class of long-term debt of the registrant or any subsidiary need not be filed if the total amount of securities authorized thereunder amounts to less than 2% of the total assets of the registrant and its subsidiaries on a consolidated basis and if the registrant files an agreement to furnish copies of such instruments to the Commission upon request.

5. Copies of all investment advisory contracts to which the registrant is party.

6. If the registrant is an open-end investment company, copies of each underwriting or distributing contract between the registrant and a principal underwriter, and specimens or copies of all agreements between principal underwriters and dealers.

7. Copies of all bonus, profit sharing, pension or other similar contracts or arrangements wholly or partly for the benefit of directors or officers of the registrant. If any such plan is not set forth in a formal document, furnish a reasonably detailed description thereof.

8. Copies of all custodian agreements with respect to portfolio securities of the registrant.

9. Copies of all other material contracts not made in the ordinary course of business which are to be performed in whole or in part at or after the date of filing the registration statement.

10. Copies of each notice sent to stockholders pursuant to Section 19 of the Act prior to the date of filing this form.

11. Copies of each notice and communication sent to stockholders pursuant to Section 23(c)(1) of the Act. This exhibit may be omitted if such notice or communication is contained in a report to stockholders, copies of which are required to be filed with the Commission.

12. Copies of each notice of an opportunity to submit tenders and each solicitation of tenders under Section 23(c)(2) of the Act.

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OFFICE OF
THE CHAIRMAN

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

DEC 4 1970

Honorable Harley O. Staggers
Chairman, Special Subcommittee on Investigations
Committee on Interstate and Foreign Commerce
House of Representatives
Washington, D. C. 20515

Dear Chairman Staggers:

This is with further reference to your request of October 1, 1970 for additional information supplementing Commissioner Richard B. Smith's testimony of September 24, 1970 during the hearings on Penn-Central before your Special Subcommittee on Investigations.

In our initial response of November 24, 1970, we indicated that our Chief Accountant, Mr. Andrew Barr, had been in touch with his counterpart at the ICC, Mr. Mathew Paolo, regarding your additional request for ". . . an analysis of the differences in accounting treatment by the ICC and the SEC with respect to the issuance and marketing of securities."

Since then, Mr. Barr reviewed with Mr. Paolo the draft of the reply prepared by ICC in response to your separate request to that agency on this matter. Mr. Barr made several suggestions on that draft which were incorporated in the reply as ultimately sent to you on November 25, 1970 by Chairman George M. Stafford of the ICC. We have now reviewed Mr. Stafford's November 25th reply to you and we concur in it.

I believe that this completes the information which was requested by your Special Subcommittee in your letter of October 1, 1970 for inclusion in the record of the Penn-Central hearings of September 24, 1970, but there has been one change in the facts contained in the memorandum we sent to you earlier which you may want to note in the printed hearings. At the top of page 17 of our memorandum we noted that the Exchange had suspended trading in 21 debt obligations of rail lines leased by the Penn Central Transportation Company and that "trading in these obligations is still suspended." This information was true at the time the memorandum was initially drafted by the staff, but we learned thereafter that this suspension was lifted and trading was resumed on November 16, 1970.

Sincerely yours,

A handwritten signature in cursive script, appearing to read "Hamer A. Budge".
Hamer A. Budge
Chairman

APPENDIX C

-MEMORANDUM OF THE DIVISION OF CORPORATE REGULATION
ON THE POSSIBLE DUAL REGULATORY STATUS OF
INVESTMENT COMPANY -- CARRIERS

POSSIBLE DUAL REGULATORY STATUS OF INVESTMENT COMPANY -- CARRIERS

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MEMORANDUM

RE: POSSIBLE DUAL REGULATORY STATUS OF
INVESTMENT COMPANY - CARRIERS

I. Allegheny's Present Regulatory Status

A. Registration as an Investment Company in 1968

As of January 31, 1968, more than 40 percent of Allegheny Corporation's ("Allegheny") assets consisted of investment securities. Thus, on its face, Allegheny would have been an investment company on that date within the meaning of Section 3(a)(3) of the Investment Company Act were it not for the fact that it controlled various railroads, including the New York Central Railroad Co. ("Central"). Because of such control, it was "subject to regulation under the Interstate Commerce Act" within the meaning of Section 3(c)(9) of the Investment Company Act. As a consequence it was excluded from the definition of investment company.

On February 1, 1968, Central merged with the Pennsylvania Railroad. At that point, it became questionable whether the surviving entity, the Penn-Central Railroad ("Penn-Central"), was controlled by Allegheny. As a result of the merger, Allegheny held less than 1 percent of the outstanding voting securities of the Penn-Central, and only 11 of the 25 directors of Penn-Central were directly or indirectly designated by Allegheny.^{1/} To avoid any question respecting the validity of its activities, Allegheny registered as a closed-end, non-diversified management

^{1/} Allegheny had disposed of 84.6 percent of its stock holdings of the Central in 1966, reducing its ownership of such shares from 14.2 percent to 2.2 percent of the shares outstanding; nevertheless, all of the directors of Central had continued to be Allegheny nominees, 9 of the Central directors were also directors of Allegheny and Allegheny continued to control the Central.

investment company under the Investment Company Act on April 10, 1968 and subjected itself to SEC regulation. Subsequently, Alleghany applied for and was granted an exemption from Section 7 of the Investment Company Act for the period from February 1 through April 10, 1968.

As an investment company, Alleghany has filed its quarterly, semi-annual and annual reports and proxy materials with the Securities and Exchange Commission as is required of all investment companies by the Investment Company Act of 1940. Nevertheless, Alleghany maintains that it is a company subject to regulation under the Interstate Commerce Act pursuant to the outstanding order of the Interstate Commerce Commission ("ICC"), dated March 2, 1955, and that it is not an investment company. It maintains that its investment company registration statement is filed

"solely for the purpose of eliminating such uncertainty, if any, as may exist as to Alleghany Corporation's status as a company subject to regulation under the Interstate Commerce Act and constitutes neither an admission that Alleghany Corporation is an investment company within the meaning of the Investment Company Act of 1940 nor a waiver by Alleghany Corporation of any rights or status."

B. Acquisition of Jones Motor Co.

Alleghany is attempting to simplify its present regulatory status by acquiring and operating a motor carrier, Jones Motor Co. ("Jones"). Actually, Alleghany has a twofold objective: (1) to subject itself to plenary jurisdiction and regulation as a carrier by the ICC which would permit it to avail itself of the 3(c)(9) exclusion from the Investment Company Act and (2) to provide Alleghany with sufficient operating revenues to avoid the possibility of its being taxed as a personal holding company.

To achieve these objectives, Alleghany's program is as follows:

1. Alleghany acquired over 98% of Jones' outstanding common stock and 100% of its outstanding preferred stock by means of a tender offer. Alleghany proposes, pursuant to a merger agreement to acquire the bulk of Jones' nondepreciable assets, including cash and receivables, prepaid items and its franchises and operating rights and to assume substantially all of Jones' current liabilities. The merger is conditioned upon, among other things, approval by the ICC. Pending such approval Alleghany's Jones stock has been deposited with Marine Midland Grace Trust Co. of New York, an independent voting trustee.

2. To obtain ICC approval, Alleghany has filed with the ICC at least three applications under the Interstate Commerce Act:

The first, which was filed October 4, 1968, requests relief from the status of a carrier which resulted when on March 2, and May 24, 1955, the ICC, by order, declared Alleghany to be a "noncarrier considered as a carrier" and subjected Alleghany to regulation under Sections 20(1) to (10) and 20(a) of the Interstate Commerce Act. It is based on the premise that Alleghany does not control the Penn-Central. 1/

The second, which was filed October 29, 1968, pursuant to Section 212(b) of the Interstate Commerce Act (49 U.S.C. 312(b)) requested permission for Alleghany to acquire the assets and operating rights of Jones.

1/ Penn-Central has filed an application with the ICC for authority to make it a wholly owned subsidiary of Penn-Central Holding Company. Under this proposal, stockholders of Penn-Central would exchange their shares for those of the holding company. The holding company will have 12 directors. If the exchange of shares is approved by the ICC and consummated, only one of the directors of Alleghany, Fred M. Kirby, will also be a director of the holding company.

- 4 -

Alleghany's third ICC application, filed on April 9, 1969, under Section 5(2)(a)(i) of the Interstate Commerce Act, requests permission to acquire control of Jones, consummate the merger, and acquire Jones' operating certificate. It has a number of possible jurisdictional bases:

- a. Alleghany's acquisition of Jones, if Alleghany retains its status as a carrier (either by virtue of the outstanding 1955 ICC orders or by its control in fact of various carriers) may be a "purchase, lease, or contract to operate the properties of another carrier" by a carrier within the meaning of Section 5 (2)(a)(i) of the Interstate Commerce Act.
- b. Since Jones has trucking subsidiaries, Alleghany may be acquiring two or more carriers or a carrier system. If Alleghany is no longer a carrier, that portion of Section 5(2)(a)(i) may apply which requires the approval and authorization of the ICC for "a person which is not a carrier to acquire control of two or more carriers through ownership of their stock or otherwise."
- c. If Alleghany, in fact, controls one or more carriers and if Alleghany itself is no longer a carrier, that portion of Section 5(2)(a)(i) may apply which requires the approval and authorization of the ICC for a "person which is not a carrier and which has control of one or more carriers to acquire control of another carrier through ownership of its stock or otherwise."
3. The Alleghany shareholders, at the company's April 25, 1969 annual meeting, voted to amend the company's Articles of Incorporation to allow it to engage in the business of a common carrier and authorized it to cease to be an investment company.
4. If the ICC grants the requested applications, Alleghany intends to file an application with the SEC pursuant to Section 8(f) of the Investment Company Act to terminate its status as an investment company on the ground that it is a carrier subject to regulation by ICC and, therefore, is excluded from the definition of an investment company under Section 3(c)(9).

C. Alleghany's Portfolio At December 31, 1968

At December 31, 1968, Alleghany had total assets of over \$242 million. Of this amount, \$13.3 million, or 5.6 percent, was invested in Jones. Alleghany's largest holding, 44.8 percent of Alleghany's assets, at December 31, 1968, was in Investor Diversified Services, Inc. ("IDS"). IDS is now in the business of providing a number of financial services. Its status as an investment company was therefore terminated on February 20, 1969. Alleghany through its ownership of 46.6 percent of IDS' outstanding voting securities controls IDS.

In addition, at December 31, 1968, Alleghany had invested more than 5 percent of its total assets in each of three other companies as follows:

Percentage of Alleghany's Assets	Name of Company	Percentage of Voting Securities of Subject Company Owned by Alleghany
18.1	Missouri-Pacific Railroad Company ("Mo Pac")	Less than 5 percent of total outstanding shares of Class A and B capital stock combined, but 52.3 percent of the Class B
5.1	Penn-Central	0.85 percent ^{1/}
9.2	Manufacturers Hanover Trust Company ("Mfrs. Hanover")	Less than 5 percent

^{1/} IDS is the investment adviser of a number of investment companies, three of which at December 31, 1968, owned 1,020,000 shares, or roughly 4.4 percent of the outstanding common stock of Penn-Central. However, at June 30, 1969, two of the investment companies had sold all of their Penn-Central shares and one held only 437,300 Penn-Central shares, or roughly 1.9 percent of Penn-Central's outstanding stock. Thus, assuming no changes in Alleghany's portfolio since December 31, 1968, the combined holdings of Alleghany and the investment companies advised by IDS at June 30, 1969, totaled 643,495 shares, or roughly 2.75 percent. In addition, Fred M. Kirby, Chairman of the Board of Alleghany Corporation and of IDS, is co-guardian of assets which includes 390,130 shares, or 1.7 percent, of the voting stock of Penn-Central.

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The balance of Alleghany's assets were invested as follows:

5 percent	--	Other securities
6.4 percent	--	In cash and cash items
5.8 percent	--	Other assets

Thus, 5 holdings accounted for 83 percent of Alleghany's assets and, looking only at these holdings, more than half of Alleghany's total assets (54 percent) were invested in financial service organizations (IDS and Mfrs Hanover) while 28.8 percent of its assets were invested in railway and motor carriers including Jones.

D. Section 3(c)(9) As Applied to Alleghany's Present Status

The Section 3(c)(9) exclusion from the Investment Company Act does not apply unless the ICC determines that Alleghany is a carrier or grants it carrier status subjecting it to plenary regulation by the ICC. Neither consideration by the ICC of a Section 5(2)(a) application, such as acquisition of a single carrier or carrier system by a noncarrier, nor the existence of an unrevoked ICC order conferring carrier status on Alleghany where the basis for such status no longer exists, nor the combination of such an outstanding order and ICC consideration of such a 5(2) application would amount to "regulation by the ICC" within the meaning of Section 3(c)(9) of the Investment Company Act. ICC jurisdiction over transactions involving the acquisitions of carriers is not the type of general regulation of internal affairs which justifies exclusion under Section 3(c)(9) of the Investment Company Act.

If the ICC grants the Alleghany applications and subjects Alleghany to its plenary jurisdiction under Sections 5(2), 5(3), 20, 20a, 12(1) or comparable sections of the Interstate Commerce Act, we would consider that under present law, Alleghany was "subject to regulation by the Interstate Commerce Commission" within the meaning of Section 3(c)(9) of the Investment Company Act.

II. Background of Alleghany as an Investment Company and Carrier

A. Control of the C & O

Alleghany first registered as a closed-end, non-diversified management company on November 1, 1940, the day the Investment Company Act took effect. In June, 1945, 86 percent of Alleghany's total assets was invested in securities of carriers including 38 percent in the stock of the Chesapeake & Ohio Railway Company ("C & O"). Only about 5 percent was invested in securities of other companies. On the basis of Alleghany's control of the C & O and C & O subsidiaries, the ICC issued an order, dated June 5, 1945, pursuant to Section 5(3) of the Interstate Commerce Act, declaring, among other things, that Alleghany be deemed to be a carrier and specifically imposing upon Alleghany the broad ICC regulatory requirements of Sections

20(1) to (10) and 20a(2) to (11) respecting such matters as issuance of securities, interlocking officers and directors, the manner of keeping accounts and records, and the filing of reports (261 ICC 239 (1945)).

Thereafter Alleghany filed an application with the Securities and Exchange Commission ("SEC") to terminate its registration as an investment company pursuant to Section 8(f) of the Investment Company Act. On October 4, 1945, the SEC, on the basis of the ICC's order and an examination of the provisions of the Interstate Commerce Act declared applicable to Alleghany, found that Alleghany was "subject to regulation under the Interstate Commerce Act" within the meaning of Section 3(c)(9) of the Investment Company Act. Accordingly, the SEC declared that Alleghany "has ceased to be and is not now an investment company," and ordered that Alleghany's registration

"shall forthwith cease to be in effect, provided, however, that if in the future Alleghany Corporation ceases to be subject to regulation under the Interstate Commerce Act . . . this order may be revoked, suspended or modified after appropriate notice and opportunity for hearing" (Alleghany Corporation 20 SEC 731 (1945)).

Between 1945 and 1953 Alleghany disposed of the bulk of its C & O stock, acquired a control block of the stock of IDS, which was then a registered investment company, and assumed the business characteristics of an investment company with a varied portfolio of securities. On January 19, 1954, Alleghany disposed of its remaining C & O stock and reduced its investment in transportation securities to 8 percent of its total assets. Learning of these facts, the ICC, on June 22, 1954, ordered Alleghany to show cause why its 1945 order should not be vacated and set aside insofar as it provided that Alleghany should be considered as a carrier subject to ICC regulation.

B. Control of the New York Central

Alleghany replied on June 29, 1954, indicating that it had acquired control of the New York Central Railroad Company ("Central"). It requested postponement of ICC action in order to permit the filing of an application for approval of a contemplated rearrangement by Central of the ownership and control of its subsidiaries, as well as a declaration of the continuation of Alleghany's status as a company "considered as a carrier" subject to ICC regulation.

(1) Proceedings Before the Regulatory Agencies

In view of the changed character of Alleghany's business, on July 7, 1954, the SEC issued a Notice and Order for Hearing pursuant to the reservation of jurisdiction contained in its 1945 order. On July 19, 1954, Alleghany requested that the SEC hearing be postponed pending the outcome of the ICC proceeding to determine whether to continue to subject Alleghany to regulation as provided in Section 5(3) of the Interstate Commerce Act.

On September 17, 1954, Alleghany, joined in an application by the Central and its subsidiaries, filed with the ICC pursuant to Section 5(2) of the Interstate Commerce Act for approval of an Intra-system merger and lease modification. In connection with this application, Alleghany sought a determination from the ICC that it be deemed a carrier by reason of its alleged control of the Central.

By stipulation dated October 14, 1954, the SEC proceedings were postponed subject to call. Alleghany agreed that if the ICC revoked, modified or suspended its order of June 5, 1945, in such manner as to relieve Alleghany from compliance with certain provisions of the Interstate Commerce Act specified in said Order, Alleghany would not, without first obtaining approval of the SEC, engage in any act or consummate any transaction which it could not if it were a registered investment company.

The SEC intervened in the ICC proceedings, taking the position that in view of Alleghany's investment portfolio and investment activities, Alleghany was again an investment company within the definition of this term contained in the Investment Company Act and

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that the transactions in which Alleghany had been engaged were of a kind which Congress sought to be regulated under the Investment Company Act.

The SEC took the position that since under Section 5(3) of the Interstate Commerce Act a company may be deemed a carrier "to the extent provided by the Commission in such order," the ICC, in its discretion, should limit its jurisdiction over Alleghany to any acquisition of carriers under Section 5(2) and that, without "carrier" status, Alleghany would thus be subject to the broader and more comprehensive regulatory provisions of the Investment Company Act.

The ICC, Division 4, on March 2, 1955, rejected the SEC's position, approved the merger and continued Alleghany's status as a non-carrier to be considered as a carrier subject to the regulatory provisions provided by Section 5(3) of the Interstate Commerce Act.

(Louisville & J. B. & R. Co. Merger, 290 ICC 725 (1955)). This decision was affirmed by the full Commission on May 24, 1955, which also held that it had no discretion to yield jurisdiction over Alleghany to the SEC (Louisville & J. B. & R Co. Merger, 295 ICC 11 (1955)). On May 26, 1955, two days later, Division 4 approved a new issue of convertible preferred stock by Alleghany.

In its May 24, 1955 opinion the ICC also considered whether Alleghany should have secured its prior approval before acquiring Central. To resolve that question, the ICC looked to whether Alleghany was in the transportation business at the time of the Central acquisition. If the 1945 order had remained effective, then ICC approval would have been necessary. The ICC concluded that such approval was not needed because

Alleghany ceased to be a carrier for regulatory purposes under the 1945 order after its divestiture of the C & O stock. The ICC held, however, that Alleghany was to be considered as a carrier again effective after its newly acquired control over Central, 295 ICC 11 at 16-17 (1955).

(2) The Breswick Litigation

Immediately thereafter, minority common stockholders of Alleghany commenced an action to enjoin the enforcement of and set aside these orders. The overriding issue in the case was whether Alleghany was required to be registered as an investment company subject to SEC regulation at the time it issued its preferred stock. If it were required to be regulated as an investment company, its preferred stock issue would have been void. The policy question was whether companies such as Alleghany, which were predominantly investment companies, but which controlled carrier systems, should be regulated by the ICC, the SEC, or both.

In granting a temporary injunction, Breswick & Co. v. United States, 134 F. Supp. 132 (S.D.N.Y., 1955), and then a permanent injunction, Breswick & Co. v. United States, 138 F. Supp. 123 S.D. N.Y., 1955), the District Court held that the ICC was in error in concluding that Alleghany should be considered as a carrier based upon its newly acquired control of Central and that the ICC had no authority to approve the issue of preferred stock.

On appeal to the Supreme Court, the SEC maintained that, for purposes of Section 3(c)(9), the test is whether or not a company "is subject to regulation under the Interstate Commerce Act" and that the term regulation

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necessarily denotes continuous supervisory jurisdiction on the part of ICC over certain of the internal affairs of the subject company.

Hence, the SEC argued

"the exception applies only when a company is subject to continuing ICC supervision. It was not the intention of the Congress to absolve a company, otherwise an investment company, from complying with the Investment Company Act because on occasion it makes an acquisition which requires approval by the ICC under Section 5(2) of the Interstate Commerce Act, but which does not impose upon it the type of continuous ICC regulation which may be required under Section 5(3) of that Act." (Brief of the Securities and Exchange Commission, amicus curiae Alleghany Corporation v. Breswick & Co., et al, October term, 1956) 1/

Instead of dealing directly with the policy issue, the Supreme Court focused on the provisions of the Interstate Commerce Act; particularly, the jurisdiction of the ICC under Sections 5(2) and 5(3) of the Interstate Commerce Act. It held that validity of Alleghany's status order under Section 5(3) turned on compliance with the statutory requirements of Section 5(2) of ICC approval

"for a person which is not a carrier (Alleghany) and which has control of one or more carriers (Central) to acquire control of another carrier (Louisville & J. B. & K. Co.) through ownership of its stock or otherwise....."

The Court had to decide whether the merger of one controlled subsidiary of the Central into another met the statutory requirement of Section 5(2).

This raised three questions:

- (1) Was ICC approval of Alleghany's acquisition of control of Central required?
- (2) Did Alleghany in fact control Central?
- (3) Did the transaction involving the merger of Central's subsidiaries involve the acquisition of control by Alleghany over the properties of the merged subsidiaries?

1/ The SEC's views were submitted to aid in resolving issues raised under the Investment Company Act. The SEC took no position on whether the District Court had correctly construed the relevant provisions of the Interstate Commerce Act or orders of the ICC thereunder; nor on the extent of the jurisdiction of the District Court.

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The District Court had held that whatever control Alleghany had over Central did not fit within the statutory requirement of "a person which is not a carrier and which has control of one or more carriers" because the ICC had not given the approval necessary for acquisition of control of Central and its subsidiaries' "two or more carriers." (138 F. Supp. 123) The ICC and Alleghany contended that ICC approval of the acquisition of a single, integrated system was not necessary. The Supreme Court found it unnecessary to decide this question and intimated no opinion on it.

The District Court had also ruled that when Alleghany had divested itself of the control of all carriers, the 1945 ICC order became inoperative "empty fiat" so that Alleghany was no longer excepted under Section 3(c)(9) from the definition of an investment company (134 F. Supp. at 142; 138 F. Supp. at 129). The Supreme Court also found it unnecessary to consider this question. Moreover, On December 9, 1955, during the pendency of the proceedings, Alleghany had registered as an investment company.

The Supreme Court found that Alleghany in fact controlled the Central within the meaning of Section 5(2). It decided that Section 5(2) did not require "approved control"; and that, therefore, Alleghany was a person, not a carrier, which had control of one or more carriers ("the Central"). It also held that the merger of two Central subsidiaries was the acquisition of control by the Central over the merged company because it accomplished a significant increase in the power of the Central over the merged company.

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Thus, the Supreme Court sustained ICC jurisdiction over Alleghany, upheld Alleghany's status as carrier and reversed the judgment of the District Court. It remanded the case to the District Court for consideration of the claim that "the preferred stock issue as approved by the Commission was in violation of the Interstate Commerce Act." Mr. Justice Douglas, dissented, noting that by granting Alleghany carrier status, it "escapes the far more rigorous supervision which is imposed on it by the Investment Company Act" (353 U.S. 151 at 179).

The District Court then sustained the stock issue against attack on its basic fairness, but enjoined the order approving the issue on the ground that the ICC had not approved applicant's acquisition of control of a subsidiary as a necessary preliminary to approval of the stock issue. (156 F. Supp. 227) The decision of the District Court on remand was reversed, *per curiam*, on the ground that the basis of its decision was precluded by the mandate and opinion of the Supreme Court. (355 U.S. 415)

(3) The Dissent

Mr. Justice Douglas again dissented (the Chief Justice and Mr. Justice Black concurring in the dissent). His dissent urged that it was necessary to decide whether or not acquisition of a carrier system is the acquisition of "two or more carriers" within the meaning of Section 5(2)(a)(1) of the Interstate Commerce Act because Section 5(4) of the Interstate Commerce Act makes it unlawful without ICC approval for any person to enter into any transactions within the scope of Section 5(2)(a).

The dissent quoted with approval the decision of the District Court (156 F. Supp. 227 at 236) which held that

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"The approval of acquisition and continued control is an obvious first question in any application by Alleghany because unless the Commission intends to approve this control . . . it would be granting a wrongdoer sanctuary from the Investment Company Act; . . ." (355 U.S. 415 at 422 (1957)).

Finally, the dissent raised the question whether Congress intended to permit

"such broken-field running between two statutes, designed to protect the public interest, without a full inquiry by the Commission (ICC) into the primary acquisition of control of Central by Alleghany?" (355 U.S. 415 at 423).

(4) Subsequent Litigation Involving Alleghany

Several months after the Supreme Court opinion the question of the vitality of the 1945 ICC order was raised again in a related stockholders derivative action, Schwartz v. Bowman, 156 F. Supp. 361 (S.D. N.Y., 1957), appeal dismissed sub nom Schwartz v. Eaton, 264 F. 2d 195 (C.A. 2, 1959), which complained that the disposal of the C & O stock and the other transactions effected prior to the ICC's 1955 reassertion of jurisdiction were in violation of the Investment Company Act. In that action, it was again argued that the 1945 order was in effect so that Alleghany was excluded from the Investment Company Act, under Section 3(c)(9), at the time of the transactions in issue. And again, the Court refused to so hold. Citing the language in Breswick & Co. v. United States, 138 F. Supp. 123 (S. D. N. Y., 1955), the Court ruled that an order subjecting a company to regulation as if it were a carrier must have, as its basis, the company's

- 17 -

active participation in a transportation business.^{1/}

In summary, the Alleghany litigation resulted in the conclusion that the 3(c)(9) exclusion from the Investment Company Act was unavailable when the 1945 ICC order became inoperative as a result of Alleghany's departure from the transportation business (See 156 F. Supp. at 363 citing with approval 138 F. Supp. at 129) but it became available again when Alleghany re-entered the transportation business.

III. Hoover v. Allen (Regulation of the American Hawaiian Steamship Co.)

- Hoover v. Allen (241 F. Supp. 213 (S.D.N.Y. 1965))

involved a claim by the American-Hawaiian Steamship Company, a dormant water carrier, that it was subject to regulation within the meaning of Section 3(c)(9) because it held a Certificate of Public Convenience and Necessity from the ICC. The court held that the mere existence of ICC jurisdiction by itself was insufficient to satisfy the provisions of Section 3(c)(9).

^{1/} In Schwartz v. Bowman (244 F. Supp. 51 (S.D.N.Y. 1965, certiorari denied 385 U.S. 921) and again in Schwartz v. Alleghany Corp. (282 F. Supp. 161 (S.D.N.Y.)) based upon substantially the same facts, the issue of whether or not Alleghany ceased to be subject to ICC regulation when it divested itself of C. & O. stock, was again raised. In both instances, the court circumvented the issue on the grounds that it lacked jurisdiction to consider the questions raised.

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Guided by Mr. Justice Brennan's concurring opinion in S.E.C. v. Variable Annuities Life Insurance Co. (359 U.S. 65 at 73), the Court examined the type of regulation to which the company is or may be subject by the ICC. Looking to the general purposes of the Investment Company Act, as stated in Section 1(b), the Court determined that the exclusory provisions of Section 3 of the Investment Company Act must be narrowly construed (241 F. Supp. 213 at 246). It held that, in order to avail itself of the 3(c)(9) exclusion, a company would have to be subject to regulation by the ICC under Sections 20, 20(a), 12(1) and 5(2) or comparable sections of the Interstate Commerce Act (241 F. Supp. 213 at 248).^{1/}

Thus, under this decision, plenary jurisdiction of a substantial nature by the ICC over a company, otherwise an investment company, is necessary to satisfy the requirements of Section 3(c)(9) of the Investment Company Act -- the mere repose of jurisdiction in the ICC is not sufficient.

^{1/} Sections 20(1) - (10) require the filing of annual, periodic and special reports. They authorize the ICC to prescribe the times and forms for filing reports, and to establish uniform systems of accounts, rates of depreciation charges, and the forms of any accounts, records and memoranda to be kept (to which the ICC shall have access). They also prescribe penalties for failure to comply with such requirements and authorize the institution of mandamus proceedings to compel compliance. Section 20(a) provides for ICC regulation over the issuance of securities or assumption of debt by railroads and curtails the establishment of interlocking directors; Section 12(1) provides ICC authority to "inquire into and report on the management" of carriers by rail subject to its jurisdiction, and Section 5(2) provides generally for ICC approval or authorization of the merger, consolidation and acquisition of carriers, their properties or franchises.

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 JAMES F. HASTINGS, N.Y.

Congress of the United States
 House of Representatives
 Committee on Interstate and Foreign Commerce
 Room 2125, Rayburn House Office Building
 Washington, D.C. 20515

W. E. WILLIAMSON, CLERK

March 10, 1969

CHAIRMAN'S OFFICE
 RECEIVED

MAR 11 1969

SEC. & EXCH. COMM.

Hon. Hamer H. Budge
 Chairman
 Securities and Exchange Commission
 Washington, D. C. 20549

Dear Chairman Budge:

Your Commission has been asked routinely to comment upon several bills which I introduced having to do with carrier control, including H.R. 7373 and H.R. 7374.

In this connection, I am enclosing a copy of the release which I issued on February 20 at the time of the introduction of the bills.

In your reply, I wish that you would consider the beneficial question of whether or not the Interstate Commerce Commission has jurisdiction of whether or not the carrier is head of a system or if it does not, whether you have jurisdiction in this area. I am reminded of the raising of this question in Alleghany Corp. v. Brewster & Company, decided April 22, 1957, and January 27, 1958.

Sincerely yours,

Harvey O. Staggers
 HARVEY O. STAGGERS, M.C.
 CHAIRMAN

HOS:ml1

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Congress of the United States
 House of Representatives
 Committee on Interstate and Foreign Commerce
 Room 2123, Rayburn House Office Building
 Washington, D.C. 20515

15
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 Assembly
 please

April 17, 1969

CHAIRMAN'S OFFICE
RECEIVED

APR 22 1969

SEC. & EXCH. COMM.

Hon. Hamer H. Budge
 Chairman
 Securities and Exchange Commission
 Washington, D. C. 20515

Dear Chairman Budge:

I am enclosing herewith copy of a news article in the Daily Traffic World of April 10 relative to the filing by Alleghany Corporation of an application with the Interstate Commerce Commission under section 5 of the Interstate Commerce Act to acquire control of Jones Motor Company, Inc.

Naturally, this reminds me of a previous circumstance wherein the same company was involved and the filing of the merger application under section 5 and the ensuing decisions of the Supreme Court leading to the retention of jurisdiction in the Interstate Commerce Commission rather than in the Securities and Exchange Commission under the Investment Company Act. Indeed this news article states that one of the reasons given by Alleghany for acquiring this motor carrier is that of removing any ambiguity resulting from the dual status of Alleghany under the Interstate Commerce Commission and as an investment company under the Securities and Exchange Commission.

I wish that you would explain to me just what is the situation regarding Alleghany, having in mind the decision of the Supreme Court in Alleghany Corporation vs. Breswick & Co., et al, 353 U.S.151 and 353 U.S.415, with particular reference to the dissenting opinion of Justice Douglas regarding the jurisdiction of the two Acts, and whether there continues to be any ambiguity here that needs clarification by legislation.

Sincerely yours,

Harley O. Staggers
 HARLEY O. STAGGERS, M.C.
 CHAIRMAN

Hearings before a Subcommittee of the Committee on Interstate and Foreign Commerce, House of Representatives on H. R. 2481 (86th Cong. 1st. Sess.), pp. 408-413.

V. ICC regulation of holding companies and its purposes

Railroad holding companies were first subjected to regulation by the ICC pursuant to the provisions of the Emergency Railroad Transportation Act of 1933 (48 Stat. 217-220). The legislative history of that act makes it abundantly clear that its purpose was twofold, namely, (i) to prevent, through the holding company device, the unification of operating railroads without the ICC supervision which was contemplated by the Transportation Act of 1920; and (ii) to prevent the holding companies from creating top-heavy capital structures which would create pressures on the operating railroad subsidiaries to indulge in unsound financial practices in order to service excessive amounts of holding company fixed-return securities.¹⁹ The applicable provisions of the Interstate Commerce Act are as follows:

Section 5(2) provides, in pertinent part:

"(a) It shall be lawful, with the approval and authorization of the Commission,

* * * * *

"(i) * * * For a person which is not a carrier to acquire control of two or more carriers through ownership of their stock or otherwise; or for a person which is not a carrier and which has control of one or more carriers to acquire control of another carrier through ownership of its stock or otherwise;

* * * * *

"(c) in passing upon any proposed transaction under the provisions of this paragraph (2), the Commission shall give weight to the following considerations, among others: (1) The effect of the proposed transaction upon adequate transportation service to the public; (2) the effect upon the public interest of the inclusion, or failure to include, other railroads in the territory involved in the

¹⁹ Senate hearings on S. 3580, pt. 2, p. 777.

²⁰ *Ibid.*

²¹ Commissioner Eastland, speaking on behalf of the Interstate Commerce Commission, the sponsor of S. 2903, stated, *inter alia*, that because of the lack of powers over the investments of railroads in subsidiaries, which in turn invested in noncontrolling interests in railroad and other securities, that the law as then in force was not "adequate to protect the investor in railroad securities." Hearings before a subcommittee of Committee of Interstate Commerce on S. 2610 (successor to S. 1310 and subsequently amended and reintroduced as S. 2903), 76th Cong., 1st sess., p. 30.

²² Hearings before the House Committee on Interstate and Foreign Commerce on H.R. 9050, 72d Cong., 1st sess., pp. 67-74; see also pp. 247-250.

proposed transaction; (3) the total fixed charges resulting from the proposed transaction; and (4) the interest of the carrier employees affected.

* * * * *

"(c) No transaction which contemplates a guaranty or assumption of payment of dividends or of fixed charges, shall be approved by the Commission under this paragraph (2) except upon a specific finding by the Commission that such guaranty or assumption is not inconsistent with the public interest. No transaction shall be approved under this paragraph (2) which will result in an increase of total fixed charges, except upon a specific finding by the Commission that such increase would not be contrary to public interest."¹¹

Section 5(3) of the Interstate Commerce Act provides as follows:

"(3) Whenever a person which is not a carrier is authorized, by an order entered under paragraph (2), to acquire control of any carrier or of two or more carriers, such person thereafter shall, to the extent provided by the Commission in such order, be considered as a carrier subject to such of the following provisions as are applicable to any carrier involved in such acquisition of control: Section 20 (1) to (10), inclusive, of this chapter, sections 304(a)(1) and (2) and 320 of chapter 8 of this title, and section 913 of chapter 12 of this title, (which relate to reports, accounts, and so forth, of carriers), and section 20a(2) to (11), inclusive, of this chapter, and section 314 of chapter 8 of this title, (which relate to issues of securities and assumptions of liability of carriers), including in each case the penalties applicable in the case of violations of such provisions. In the application of such provisions of section 20a of this chapter and of section 314 of chapter 8 of this title, in the case of any such person, the Commission shall authorize the issue or assumption applied for only if it finds that such issue or assumption is consistent with the proper performance of its service to the public by each carrier which is under the control of such person, that it will not impair the ability of any such carrier to perform such service, and that it is otherwise consistent with the public interest."

Sections 20(1) to 20(10) relate primarily to the authority of the ICC in connection with railroads and certain other carriers to require the filing of annual, periodic and special reports; they authorize the ICC to prescribe the times and forms for filing reports; and to establish uniform systems of accounts, rates of depreciation charges, and the forms of any accounts, records and memorandums to be kept (to which the ICC shall have access); they prescribe penalties for failure to comply with such requirements and authorize the institution of mandamus proceedings to compel compliance.

Motor carriers and water carriers are subjected to similar regulatory provisions by chapters 8 and 12, respectively, of the Interstate Commerce Act. Sections 20a(2) to 20a(11), in general, require the prior approval of the ICC for the issuance of securities and the assumption of liabilities. Section 314 subjects motor carriers and controlling persons thereof to the provisions of section 20a, but no provision is made for the regulation of water carriers or freight forwarders in this respect.

VI. Comparison of investor protection afforded under the Interstate Commerce Act and under the Investment Company Act

(a) *Financial structure.*—The standards of sections 5 (2) and (3) and 20a(2) of the Interstate Commerce Act for approval of the issuance of securities or assumption of liabilities by a holding company are designed essentially for the protection of the underlying carriers subject to its control, although questions of fairness to security holders have been given consideration by the ICC. The primary objective of these sections is the prevention of excessive fixed charges at the holding company level determined on a case-by-case basis in light of the purposes for which the securities are issued, and the capital structures of the controlled companies. To the extent that railroads and railroad holding companies attain sound financial structures, investors will undoubtedly be benefited.

The capital structure requirements of the Investment Company Act are more definitive and particularly pertinent to an investment company, whether diversified or nondiversified. Section 18 of the Investment Company Act, in recognition of the adverse effect on the public interest found by the Congress

¹¹ The phrase "public interest" as used in section 5(2) of the Interstate Commerce Act, as amended, means "public interest in the maintenance of an adequate rail transportation system" (*United States v. Lowden*, 308 U.S. 225).

to result from excessive senior securities contains specific limitations and requirements as to the senior securities which may be issued by a registered closed-end investment company.²² Its purposes are twofold, namely, to afford adequate protection to the holder of the senior security itself, and to prevent the common stock of the investment company from becoming unduly speculative as a result of the leverage which attends senior securities.

Section 18(a) of the Investment Company Act prohibits the issuance of senior securities representing indebtedness unless there is a minimum asset coverage of 300 percent for all such indebtedness, and provision is made to prohibit dividends or distributions on the capital stock unless these asset coverages exist. Similarly, the issuance of senior securities representing preferred stocks is prohibited unless there is a minimum asset coverage of 200 percent for the combined indebtedness and preferred stock, and certain other restrictive investor safeguards are included, such as the power to control the board of directors in the event of specified defaults in preferred stock dividends and dividend restrictions. Long term warrants are prohibited by section 18(d); common stock must have equal voting rights pursuant to section 18(i). Section 23 contains restrictive provisions covering the sale of an investment company's stock at less than its net asset value.

(b) *Other protective measures not covered by the Interstate Commerce Act.*—Because of its different primary objectives, the Investment Company Act contains provisions in addition to those noted above which are not touched upon in the Interstate Commerce Act. Section 21, for example, prohibits "upstream loans" by an investment company to a controlling person. Section 23 is designed to protect investors from dilution or discriminatory treatment upon the repurchase by the investment company of any of its outstanding stock.

A most important provision designed to protect the investment company against improvident self-dealing transactions with "insiders," and other affiliated persons, is found in section 17 (a) and (b), which prohibit most insider transactions unless excepted by specific order of the Commission pursuant to a finding, among other things, that "the terms of the transactions, including the considerations to be paid or received, are reasonable and fair and do not involve overreaching." The statute provides for a hearing at which interested persons, including public investors, may be heard and present evidence bearing on the question of whether the foregoing statutory standard has been satisfied. In addition, protective measures are contained in subsections (d), (e), (f), (g), (h), and (i) of section 17. Subsection (d) prohibits "insiders" from participating jointly with the investment company in certain transactions in contravention of SEC rules to prevent unfairness to the investment company. Subsection (e) prevents rebates, indirect commissions, or "kickbacks" on the purchase and sale of the investment company's properties or securities and the charging of excessive brokerage commissions; subsections (f) and (g) contain provisions designed to safeguard the assets of the company by custodial arrangements and the bonding of persons with access to cash or securities; subsections (h) and (i) prohibit certain exculpatory charter or bylaw provisions which would purport to protect certain insiders from liability to the company for willful misconduct, bad faith, gross negligence or reckless disregard of their duties.

Other investor protective measures provided by the Investment Company Act pertinent to the type of investment company here involved include: requirements for a minimum number of independent directors (section 10); requirements for specific statements of the investment policies of the company and a requirement that stockholders must consent to any change therein (sections 8(b) and 13(a)); restrictions against pyramiding of investment companies (section 12(d)) and cross-ownership (section 20(c)); provisions covering the election of directors (section 16(a)) and the appointment of independent accountants (section 32). The Commission is authorized to bring suit to enjoin plans of reorganization believed to be grossly unfair (section 25(c)) and to cause the removal of management found to be guilty of gross misconduct or gross abuse of trust (section 36). Section 19 requires that the source of dividends, whether from capital or earnings, be disclosed to shareholders.

Reporting requirements under both acts are discussed below.

²² Section 1(b)(7) of the act provides that "the national public interest and the interest of investors are adversely affected . . . (7) when investment companies by excessive borrowing and the issuance of excessive amounts of senior securities increase unduly the speculative character of their junior securities; . . ."

The foregoing presentation should make it abundantly clear that just as the basic purposes of the Interstate Commerce Act and the Investment Company Act differ, so do the kinds of regulation imposed under both acts differ and the powers granted to the agencies administering this regulation. While both overlap in a limited area, they do not necessarily coincide nor are they coextensive. Some of the transactions in which Allegheny has engaged, which were not subject to the approval of the ICC but would have been subject to the approval of the SEC in the interests of investors, are set forth in appendix A.

In the light of the foregoing there would seem to be no basis for Mr. Wallace's statement that the ICC jurisdiction and scrutiny in the interests of investors is "more sweeping and pervasive" than the jurisdiction specifically designed for those interests in the Investment Company Act. We need note only that Chairman Tuggle of the ICC in his letter to the Senate, dated June 16, 1959, stated that he sees "no good reason why either a carrier or a noncarrier which is primarily engaged in the business of an investment company should be exempt from the broader regulation applicable to other investment companies which is provided for in the Investment Company Act," save for limited purposes.

VII. Concurrent regulation by the SEC and the ICC

As the committee is aware we have submitted a revised section 7, which would add a new paragraph (C) to section 3(c)(9) and add a new section 6(f) to the act. These revisions have been worked out with the Interstate Commerce Commission. Their purpose and effect is set forth in a separate memorandum submitted herewith. The bill as revised would (a) subject the investment activities of these essentially investment companies to regulation under the Investment Company Act and (b) subject the carrier and related activities of these companies and their operating subsidiaries to the exclusive regulatory jurisdiction of the Interstate Commerce Act. It also embodies an accommodation in those areas in which, because of the dual nature of the companies involved as investment companies with control over carriers or with some carrier operations, their activities may impinge on the national public interest as it is expressed in the Investment Company Act and as it is expressed in the Interstate Commerce Act.

The area of overlapping jurisdiction, is fortunately, not great. As noted, the ICC has jurisdiction over the acquisition of control of two or more carriers by persons who are not carriers. The Investment Company Act requires only that the intention to acquire such control be stated among the investment policies which the company adopts. No conflict is to be anticipated here.

If the acquisition of control over carriers is to be made from an affiliated person of the investment company, it would require a finding by the SEC under section 17 that it was a fair transaction before it might be consummated. However, the SEC is of the view that such an acquisition is essentially a carrier operation as a "unification of railroads," and therefore of direct concern to the ICC in the implementation of the national transportation policy. Accordingly, as manifested in the new section 6(f), we propose that a transaction of this character be subjected only to the scrutiny of the ICC. Presumably the ICC's powers are sufficiently pervasive to consider any unfairness aspect of the matter. Similarly, were this hypothetical acquisition of a controlling block of stock of a railroad to be financed by the issuance of securities, ICC approval thereof under section 20a would be required. If these securities meet the standards of section 18 of the Investment Company Act no approval of the SEC would be required even if the company were fully subject to the requirements of the Investment Company Act. Here again, since the unification of railroads is at issue and the security issuance is incidental, we propose in section 6(f) to make section 18 inapplicable to this type of transaction and thus preserve the exclusive and plenary jurisdiction of the ICC under section 20a.

In keeping with our approach where matters of carrier operations are directly involved, we further propose in section 6(f) that companies which are primarily engaged in carrier or related operations and which are affiliates of an investment company, be exempted from the affiliate restrictions of section 17 of the Investment Company Act in their transactions between themselves or with other persons relating to their carrier or related operations. This exemption contained in new section 6(f), is designed to reach the problems which Mr. Gray, counsel to the New York Central, outlined in his statement to this committee.

So far as the investment activities of the investment-holding company are concerned, many of these activities are beyond the reach of the Interstate Commerce Commission and presently are unregulated. The effect of the revised bill would be to subject certain of these activities to regulation solely under the Investment Company Act. Obviously no conflict of regulation will arise in these situations.¹³

We turn now to the areas in which there will be dual regulation; namely, the issuance of securities, accounting and reporting.

We propose that the issuance of securities by investment-holding companies, for purposes other than the financing of carrier or related operations or the acquisition of control over carriers, be subject to regulation under the Interstate Commerce Act and the Investment Company Act.

In a given case the provisions of section 18 of the Investment Company Act may impose more restrictive standards on the issuance of senior securities (i.e., debt and preferred stocks) than may be thought necessary by the ICC under section 20a in order to limit the parent company's fixed charges in the interests of controlled carriers and their security holders. It is difficult to see how compliance with these more restrictive standards will detrimentally affect these interests. To the extent that the converse situation obtains the ICC jurisdiction will remain and its exercise will be without detriment to the parent company investors.

Similarly, the interests of carriers and their security holders would not be adversely affected if a parent investment company could not finance its investment activities, or make adjustments in its capital structure, by the use of long term warrants or rights to purchase common stock, which are proscribed by the provisions of section 18(d) of the Investment Company Act.

Alleghany has represented to this committee that the ICC in approving the exchange of its convertible 6 percent preferred stock for its outstanding 5½ percent preferred stock determined that the "best interests of the national transportation system and of investors in Alleghany justified the issuance of Alleghany's 6 percent preferred stock." Alleghany would thus imply that the action of the SEC in failing to exempt the issuance of this stock from section 18(d) of the Investment Company Act was detrimental to these interests. Contrary to Alleghany's representation the ICC stated:

"It does not appear that the proposed issue will adversely affect any carrier under the control of the applicant, or impair such carriers' ability to serve the public. Nor, with the modification hereinafter stated, does it appear that the proposal will be unfair or inequitable to any class of the applicant's stockholders."

It then made the statutory findings required by the Act.¹⁴

The preferred stock exchange was designed as a method of eliminating the arrears on the outstanding preferred stock, which had been accumulating for over 25 years. Thus, the impediment to payment of dividends on Alleghany's common stock would be removed. Other methods of accomplishing this objective existed. The record created before the SEC disclosed that these alternatives were not considered by Alleghany's management to be as advantageous to the holders of common stock. The SEC found that the new preferred stock was in essence a right to purchase common stock within the intentment of section 18(d) of the act. This right to purchase was not only a highly volatile and speculative security, but it rendered the common stock as well highly volatile and speculative. Both securities were rendered inherently difficult to evaluate and the very experts introduced to support the exemption application differed sharply as to values. In the light of the entire record, the SEC could not find the exemption consistent with the protection of investors.

¹³ Certainly, the many unregulated transactions in which Alleghany has engaged, shown in appendix A, do not evidence a particular concern for the interests of investors in its subsidiary railroad securities whom Alleghany now so vigorously seeks to protect from the alleged ineptitude of the SEC. We do not comment upon the protection afforded the interests of Alleghany's own investors to be found in these unregulated transactions since many of them formed the basis of derivative stockholders' actions which are now in the process of settlement.

¹⁴ The ICC found that the transactions were "consistent with the proper performance of its service to the public by each carrier which is under the control of such corporation, that it will not impair the ability of any such carrier to perform such service, that it is otherwise consistent with the public interest, and that it (a) is for lawful objects within its corporate purposes and compatible with the public interest, which are necessary and appropriate for and consistent with the proper performance by such carrier of service to the public as a common carrier, and which will not impair its ability to perform that service, and (b) is reasonably necessary and appropriate for such purposes."

Because of the adverse effect of this type of security on investors, both present and future, the Investment Company Act proscribes management's choice to issue this type of security and compels a more conventional method of accomplishing the objectives sought by the proposed exchange. It is this kind of restriction on management's choice, made in the interests of one class of its security holders, which causes Alleghany's present obsession with "strangulation," rather than dual regulation.

Section 23 of the Investment Company Act would also be applicable to the issuance of securities for investment purposes. Generally speaking section 23 prohibits the issuance of securities for services or property and prevents the issuance of common stock at less than net asset value. Refusal of the SEC or ICC to permit the issuance of watered securities or securities resulting in dilution would not adversely affect either interest these agencies seek to protect, nor would it create any conflict.

Of the same genre are the conflicts which Alleghany suggests might exist if the SEC invokes the powers under section 25 of the Investment Company Act to "thwart" ICC approval of securities. The only powers under section 25 which could be used in the manner suggested are those granted to a district court of the United States to enjoin the consummation of any plan of reorganization which the court determines "to be grossly unfair or to constitute gross misconduct or gross abuse of trust on the part of the officers, directors, or investment advisers of such registered company or other sponsors of such plan." Even were the farfetched assumption to be made that the ICC would approve the issuance of securities in connection with such a plan, its plenary and exclusive jurisdiction may in any event be thwarted under existing law by a suit of stockholders. Section 25 merely grants the SEC the power to bring proceedings, in the statutory words, "upon behalf of security holders of such registered company, or any class thereof." It creates no new conflicting rights.

Section 30 of the Investment Company Act, as interpreted by the SEC, imposes no requirements as to the keeping of accounts other than compliance with sound accounting principles. This would not require any changes in the method of internal accounting followed by the type of investment companies we are concerned with here. The reports required to be filed with the SEC under the Investment Company Act would contain all of the substantive data and most of the details contained in the reports currently being filed with the ICC. The reports to the SEC would be supplemented, however, with data essential to the interests of investors, such as disclosure of realized gains or losses on investments, statements of unrealized appreciation or depreciation of investments, information showing the value as well as the cost of each investment and information showing separately the distribution made to shareholders from net investment income and from realized gain on investments. Information is also required as to ratios of operating and management expenses to average value of total net assets and total investment income.

Any fears that the interests of the consumer and investor public in carriers might be adversely affected by concurrent SEC regulation of these investment companies are wholly without foundation. The SEC is fully aware of the impact of parent company activity on its subsidiaries and the consumer and investment interests therein. Indeed, the fundamental purposes of the Public Utility Holding Company Act of 1935, which the SEC administers, is the protection of the public interest and the interests of investors and consumers. To this end extensive powers over the affairs of electric and gas utility holding companies and their operating subsidiaries are granted the SEC. State regulation of operating utility companies is thus to be made more effective. Similarly, certain electric utility companies which are subject to the Federal Power Commission jurisdiction in respect of rates, accounting and other regulatory matters, are also subject to the SEC's concurrent jurisdiction, which is paramount in the event of conflict.

Alleghany has sought to create the impression that if it were subject to regulation under the Investment Company Act many of the securities which it has issued would be unlawful and to the extent that conversion or exchange rights exist thereunder they would be inoperable. The Investment Company Act has never been construed to invalidate the rights created by securities which were issued by companies in good faith at a time when they were not subject to the Act. Alleghany's status at the time it issued its outstanding securities has been definitively determined by the Supreme Court of the United States. We do not believe, as Alleghany has suggested to the SEC, that the bill need include specific provisions to affirm the validity of these contract rights.