Holding Companies

[William Jennings Bryan] urged greater regulation of trusts even more floridly in 1899: “When I lived upon a farm . . . we used to protect property from the hogs by putting rings in [their] noses . . . . The thought came to me that one of the great purposes of government was to put rings in the noses of hogs.”

Holding companies were already attracting criticism. Ohio Attorney General Wade Ellis in 1905 called them “the most effective, and most invidious, and the cheapest of all combinations in restraint of trade . . . . the promoters have the use of the investment of all the minority holders in all the corporations brought under their control. . . . Thus a vast industry is brought under the domination of manipulators.”

A majority of the capitalization of holding companies typically took the form of bonds and non-voting preferred stock, leaving all the voting rights with the owners of the common stock. Because a minority of voting shares is usually enough to exert control, this arrangement would allow [Samuel] Insull to control all the operating utilities with a minority of just the common stock of Middle West, a very small percentage of the total worth of the utilities. This practice of issuing preferred stock without voting rights, which was becoming increasingly common, was described by Harvard political economist and critic of corporate economics William Z. Ripley as “a bald and outrageous theft of the last tittle of responsibility for management of the actual owners by those who are setting up these latest financial erections.” His admonition did not deter Insull. He anticipated acquiring many more utilities throughout the Midwest, with the holding company mechanism providing needed funds.

As the economy began to recover from the recession of 1920-21, more utility owners began to create holding companies, and owners of existing holding companies began to add layers. The burgeoning empires swallowed more than 300 private utilities each year, with municipal utilities also an attractive target. Electric utilities needed about six times as much investment as manufacturing companies to generate a dollar of annual revenue. With the industry growing by leaps and bounds, equity provided by local business leaders and loans provided by local banks could never have met the need. Historian Thomas P. Hughes considers the holding company as important to solving the adolescent industry’s capital shortage as Edison’s inventions were to eliminating the infant industry’s technological bottlenecks.

The advantages were undeniable. The holding companies could provide good management advice, acquire capital on favorable terms, build larger and more efficient plants, and obtain better prices by purchasing in larger quantities.

They could also apply more effective pressure on government, through campaign contributions or expert testimony before regulatory commissions, to keep rates from being cut as fast as technological advances might warrant.

With no effective regulatory scrutiny, holding companies could also pad the management and engineering contracts with their utilities. According to a study by the Twentieth Century Fund, such contracts "provided opportunities … to drain considerable sums from operating companies into the pockets of a few people who controlled the holding companies." Frederick Lewis Allen of *Harper's Weekly* wrote that holding companies could siphon revenues from electricity customers "so adroitly that a regulating commission could not see it go."

In late January any remaining hopes of cooperation were dashed. Three utility executives, Willkie, Clarence E. Groesbeck of Bond and Share, and Harvey C. Couch, president of a holding company in Arkansas, Louisiana, and Mississippi, sought a meeting with the president. They wanted to clarify his views on holding companies, rural electrification, and government dams. Lilienthal and Commissioners McNinch and Basil Manly of the Federal Power Commission also attended.

Roosevelt ran through a list of holding company abuses, and Lilienthal wrote in his journal that he could see Willkie "getting hotter and hotter…. Finally, he took his glasses out of his breast coat pocket and using them as a pointer, he leaned over and pointing this object at the President as he spoke, said, 'If you will give us a Federal incorporation law, we can get rid of holding companies.' He didn't preface it by 'Mr. President,' and he didn't say it with the courtesy that you would accord if you were addressing the vice president of a bank, much less the President of the United States. And from the moment he did this pointing job, the conference was on a completely different basis."

In the Senate . . . a special investigating committee chaired by a crusading New Deal supporter from Alabama, Hugo Black, was especially vigorous. Black had called holding companies "a blood-sucking business, a vampire" and believed an exposure of utility lobbying practices would undercut the industry's credibility, and his tactics included broad subpoenas for messages between utility officials and their lobbyists. Civil libertarians objected vehemently, but he did not back down.

. . . . Black heard from a Congressman who had received over eight hundred telegrams against the bill from a small town in his northwestern Pennsylvania district. Three out of four of the senders' names started with one of the first few letters of the alphabet, which suggested the names had been plucked out of a phone book or list of utility customers. When contacted, many of the supposed senders denied having sent them. Black's staff determined that the

local office of Associated Gas & Electric (AG&E), a ten-layer holding company pyramid, had told one of its salesmen to generate the telegrams.

The committee also discovered that AG&E had paid messenger boys three cents for each signature obtained. Black called one of them, 19-year-old Elmer Danielson, as a witness, asking the boy if the petitioners had known what they were signing. To much laughter, the unsophisticated teenager said he explained the complicated Wheeler-Rayburn bill to them. Corcoran later wrote that the exchange “really turned the tide of almost certain defeat for Roosevelt.” Black told a friend, “Another revelation like that, and we will compel the House to approve the death sentence.”

But Black needed a better villain than a young messenger, and he found one. He had announced on July 14 that he intended to subpoena Howard C. Hopson, the founder and president of AG&E. Hopson was described by one writer as “the crown prince of corporate jazz” who surpassed Insull in “holding company legerdemain.”

Aided by his tax return, which Roosevelt ordered released, in violation of normal procedures, Black elicited a wealth of evidence against Hopson. Money that should have been paid as dividends had been diverted to Hopson as income. He’d also received millions in income from a personally owned utility service company. Prodigious revenues from ratepayers had been devoted to lobbying, telegrams to Congress had been mass manufactured, and records had been destroyed. Hopson became the new face of holding company abuses.

While the TVA battle was being waged on several fronts, the challenges to the Holding Company Act continued to work their way through the courts. Because the Supreme Court had previously struck down regulations that were much less invasive than the death sentence, the administration had decided to concentrate its argument on the registration requirement, hoping to avoid a broader ruling. And it sought to delay the case, hoping for the retirement of one or more of the conservative justices. The narrow focus had led to a preliminary success in January 1937, when Judge Julian Mack of the district court in New York upheld two sections of the law in *Electric Bond and Share Company v. SEC*, ruling that companies must register and disclose their financial holdings. The SEC could then conduct administrative proceedings to limit them to a single, geographically integrated system.

The ruling was upheld on appeal to the circuit court, and Willkie was dealt a new blow when in March the Supreme Court issued a resounding decision upholding the registration requirement in the Holding Company Act. In a decision written and read by Chief Justice Hughes, the Court upheld the lower court decisions in *Bond and Share* by a 6-1 vote.

By 1941, the war in Europe created steep demands on the power sector. With entry into the war now considered nearly inevitable, a number of holding companies, led by Bond and Share and C&S, made another plea to delay further

action by the SEC to ensure that their performance in the war effort would not be hindered. “We’ve got a bear by the tail,” the vice president of C&S’s South Carolina Power subsidiary wrote to Roosevelt. “By the grace of God, we will handle the bear, but let us give him our undivided attention until he’s handled.” Edward C. Eicher, newly appointed chairman of the SEC, strongly disagreed. “The present scattered systems have ‘Balkanized’ the utility assets of this country. The resultant hodgepodge utility operations require the surgery of Section 11 [the law’s provision for the ‘death sentence’] in order that integrated utility properties may be developed in accordance with the power needs of the area served.”