TAKEOVER BIDS

HEARING

BEFORE THE

SUBCOMMITTEE ON COMMERCE AND FINANCE

OF THE

COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE

HOUSE OF REPRESENTATIVES

NINETIETH CONGRESS

SECOND SESSION

ON

H.R. 14475, S. 510

BILLS PROVIDING FOR FULL DISCLOSURE OF CORPORATE EQUITY OWNERSHIP OF SECURITIES UNDER THE SECURITIES EXCHANGE ACT OF 1934

JULY 1, 1968

Serial No. 90-44

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

U.S. GOVERNMENT PRINTING OFFICE
96-699 WASHINGTON : 1968

COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE

HARLEY O. STAGGERS, West Virginia, *Chairman*

SAMUEL N. FRIEDEL, Maryland
TORBERT H. MACDONALD, Massachusetts
JOHN JARMAN, Oklahoma
JOHN E. MOSS, California
JOHN D. DINGELL, Michigan
PAUL G. ROGERS, Florida
HORACE R. KORNEGAY, North Carolina
LIONEL VAN DEERLIN, California
J. J. PICKLE, Texas
FRED B. ROONEY, Pennsylvania
JOHN M. MURPHY, New York
DAVID E. SATTERFIELD III, Virginia
DANIEL J. RONAN, Illinois
BROCK ADAMS, Washington
RICHARD L. OTTINGER, New York
RAY BLANTON, Tennessee
W. S. (BILL) STUCKEY, JR., Georgia
PETER N. KYROS, Maine

WILLIAM L. SPRINGER, Illinois
SAMUEL L. DEVINE, Ohio
ANCHER NELSEN, Minnesota
HASTINGS KEITH, Massachusetts
GLENN CUNNINGHAM, Nebraska
JAMES T. BROYHILL, North Carolina
JAMES HARVEY, Michigan
ALBERT W. WATSON, South Carolina
TIM LEE CARTER, Kentucky
G. ROBERT WATKINS, Pennsylvania
DONALD G. BROTZMAN, Colorado
CLARENCE J. BROWN, JR., Ohio
DAN KUYKENDALL, Tennessee
JOE SKUBITZ, Kansas

W. E. WILLIAMSON, *Clerk*
KENNETH J. PAINTER, *Assistant Clerk*

Professional Staff

ANDREW STEVENSON
JAMES M. MENGER, Jr.
WILLIAM J. DIXON
ROBERT F. GUTHRIE

SUBCOMMITTEE ON COMMERCE AND FINANCE

JOHN E. MOSS, California, *Chairman*

JOHN M. MURPHY, New York
RAY BLANTON, Tennessee
W. S. (BILL) STUCKEY, JR., Georgia
HASTINGS KEITH, Massachusetts
G. ROBERT WATKINS, Pennsylvania

CONTENTS

TAKEOVER BIDS

MONDAY, JULY 1, 1968

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

The subcommittee met at 10 a.m., pursuant to notice, in room 2322, Rayburn House Office Building, Hon. John E. Moss (chairman of the subcommittee) presiding.

Mr. Moss. This morning the Subcommittee on Commerce and Finance is conducting hearings on two bills, H.R. 14475 and S. 510, which have for their purpose the amendment of the Securities and Exchange Act of 1934 to provide for additional disclosure of the ownership of the corporate equity securities, particularly as such disclosure relates to acquisition of securities as the result of tender offers and the equitable treatment of the persons tendering their stock in response to such offers.

I am certain that we all are aware from a reading of the daily papers of the tremendous number of offers to purchase stock which consistently are being made both for cash and for the exchange of other securities. The opportunities which are present for the acquisition of shares without the investor who tenders his shares as a result of the offer being adequately informed of the facts on which he can appraise the merits of the offer, or indeed the merits of retaining his interest in the corporation, are all too evident.

The legislation here being considered provides for disclosure in connection with cash tender offers for accumulating large blocks of equity securities through the requiring of filing of information with the Securities and Exchange Commission.

It is not the purpose to prevent the making of any such offers, but solely the purpose of seeing that investors adequately are informed of the relative merits of their position before and after accepting such offer so that they can make a judgment properly required.

The bill H.R. 14475, which I introduced, is substantially in the same form as S. 510 passed the Senate except for the specific inclusion of a coverage of securities issued by a closed-end investment company and for certain provisions having to do with the time of filing of the information statement with, and its review by, the SEC.

At this point in the record we shall include the legislation under consideration and such agency reports thereon that are available.

(H.R. 14475 and S. 510, and departmental reports thereon, follow:)

[H.R. 14475, 90th Cong., first sess.]

A BILL Providing for full disclosure of corporate equity ownership of securities under the Securities Exchange Act of 1934

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 12(i) of the Securities Exchange Act of 1934 is amended by striking out "sections 12, 13, 14(a), 14(c), and 16" and inserting in lieu thereof "sections 12, 13, 14(a), 14(c), 14(d), 14(f), and 16".

SEC. 2. Section 13 of the Securities Exchange Act of 1934 is amended by adding at the end thereof the following new subsections:

"(d) (1) Any person who, after acquiring directly or indirectly the beneficial ownership of any equity security of a class which is registered pursuant to section 12 of this title, or any equity security issued by a closed-end investment company registered under the Investment Company Act of 1940, is directly or indirectly the beneficial owner of more than 10 per centum of such class shall, within ten days after such acquisition, send to the issuer of the security at its principal executive office, by registered or certified mail, send to each exchange where the security is traded, and file with the Commission, a statement containing such of the following information, and such additional information, as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors—

"(A) the background and identity of all persons by whom or on whose behalf the purchases have been or are to be effected;

"(B) the source and amount of the funds or other consideration used or to be used in making the purchases, and if any part of the purchase price or proposed purchase price is represented or is to be represented by funds or other consideration borrowed or otherwise obtained for the purpose of acquiring, holding, or trading such security, a description of the transaction and the names of the parties thereto, except that where a source of funds is a loan made in the ordinary course of business by a bank, as defined in section 3(a)(6) of this title, it will be sufficient to so state;

"(C) if the purpose of the purchases or prospective purchases is to acquire control of the business of the issuer of the securities, any plans or proposals which such persons may have to liquidate such issuer, to sell its assets to or merge it with any other persons, or to make any other major change in its business or corporate structure;

"(D) the number of shares of such security which are beneficially owned, and the number of shares concerning which there is a right to acquire, directly or indirectly, by (i) such person, and (ii) by each associate of such person, giving the name and address of each such associate; and

"(E) information as to any contracts, arrangements, or understandings with any person with respect to any securities of the issuer, including but not limited to transfer of any of the securities, joint ventures, loan or option arrangements, puts or calls, guaranties of loans, guaranties against loss or guaranties of profits, division of losses or profits, or the giving or withholding of proxies, naming the persons with whom such contracts, arrangements, or understandings have been entered into, and giving the details thereof.

"(2) If any material change occurs in the facts set forth in the statements to the issuer and the exchange, and in the statement filed with the Commission, an amendment shall be transmitted to the issuer and the exchange and shall be filed with the Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

"(3) When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a 'person' for the purposes of this subsection.

"(4) In determining, for purposes of this subsection, any percentage of a class of any security, such class shall be deemed to consist of the amount of the outstanding securities of such class, exclusive of any securities of such class held by or for the account of the issuer or a subsidiary of the issuer.

"(5) The provisions of this subsection shall not apply to—

"(A) any acquisition of the beneficial ownership of a security which, together with all other acquisitions by the same person of securities of the same class during the preceding twelve months, does not exceed 2 per centum of that class;

"(B) any acquisition of an equity security by the issuer of such security;

"(C) any acquisition or proposed acquisition of a security which the Commission, by rules or regulations or by order, shall exempt from the provisions of this subsection as not entered into for the purpose of, and not having the effect of, changing or influencing the control of the issuer or otherwise as not comprehended within the purposes of this subsection.

"(e)(1) It shall be unlawful for an issuer, to purchase any equity security which it has issued 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 or in order to prevent such acts and practices as are fraudulent, deceptive, or manipulative. Such rules and regulations may require such issuer to provide holders of equity securities of such class with such information relating to the reasons for such purchase, the source of funds, the number of shares to be purchased, the price to be paid for such securities, the method of purchase, and such additional information, as the Commission deems necessary or appropriate in the public interest or for the protection of investors, or which the Commission deems to be material to a determination whether such security should be sold.

"(2) For the purpose of this subsection, a purchase by or for the issuer, or any person controlling, controlled by, or under common control with the issuer, or any bonus, profit sharing, pension, retirement, thrift, savings, incentive, stock purchase, or similar plan of the issuer or any such person shall be deemed to be a purchase by the issuer."

SEC. 3. Section 14 of the Securities Exchange Act of 1934 is amended by adding at the end thereof the following new subsections:

"(d)(1) It shall be unlawful for any person, directly or indirectly, by use of the mails or by any means or instrumentality of interstate commerce or of any facility of a national securities exchange or otherwise, to make a tender offer for, or a request or invitation for tenders of, any class of any equity security which is registered pursuant to section 12 of this title, or any equity security issued by a closed-end investment company registered under the Investment Company Act of 1940, if after consummation thereof, such person would, directly or indirectly, be the beneficial owner of more than 10 per centum of such class, unless five days prior to the date copies of such material are first published or sent or given to security holders, such person has filed with the Commission a statement containing such of the information specified in section 13(d) of this title, and such additional information as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors. All requests or invitations for tenders or advertisements making a tender offer or requesting or inviting tenders of such a security shall be filed as a part of such statement and shall contain such of the information contained in such statement as the Commission may by rules and regulations prescribe. Preliminary copies of any additional material soliciting or requesting such tender offers subsequent to the initial solicitation or request shall contain such information as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors, and shall be filed with the Commission at least two days prior to the date copies of such material are first published or sent or given to security holders. Copies of all statements, in the form in which such material is furnished to security holders and the Commission, shall be sent to the issuer not later than the date such material is first published or sent or given to any security holders. All copies of preliminary statements filed with the Commission hereunder shall be for the information of the Commission only, except that such statements may be disclosed to any appropriate department or agency of Government and the Commission may make such inquiries or investigation in regard to such statements as may be necessary for an adequate review thereof by the Commission. Definitive copies of all statements, in the form in which such material is furnished to security holders, shall be filed with, or mailed for filing to, the Commission and shall be sent to the issuer not later than the date such material is first published or sent or given to any security holders. The time periods contained in this subsection may be shortened as the Commission may direct.

"(2) When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a 'person' for purposes of this subsection.

"(3) In determining, for purposes of this subsection, any percentage of a class of any security, such class shall be deemed to consist of the amount of the outstanding securities of such class, exclusive of any securities of such class held by or for the account of the issuer or a subsidiary of the issuer.

"(4) Any solicitation or recommendation to the holders of such a security to accept or reject a tender offer or request or invitation for tenders shall be made in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

"(5) Securities deposited pursuant to a tender offer or request or invitation for tenders may be withdrawn by or on behalf of the depositor at any time until the expiration of seven days after the time definitive copies of the offer or request or invitation are first published or sent or given to security holders or at any time thereafter until taken up by the offeror, subject to such terms and conditions as the Commission may prescribe by rules and regulations as necessary or appropriate in the public interest or for the protection of investors.

"(6) Where any person makes a tender offer or request or invitation for tender for less than all the outstanding equity securities of a class, and where a greater number of securities is deposited pursuant thereto than such person is bound or willing to take up and pay for, the securities taken up shall be taken up as nearly as may be pro rata, disregarding fractions, according to the number of securities deposited by each depositor, except as the Commission may otherwise prescribe by rules and regulations as necessary or appropriate in the public interest or for the protection of investors.

"(7) Where any person varies the terms of a tender offer or request or invitation for tenders before the expiration thereof by increasing the consideration offered to holders of such securities, such person shall pay the increased consideration to each security holder whose securities are taken up and paid for pursuant to the tender offer or request or invitation for tenders whether or not such securities have been taken up by such person before the variation of the tender offer or request or invitation.

"(8) The provisions of this subsection shall not apply to any offer for, or request or invitation for tenders of, any security—

"(A) if the acquisition of such security, together with all other acquisitions by the same person of securities of the same class during the preceding twelve months, would not exceed 2 per centum of that class;

"(B) by the issuer of such security; or

"(C) which the commission, by rules or regulations or by order, shall exempt from the provisions of this subsection as not entered into for the purpose of, and not having the effect of, changing or influencing the control of the issuer or otherwise as not comprehended within the purposes of this subsection.

"(e) It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation.

"(f) If, pursuant to any arrangement or understanding with the person or persons acquiring securities in a transaction subject to subsection (d) of this section or subsection (d) of section 13 of this title, any persons are to be elected or designated as directors of the issuer, otherwise than at a meeting of security holders, and the persons so elected or designated will constitute a majority of the directors of the issuer, then, prior to the time any such person takes office as a director, and in accordance with rules and regulations prescribed by the Commission, the issuer shall file with the Commission, and transmit to all holders of record of securities of the issuer who would be entitled to vote at a meeting for election of directors, information substantially equivalent to the information which would be required by subsection (a) or (c) of this section to be transmitted if such person or persons were nominees for election as directors at a meeting of such security holders."

[S. 510, 90th Cong., first sess.]

AN ACT Providing for full disclosure of corporate equity ownership of securities under the Securities Exchange Act of 1934

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 12(i) of the Securities Exchange Act of 1934 is amended by striking out "sections 12, 13, 14(a), 14(c), and 16" and inserting in lieu thereof "sections 12, 13, 14(a), 14(c), 14(d), 14(f), and 16".

SEC. 2. Section 13 of the Securities Exchange Act of 1934 is amended by adding at the end thereof the following new subsections:

"(d)(1) Any person who, after acquiring directly or indirectly the beneficial ownership of any equity security of a class which is registered pursuant to section 12 of this title, is directly or indirectly the beneficial owner of more than 10 per centum of such class shall, within ten days after such acquisition, send to the issuer of the security at its principal executive office, by registered or certified mail, send to each exchange where the security is traded, and file with the Commission, a statement containing such of the following information, and such additional information, as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors—

"(A) the background and identity of all persons by whom or on whose behalf the purchasers have been or are to be effected;

"(B) the source and amount of the funds or other consideration used or to be used in making the purchases, and if any part of the purchase price or proposed purchase price is represented or is to be represented by funds or other consideration borrowed or otherwise obtained for the purpose of acquiring, holding, or trading such security, a description of the transaction and the names of the parties thereto, except that where a source of funds is a loan made in the ordinary course of business by a bank, as defined in section 3(a)(6) of this title, it will be sufficient to so state;

"(C) if the purpose of the purchases or prospective purchases is to acquire control of the business of the issuer of the securities, any plans or proposals which such persons may have to liquidate such issuer, to sell its assets to or merge it with any other persons, or to make any other major change in its business or corporate structure;

"(D) the number of shares of such security which are beneficially owned, and the number of shares concerning which there is a right to acquire, directly or indirectly, by (i) such person, and (ii) by each associate of such person, giving the name and address of each such associate; and

"(E) information as to any contracts, arrangements, or understandings with any person with respect to any securities of the issuer, including but not limited to transfer of any of the securities, joint ventures, loan or option arrangements, puts or calls, guaranties of loans, guaranties against loss or guaranties of profits, division of losses or profits, or the giving or withholding of proxies, naming the persons with whom such contracts, arrangements, or understandings have been entered into, and giving the details thereof.

"(2) If any material change occurs in the facts set forth in the statements to the issuer and the exchange, and in the statement filed with the Commission, an amendment shall be transmitted to the issuer and the exchange and shall be filed with the Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

"(3) When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a 'person' for the purposes of this subsection.

"(4) In determining, for purposes of this subsection, any percentage of a class of any security, such class shall be deemed to consist of the amount of the outstanding securities of such class, exclusive of any securities of such class held by or for the account of the issuer or a subsidiary of the issuer.

"(5) The provisions of this subsection shall not apply to—

"(A) any acquisition or offer to acquire securities made or proposed to be made by means of a registration statement under the Securities Act of 1933;

"(B) any acquisition of the beneficial ownership of a security which, together with all other acquisitions by the same person of securities of the same class during the preceding twelve months, does not exceed 2 per centum of that class;

"(C) any acquisition of an equity security by the issuer of such security;

"(D) any acquisition or proposed acquisition of a security which the Commission, by rules or regulations or by order, shall exempt from the provisions of this subsection as not entered into for the purpose of, and not having the effect of, changing or influencing the control of the issuer or otherwise as not comprehended within the purposes of this subsection.

"(e)(1) It shall be unlawful for an issuer, to purchase any equity security which it has issued 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 or in order to prevent such acts and practices as are fraudulent, deceptive, or manipulative. Such rules and regulations may require such issuer to provide holders of equity securities of such class with such information relating to the reasons for such purchase, the source of funds, the number of shares to be purchased, the price to be paid for such securities, the method of purchase, and such additional information, as the Commission deems necessary or appropriate in the public interest or for the protection of investors, or which the Commission deems to be material to a determination whether such security should be sold.

"(2) For the purpose of this subsection, a purchase by or for the issuer, or any person controlling, controlled by, or under common control with the issuer, or any bonus, profit sharing, pension, retirement, thrift, savings, incentive, stock purchase, or similar plan of the issuer or any such person shall be deemed to be a purchase by the issuer."

SEC. 3. Section 14 of the Securities Exchange Act of 1934 is amended by adding at the end thereof the following new subsections:

"(d)(1) It shall be unlawful for any person, directly or indirectly, by use of the mails or by any means or instrumentality of interstate commerce or of any facility of a national securities exchange or otherwise, to make a tender offer for, or a request or invitation for tenders of, any class of any equity security which is registered pursuant to section 12 of this title, if, after consummation thereof, such person would, directly or indirectly, be the beneficial owner of more than 10 per centum of such class, unless at the time copies of the offer or request or invitation are first published or sent or given to security holders such person has filed with the Commission a statement containing such of the information specified in section 13(d) of this title, and such additional information as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors. All requests or invitations for tenders or advertisements making a tender offer or requesting or inviting tenders of such a security shall be filed as a part of such statement and shall contain such of the information contained in such statement as the Commission may by rules and regulations prescribe. Copies of any additional material soliciting or requesting such tender offers subsequent to the initial solicitation or request shall contain such information as the Commission may by rules and regulations prescribe as necessary or appropriate in the public interest or for the protection of investors, and shall be filed with the Commission not later than the time copies of such material are first published or sent or given to security holders. Copies of all statements, in the form in which such material is furnished to security holders and the Commission, shall be sent to the issuer not later than the date such material is first published or sent or given to any security holders.

"(2) When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a 'person' for purposes of this subsection.

"(3) In determining, for purposes of this subsection, any percentage of a class of any security, such class shall be deemed to consist of the amount of the outstanding securities of such class, exclusive of any securities of such class held by or for the account of the issuer or a subsidiary of the issuer.

"(4) Any solicitation or recommendation to the holders of such a security to accept or reject a tender offer or request or invitation for tenders shall be made in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

"(5) Securities deposited pursuant to a tender offer or request or invitation for tenders may be withdrawn by or on behalf of the depositor at any time until the expiration of seven days after the time definitive copies of the offer or

invitation are first published or sent or given to security holders, and at any time after sixty days from the date of the original tender offer or request or invitation, except as the Commission may otherwise prescribe by rules, regulations, or order as necessary or appropriate in the public interest or for the protection of investors.

"(6) Where any person makes a tender offer, or request or invitation for tenders, for less than all the outstanding equity securities of a class, and where a greater number of securities is deposited pursuant thereto within ten days after copies of the offer or request or invitation are first published or sent or given to security holders than such person is bound or willing to take up and pay for, the securities taken up shall be taken up as nearly as may be pro rata, disregarding fractions, according to the number of securities deposited by each depositor. The provisions of this subsection shall also apply to securities deposited within ten days after notice of an increase in the consideration offered to security holders, as described in paragraph (7), is first published or sent or given to security holders.

"(7) Where any person varies the terms of a tender offer or request or invitation for tenders before the expiration thereof by increasing the consideration offered to holders of such securities, such person shall pay the increased consideration to each security holder whose securities are taken up and paid for pursuant to the tender offer or request or invitation for tenders whether or not such securities have been taken up by such person before the variation of the tender offer or request or invitation.

"(8) The provisions of this subsection shall not apply to any offer for, or request or invitation for tenders of, any security—

"(A) proposed to be made by means of a registration statement under the Securities Act of 1933;

"(B) if the acquisition of such security, together with all other acquisitions by the same person of securities of the same class during the preceding twelve months, would not exceed 2 per centum of that class;

"(C) by the issuer of such security; or

"(D) which the Commission, by rules or regulations or by order, shall exempt from the provisions of this subsection as not entered into for the purpose of, and not having the effect of, changing or influencing the control of the issuer or otherwise as not comprehended within the purpose of this subsection.

"(e) It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulatve acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation.

"(f) If, pursuant to any arrangement or understanding with the person or persons acquiring securities in a transaction subject to subsection (d) of this section or subsection (d) of section 13 of this title, any persons are to be elected or designated as directors of the issuer, otherwise than at a meeting of security holders, and the persons so elected or designated will constitute a majority of the directors of the issuer, then, prior to the time any such person takes office as a director, and in accordance with rules and regulations prescribed by the Commission, the issuer shall file with the Commission, and transmit to all holders of record of securities of the issuer who would be entitled to vote at a meeting for election of directors, information substantially equivalent to the information which would be required by subsection (a) or (c) of this section to be transmitted if such person or persons were nominees for election as directors at a meeting of such security holders."

Passed the Senate August 30 (legislative day, August 29), 1967.

Attest: FRANCIS R. VALEO, *Secretary.*

SECURITIES AND EXCHANGE COMMISSION,
Washington, D.C., October 16, 1967.

Hon. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your letter of September 11, 1967 requesting our comments on S. 510, as well as your earlier letter requesting our comments on H.R. 12210.

S. 510, as passed by the Senate, reflects many changes made by the Senate Banking and Currency Committee in the bill originally introduced, including a number of changes suggested by this Commission. While the Senate Committee did not adopt all of the suggestions we made, we believe the bill passed by the Senate is a constructive approach to a problem which requires Congressional attention.

On the other hand, we would like to have the opportunity to submit for the consideration of your Committee a statement in support of the recommendations which we made to the Senate Committee which were not embodied in the bill enacted by the Senate. We believe that these further changes would materially improve an already good bill. In addition, we have some further changes to suggest to close a gap in the coverage of the bill which was brought to our attention recently. We are now preparing a statement incorporating these recommendations which we hope to submit to you shortly or at such time as public hearings on the bill are held by your Committee.

In regard to H.R. 12210, we note that it is substantially identical to S. 510 as originally introduced. The statements which we submitted to the Senate Committee set forth in detail our difficulties with that measure in its original form. We therefore believe that S. 510, as passed by the Senate, or any comparable legislation that may be introduced in the House, would be a more useful starting point for your Committee's deliberations.

Sincerely,

MANUEL F. COHEN, *Chairman.*

BOARD OF GOVERNORS,
FEDERAL RESERVE SYSTEM,
Washington, D.C., October 31, 1967.

Hon. HARLEY O. STAGGERS,
Chairman, House Interstate and Foreign Commerce Committee,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: S. 510, now pending before your Committee, would provide for disclosure of ownership of corporate equity securities under the Securities Exchange Act of 1934. The Board of Governors is in accord with the purposes of this bill, particularly as it would require disclosures relating to acquisition of substantial interests in banks, and equitable treatment of persons tendering bank stock in response to purchase offers. Bank stock could become less attractive as an investment, with the result that banks might find it more difficult to raise needed capital, if the interests of minority shareholders are not fully protected in connection with negotiations to merge or acquire banks. The proposed bill would take a noteworthy step toward providing minority shareholders with the opportunity for prior notice, and the equal opportunity to dispose of their shares, which the Board believes necessary both for equitable treatment and good business practice.

However, the Board notes that in its present form, the bill virtually exempts financing arrangements from disclosure where funds are provided by means of a loan made in the ordinary course of business by a bank. The Board is not aware of any reason why the same disclosure requirements should not apply to banks as to other lenders. In addition, as explained below, information as to bank financing of tender offers would materially assist the Board in carrying out its duties under the 1934 Act. For this reason, the Board would recommend deletion of the provision permitting non-disclosure of information relating to bank financing of tender offers. However, if your Committee believes, for any reason, that the name of the bank making such a loan should not be disclosed, the Board would urge that a provision be substituted that would accord confidential treatment to the identity of the bank lender.

The sharp recent increase in the number of tender offers has highlighted certain problems under the Board's Regulation U (Loans by Banks for the Purpose

of Purchasing or Carrying Registered Stocks), issued pursuant to section 7(d) of the 1934 Act, the statute which S. 510 would amend. A significant amount of credit may flow into the securities markets through this channel, which has escaped margin regulation for technical reasons. Such credit could be brought within the scope of margin regulation under existing law, but in order to reach an informed conclusion in this area it would be helpful if the Board knew a good deal more than it does at present about the amount and character of such credit.

Such information could perhaps be collected directly from banks, but this would impose an additional burden, particularly since reporting banks would first have to determine what loans involved "tender offers". The present bill places the responsibility for reporting on the borrower, who is in the best position to know the purpose of a loan. Thus, there would be less diffusion of responsibility and considerable economy of effort if the Board could be furnished with the information it needs under the program already envisaged by S. 510. At the same time, the interests of offerees would better be served if they had available to them information on the terms of bank financing for tender offers. What collateral was to be provided, how long the loan was to remain outstanding, and how it was to be repaid, are all matters that could affect the decision whether or not to accept a tender offer, regardless of the source of the loan.

An additional benefit would be realized in the area of supervision of the Board's Regulation U. Because such bank financing is typically short-term, the purpose of the loan has usually been accomplished by the time the situation comes to the attention of the supervisory authorities, and the loan has been, or is about to be, paid off. It would be helpful in ensuring compliance with the regulation if advice were secured that a particular bank was financing an offer at the time when the offer was first made.

Enclosure A herewith shows section 13(d)(1)(B) of the Act, as it would read with the exemption deleted, and Enclosure B shows the same section as it would read if non-disclosure of the lending bank's identity was substituted for the present complete exemption.

Sincerely,

J. L. ROBERTSON,
Vice Chairman.

ENCLOSURE A

Part of Section 2 of S. 510 (a bill providing for full disclosure of corporate equity ownership under the Securities Exchange Act of 1934), amending section 13 of the Securities Exchange Act of 1934, marked to indicate changes that would be made by an amendment proposed by the Federal Reserve System to omit the exemption for disclosure as to bank financing of tender offers (proposed deletion enclosed in black brackets):

"(d)(1) . . .

"(B) the source and amount of the funds or other consideration used or to be used in making the purchase, and if any part of the purchase price of proposed purchase price is represented or is to be represented by funds or other consideration borrowed or otherwise obtained for the purpose of acquiring, holding, or trading such security, a description of the transaction and the names of the parties thereto[,]; [except that where a source of funds is a loan made in the ordinary course of business by a bank, as defined in section 3(a)(6) of this title, it will be sufficient so to state;]"

ENCLOSURE B

Part of Section 2 of S. 510 (a bill providing for full disclosure of corporate equity ownership under the Securities Exchange Act of 1934), amending section 13 of the Securities Exchange Act of 1934, marked to indicate changes that would be made by an amendment proposed by the Federal Reserve System to provide that the exemption for disclosure as to bank financing to tender offers be omitted and in its place there be substituted a requirement that the name of the bank financing such an offer be kept confidential:

"(d)(1) . . .

"(B) the source and amount of the funds or other consideration used or to be used in making the purchase, and if any part of the purchase price or proposed purchase price is represented or is to be represented by funds or other consideration borrowed or otherwise obtained for the purpose of acquiring, holding, or trading such security, a description of the transaction

and the names of the parties thereto, except that where a source of funds is a loan made in the ordinary course of business by a bank, as defined by section 3(a)(6) of this title, it will be sufficient so to state; *if the person filing such statement so requests, the name of the bank shall not be made available to the public;*"

Mr. Moss. Our first witness this morning is the Honorable Manuel F. Cohen, Chairman of the Securities and Exchange Commission.

Mr. Cohen.

STATEMENT OF HON. MANUEL F. COHEN, CHAIRMAN, SECURITIES AND EXCHANGE COMMISSION; ACCOMPANIED BY PHILIP A. LOOMIS, JR., GENERAL COUNSEL

Mr. COHEN. Good morning.

Mr. Moss. Good morning.

For the record will you identify the gentleman accompanying you.

Mr. COHEN. Gentlemen, I am accompanied by Mr. Philip A. Loomis, Jr., General Counsel of the Commission. At the outset I would like to express my appreciation for the opportunity to appear before you with regard to this proposed amendment to the 1934 act which in our opinion is very important and fills a gap in the existing scheme of investor protection, a gap which incidentally has been dealt with in other countries of the Western World for some time. I should also add, in particular, the most recent legislative action in this area is that which occurred in Canada. As you indicated, Mr. Chairman, I am here to testify on H.R. 14475 and S. 510, bills to amend the Securties Exchange Act of 1934. To repeat, the purpose of this legislation is to fill a gap in the existing scheme of investor protection with respect to the increasingly important area of so-called "takeover bids." These involve situations where someone makes a general offer to purchase the shares of a publicly owned corporation from the shareholders, usually with the objective of obtaining control and often as a prelude to a merger. I have a detailed statement which explains the reasons for this legislation, the need for it, and the manner in which it deals with the matter. In order to save the time of this committee I would like to introduce this statement for the record and to summarize briefly certain pertinent considerations, particularly recent development. With the permission of the chairman I will hand the full statement to the reporter for inclusion in the record.

Mr. Moss. Without objection, the full statement will be received for inclusion in the record at this point and you may proceed to summarize it.

(Mr. Cohen's prepared statement follows:)

STATEMENT OF HON. MANUEL F. COHEN, CHAIRMAN, SECURITIES AND EXCHANGE COMMISSION

Mr. Chairman and Members of the Committee, I am Manual F. Cohen, Chairman of the Securities and Exchange Commission. I am here at your invitation to testify on H.R. 14475 and S. 510, bills to amend the Securities Exchange Act of 1934.

The bills are designed solely to fill a gap in the provisions of the Securities Exchange Act to cover planned acquisitions of large blocks of securities of publicly-held companies, where control of the company may be at stake. It is not intended to encourage or to discourage such activity or to provide management or any other group with special privileges over any other. This has become an

area of increasing significance in recent years and is to be distinguished from planned offerings of blocks of securities—dealt with primarily by the Securities Act of 1933, as well as ordinary trading of securities in the secondary markets which is the primary focus of existing provisions of the Securities Exchange Act.

The bills have a much closer relationship to existing provisons of the Exchange Act regulating solicitation of proxies, since acquisitions of blocks of voting securities are typically alternatives to proxy solicitations, as methods of capturing or preserving control. In either case there is involved a form of industrial warfare in which the stakes are high, and two or more groups are attempting to manipulate the public security holder to their own advantage. A proxy fight, as such, is an attempt to ruin the public security holder's vote, leaving him in a position to share with other security holders the advantages or disadvantages of the outcome of the struggle for control. The special problems of the block acquisition result from attempts to cause, or resist, a substantial shift of ownership away from existing security holders.

The bills before you deal with stock acquisitions in three specific contexts—first, the acquisition by means of a cash tender offer of more than ten percent of any class of stock of a publicly-held company; second, other acquisitions by any person or group of more than ten percent of any class of stock of a publicly-held company; and third, the repurchase by a corporation of its own outstanding shares. Each of these situations presents its own unique problems.

The Commission agrees that there is need for further protection of the public security holders in this area. We do not wish to imply, however, that block acquisitions should be encouraged or discouraged, or that the Commission should have power or responsibility to pass on the merits of a particular acquisition or proposal. As in most other areas entrusted to it, the Commission's reponsibility should be limited to requiring appropriate disclosures, to guarding against deceptive and unfair devices designed to coerce or prevent action, and it should be provided with adequate tools to deal effectively with the various techniques that have been developed, and are continuing to be devised, to seek or to prevent takeover bids and other matters dealt with in the bill. Finally, adequate authority must be accorded to deal with the violations of these precepts—all designed to give the investor the fairest possible opportunity to make his own investment decisions.

TENDER OFFERS

I turn now to tender offers. Statistics recently published show that the aggregate of cash tender offers has grown from less than $200 million in 1960 to almost a billion dollars in 1965, surpassing stock-for-stock tender offers, which aggregated about half a billion dollars in each of those years.

In this area the bills are designed first, to provide those who receive a tender offer with information adequate to an informed decision whether or not to accept; and second, to eliminate conditions surrounding the offer which discriminate unfairly among those who may desire to tender their shares or unreasonably restrict their freedom of action with respect to deposited shares at a time when there is no assurance that the tender of their shares will be accepted.

A tender offer is quite different from the ordinary market transaction with which the average investor is familiar. In so far as it is an offer at all it is subject to complex and sometimes deceptive conditions. Rather it is an invitation to the public security holder who "tenders" his security to give the other party an option—to be exercised only if certain minimum shares are tendered within a specified time and perhaps specifying a maximum which the original "offeror" is prepared to take—but giving him discretion to accept a lesser or larger amount or to extend the time limits. Tendering in response to such an offer involves deposit of the public security holder's shares or obtaining a guarantee from a stock exchange member or other financially responsible person that they will be deposited. Some conditions of this character may well be a practical necessity. Otherwise there would be no inducement to the originator of the tender offer to pay above the current market price.

But what has developed is a one-sided document. An early response may prevent the unwary investor from taking advantage of a later and better offier—or put him in the position of having given an option on his shares for a substantial period of time without any assurance that the deal will go through, or, if it does, that there will be no unfair discrimination in the acceptance of shares. Sometimes the offeror promises acceptance on a first-come first-served basis, which has the effect of increasing the pressure for a hasty deposit—so that those who respond do not have a chance to take advantage of later and better offers,

either from the same or a different source. Any tender proposal requires a security holder to make an investment decision and to do so under pressure. Typically, the price proposed is somewhat above the current market, and announced under conditions designed to leave the impression that immediate response is necessary. Typically, there is also no disclosure of the motives or plans of the person making the offer, or of the consequence to the particular investor of failing to tender his shares if a substantial percentage of the other security holders do so. Nor is there any explanation offered of any special pressures generated in the security markets as a result of the tender offer.

Information about a potential change in control can be particularly essential to an informed decision. A change in control brings with it the possibility of different operating results and different investment results, or perhaps the possibiilty of realizing on a company's liquidation value. This may be either good, or bad, depending on the facts and circumstances involved. But investors and their advisers cannot reach informed conclusions on the possible effects of a change in control until facts are available to them.

It is argued by some that the basic factor which influence shareholders to accept a tender offer is the adequacy of the price. But, I might ask, how can an investor evaluate the adequacy of the price if he cannot assess the possible impact of a change in control? Certainly without such information he cannot judge its adequacy by the current or recent market price. That price presumably reflects the assumption that the company's present business control and management will continue. If that assumption is changed, is it not likely that the market price might change? An example will show why. Assume that a company's stock sells for $5 per share—its going concern value as assessed by investors. Its earnings are poor; its prospects dim; its management uninspired. Is a cash tender offer of $6 per share adequate? Or do we need more information? Suppose a person believes that with control he can liquidate the company and realize $15 per share, or maybe more. Certainly the company's shareholders would want to know about liquidation plans. Indeed, it is the plan to liquidate which makes the bidder willing to pay more than $5 per share. Whether or not the company's liquidation value is generally known is not important, for without someone to carry out the liquidation, this value is unobtainable. If the company's shareholders, at the time of the tender offer, know of the plan to liquidate. would they consider $6 per share adequate?

Where competing offers are made, at different prices, stockholders may have even more difficulty in making any sort of rational decision, and the confusion that develops in these situations can have a very serious adverse effect on public confidence in the integrity and openness of the securities markets. In one recent example, a small manufacturing company was the subject of a takeover bid by another company formed specifically for the purpose of making the tender offer by a group of persons whose identity was not disclosed. Two other companies made competing tender offers at the same time, a fourth corporation made an exchange offer and a fifth made an offer of merger. In these circumstances the shareholders were in no position to judge the significance of these competing offers or to compare the impact on the company of the cash offers with that of the exchange offer or the merger proposal. It is important to note that under existing law the proposed technique in at least two of the offers could have produced adequate information, but it would not have been possible to obtain comparable information with respect to the other offers.

One important potential protection to security holders is an opportunity for management to furnish any information at its disposal pertinent to the merits of the offer before the security holder responds to it. At the same time protection is needed against any management efforts designed to resist bids when the information furnished may be given in the context in which the desire to obtain existing emoluments may make difficult impartial and complete disclosure of relevant facts.

It would be naive to assume that tender offers are not, at times, opposed by managements motivated by their own interests in staving off a change in control. It would, however, be as much an unfair overstatement to suggest that management, in opposing bids, is motivated solely by self-interest as to suggest that takeover bids are always improper or dangerous to the interests of investors. It may be of interest to note that attempts to discourage shareholders from accepting tender offers take a variety of forms. Recently, in order to block a takeover bid, the management of one company hurriedly called a stockholders' meeting to obtain authorization to make a competing offer to buy its own shares

at a higher price. In another situation, after a tender offer was announced, management proposed a stock split and shareholders were led to believe, contrary to fact, that approval of the stock split was an alternative to accepting the tender offer. Frequently the takeover bidders, and management opposing a tender offer, resort to extensive newspaper advertisements, or other forms of communication, not subject to the explicit disclosure requirements of the securities laws, with the result that shareholders are inundated by a rash of charges and countercharges not easily, or in reasonable time, susceptible to control under the antifraud provisions of the statutes. The plain fact is that shareholders are not in a position to make informed decisions concerning the terms of the tender offer.

To meet this problem, the bills would require a person making a tender offer for more than 10 per cent of a company's securities to file a statement with the Commission disclosing his identity and background, his shareholdings in the company, the source and amount of the funds to be used and any loans he has made to obtain the funds, any plans he may have for major changes in the company's business, and any arrangements he may have with any other person with respect to the company's securities.

Consistent with the existing pattern where the takeover is subject to the proxy rules or registration provisions of the securities acts, the Commission would be given rule-making authority to require additional information in the statement, to prescribe the minimum information required in advertisements and to develop appropriate rules with respect to the techniques employed to make the statutory scheme effective. Thus, these provisions would assure that material information was effectively brought to the attention of shareholders and, in cases of opposition or competing tenders, would prevent certain types of high-pressure appeals and procedures possible when no restraints, other than the antifraud provisions of the securities laws, relate to these activities.

The procedures provided by the bills in the case of contested tender offers are analogous to those now followed when contending factions solicit proxies under the Commission's proxy rules. These rules, which were developed entirely from a simple delegation to the Commission of rule-making authority and responsibility, are under continuous scrutiny and review in the light of experience and are generally accepted as having been successful in providing adequate and accurate information to shareholders in contests for control of their companies. While there are obvious differences between tender offers and proxy contests, there is in both situations the common element of concern with the future management and control of the company. Adequate material information is equally important to a shareholder who is faced with a decision whether to sell his securities or retain his investment in the company. We believe that the bills provide a suitable framework for providing that information without unduly hindering tender offers which are or may be beneficial to the stockholders.

The second objective of these bills is to assure fair treatment of all shareholders who decide to accept a tender offer. Often takeover bids are made under circumstances which place undue pressure on shareholders to act hastily and to accept before management or any other group has an opportunity to present opposing arguments or competing offers. On occasion because of management's advice to its shareholders that their stock was worth more than the amount offered or as a result of competing offers, tender prices have been substantially increased.

In one instance, shares that had been deposited in response to a cash offer for $36 a share on a first-come first-served basis were promptly taken up by the offeror, even after a second bid at $50 a share had been made by another offeror. Furthermore, under existing circumstances, shareholders are not assured that all, or any, of their shares will be taken up if tendered.

The Senate bill contains three substantive provisions designed to assure that all stockholders who tender their shares are treated fairly. First, it provides that deposited securities may be withdrawn at any time during the first seven days after the date of the original offer, or at any time after 60 days from the date of the original offer, except as the Commission may otherwise prescribe. Second, it provides that where a greater number of shares are tendered than the offerer is willing to accept, the shares accepted must be taken pro rata from each stockholder in proportion to the securities deposited during the first ten days. Third, when the terms of an offer are changed to raise the price, the higher

price must be paid to all stockholders, including those who tendered before the price was increased.

While these provisions could have a salutary effect, we prefer the provisions of H.R. 14475 which are described in my summary statement.

During the hearings before the Senate Committee, there was discussion of the practice known as "short tendering." Where a tender offer is made with a provision for acceptance of tendered shares on a pro-rata basis, some persons tender more shares than they own in order to gain an advantage over ordinary investors. Thus, if it is estimated that only half of the tendered shares will actually be purchased by the offeror, a short tenderor will tender twice as many shares as he owns and thus sell all of his shares, while ordinary investors sell only half. As a practical matter, short tendering is largely confined to member firms of the stock exchange, since it is usually provided that stock certificates must accompany a tender unless a member firm or a bank guarantees that they will be delivered upon acceptance. In its report, the Senate Committee suggested that the Commission could deal with this practice under the fraud provisions of the Securities Exchange Act, and the Commission has done so by adopting Rule 10b–4, which, in effect, prohibits short tendering.

ACQUISITIONS OTHER THAN TENDER OFFERS

Not all acquisitions of substantial blocks of securities are made by means of tender offers. A corporation or individual—or a group of corporations or individuals—can acquire a substantial block of stock of a company through a program of purchases in the open market, or through privately-negotiated purchases from substantial stockholders, and thus achieve the power to influence the management and control of the corporation, without the other stockholders even becoming aware of this development.

Section 16(a) of the Exchange Act, which requires ownership reports from any holder of ten per cent of the equity securities of a company, does not fully meet the need of stockholders for information in this kind of situation. It requires only information concerning number of shares and type of ownership and does not give the public stockholders adequate information about the arrangements surrounding the acquisition or the purchaser's intentions with respect to the company.

The bills would require any person or group of persons, which acquires more than ten per cent of any class of equity security of a publicly-held company, to file with the Commission, and to send to the issuer and to any exchange on which the security is listed, within seven days after the acquisition, a statement containing certain specified information. This information would be similar to that required of a person proposing to make a tender offer and would include the background and identity of the purchaser, the source of its funds, the number of shares acquired, any contracts or arrangements with respect to the securities of the company, and any plans of the purchaser to make major changes in the company's business or corporate structure.

It must be emphasized again, that in establishing requirements which will make this important information available to stockholders, we must be careful not to tip the scales to favor either incumbent managements or those who would seek to oust them. We believe that the provisions of the bills reflect on appropriate balance among competing interests which, at the same time, will fulfill the need of public stockholders to be fully informed about the control and potential control of the company in which they have invested.

There is another problem in this area which is dealt with by the bills. Under Section 14 of the Act, when directors of a registered company are to be elected at a meeting of stockholders, we require that the stockholders be furnished with full information about the nominees, whether or not proxies are solicited and whether or not the nominees have previously been elected by the stockholders. However, when a "controlling" block of stock in one of these companies is sold, and the contract of sale provides (as it often does) that the seller will procure the resignations of all or a majority of the existing directors and their replacement by designees of the buyer, the other stockholders not only do not get a chance to vote on the new directors, they normally do not even hear about the changes until they have actually taken place.

This problem is dealt with in the bills which add a new Section 14(e) to the Act. Under this provision, if a majority of the directors of a company are to be replaced without a meeting of stockholders, pursuant to an arrangement with a person who is acquiring more than ten per cent of the stock of the company, then,

before the new directors take office, the issuer must file with the Commission and furnish to its stockholders information substantially equivalent to that which would be required if the new directors were being elected at a meeting of the stockholders.

CORPORATE REPURCHASES OF THEIR OWN SHARES

Another phenomenon of increasing importance is the growing tendency of corporations to repurchase their own securities. According to a recent study, corporations listed on the New York Stock Exchange spent more than $1,300,000,000 during 1963 to purchase over 26,600,000 of their own shares. The amount expended for this purpose exceeded the amount of capital raised by these companies by selling new shares. An indication of the extent of the increase in the volume of corporate purchases of their own shares may be obtained by comparing the data for 1963 with the data for 1954, when the number of shares purchased by New York Stock Exchange listed companies was 5,800,000.

These purchases may be made for perfectly legitimate corporate purposes. A corporation may simply wish to reduce its outstanding capital stock, particularly when it has sold operating divisions or subsidiaries and has excess cash available. If the market price of its shares is less than book value or otherwise at a depressed level, the company's shares may be viewed by management as a good investment. Or the company may wish to have shares available for options, acquisitions or other purposes without increasing the total number of shares outstanding.

However, purchases by a corporation of its own shares can be used to affect the control of the corporation. The management may cause the corporation to repurchase shares for the purpose of preserving or improving the management's control position, or to counteract a tender offer or other takeover bid.

Whatever the purpose, such purchases may also have a significant effect on the market price of the shares. We have recently dealt, under existing antifraud provisions of the Exchange Act, with situations in which repurchases of shares were timed to increase the market price for such shares, while the company was negotiating to acquire other companies in exchange for such stock. In the case of one company, a repurchase program was actually used on a number of occasions to reduce the number of shares deliverable under existing contracts for acquisition of other companies.

But even where the management has no improper motive in repurchasing securities, substantial repurchase programs will inevitably affect market performance and price levels. That is why we believe that the rule-making authority contained in the bills would be a valuable adjunct to our authority under the existing antifraud provisions of the Act.

The provisions of the bills would make it unlawful for an issuer to purchase its own securities in contravention of rules or regulations which the Commission adopts because they are necessary or appropriate in the public interest, or to protect investors, irrespective of the question whether, or our ability to prove that, such activity is or may be fraudulent, deceptive or manipulative. The language, for this reason, is broader in its scope than presently applicable provisions of the Exchange Act.

The bills deal not only with purchases by the issuer itself but apply also to purchases by a parent or subsidiary of the issuer, or by a welfare or pension fund subject to the influence of the issuer's management. We have found that these give rise to similar problems.

Mr. COHEN. As the members of the committee are undoubtedly aware, one of the most striking economic and business developments in recent years has been the tremendous increase in corporate acquisitions and mergers. Every day, in the Wall Street Journal, and other publication of general circulation, one reads of two or three or more of these and often they involve the acquisition of corporations of substantial size and importance. One result of this trend has been the recent rise of the so-called "conglomerate corporation," which conducts numerous, separate and, most frequently, unrelated types of business.

Mr. KEITH. You have changed your statement there, Mr. Chairman.

Mr. COHEN. If I did it was inadvertent.

Mr. KEITH. You said in the statement "most frequently."

Mr. COHEN. That is true. I will correct my statement.

Mr. KEITH. And you corrected it by saying "very frequently."

Mr. COHEN. Well, I will change it back to "most frequently."

Mr. KEITH. I think it is of some importance.

Mr. COHEN. Yes, sir. A principal means by which these acquisitions are accomplished is the tender offer, or takeover bid, by which a corporation seeking to acquire another makes a public offer to purchase its shares. There are reasons for the popularity of tender offers. They are fairly obvious but if the committee will forgive me I would like to recite some of them anyway.

These may include speed, simplicity, and also—and of particular significance—the fact that, unlike a negotiated merger, the concurrence of existing management is not required and, unfortunately for the public interest, little or no disclosure is usually made. This contrasts with the two other principal methods by which control of a company is changed, the proxy contest and the negotiated merger or purchase of assets. In these situations, stockholders are required to vote and consequently the proxy rules apply and full disclosure is obtained. Where the 1933 act applies, of course, the registration statement contains information with respect at least to the efforts and identity of the offeror. As I will indicate later, there is a problem in that area. I might note incidentally, that this committee in 1964 wisely extended the scope of the proxy rules so that they now apply to practically all industrial corporations in which there is any significant public interest. In the tender offer, by contrast, there is no express provisions of law which requires any disclosure at all.

The offeror need not even disclose his identity, let alone his plans and purposes. Investors are therefore confronted with the necessity of making an important investment decision, the determination whether to sell their shares, or to keep them, without disclosure of material facts. The problem is compounded by the fact that the offeror usually wishes to bring all possible pressure on investors to decide quickly without reflection, and indeed without opportunity to consider relevant and material information.

The appeal is to get aboard the band wagon immediately or lose the opportunity to participate in what is made to appear an attractive offer. This situation is totally inconsistent with the basic philosophy of the Federal securities laws, as this committee has evolved them over the years in the Securities Act and the Securities Exchange Act, and in other statutes administered by the Commission, that investors should be furnished with full disclosure of material facts and given the opportunity to make a unhurried investment decision upon the basis of such disclosure. The purpose of the legislation before you is to remedy this situation.

The existence of a problem in this area has been recognized for some time. In the last Congress, and in particular on April 7, 1966, Chairman Staggers introduced H.R. 14417, a bill which was intended to accomplish essentially the same purpose as the bill before you today. Similar legislation was introduced in the Senate in that year. Such legislation, modified in the light of suggestions by various interested persons, was reintroduced in the current Congress and extensive hearings were held in the Senate Committee on Banking and Currency in the spring of 1967.

At those hearings, representatives of virtually every important organization in the securities field, including the New York Stock Exchange, which is represented here today, the American Stock Exchange, the National Association of Securities Dealers, and the Investment Bankers Association of America, appeared and testified in support of the legislation, although several of them had suggestions for changes, none, I believe, that affected the thrust or essential provisions of the bill. Following those hearings, the bill was unanimously reported out by the Senate committee and passed by the Senate on August 31, 1967.

At this point I would like to emphasize and reemphasize that the purpose of this bill, as the chairman indicated in his opening statement this morning, is a very simple one, solely to provide information to investors so that they can arrive at an informed investment decision. It is not designed to assist the offeror, nor designed to assist the management in resisting any plan put forward by the offeror. It is essentially based on the concept that the investor should have the information so that he can arrive at a decision. It would not involve the Government in any way in fashioning or effecting the terms of the offer, or of the arguments pro and con.

H.R. 14475, the other bill before you, differs from the Senate bill in certain respects. The following are the most significant: (1) Both bills require that a person making a tender offer, or otherwise proposing to acquire more than 10 percent of the outstanding stock of a company registered under the Securities Exchange Act, must file with the Commission a statement disclosing his identity together with certain information with respect to his financial arrangements and his purposes. Under the House bill, this statement must be filed with the Commission 5 days prior to the making of the tender offer, while under the Senate bill, the filing may be simultaneous with the tender offer. I think this change was made in response to suggestions made by the New York Stock Exchange. Their representatives are here today and I think they can explain their point of view on that.

We prefer, however, the provisions of the House bill, since this will give us an opportunity to examine the material and suggest any changes or corrections before it is disseminated to the public. If corrections are necessary after the material has been sent to the shareholders, this will not only be a source of embarrassment for the offeror but may also confuse the stockholders. We have come to this view after almost 35 years of experience under the proxy rules. Frequently proxy soliciting material filed by a contestant or by management may be, perhaps inadvertently but nevertheless may be, misleading—so misleading as to warrant correction. The Commission usually secures correction informally.

On occasion it is necessary to go to the courts but in either case, it is obvious what has happened and this frequently proves to be of embarrassment either to management or to the contestants in a way that perhaps affects the consideration of the issue by the shareholders on the mertis. Incidentally, in a proxy contest the Commission's rules require that the material be filed within 10 days before the filing. The so-called 5 day provision is designed to serve the same purpose in that connection, without blowing the Commission's horn too loudly, it is generally conceded that the Commission's administration of the proxy

rules is a model of administrative regulation by rulemaking which has served the purposes of the economy well.

There are differences between the proxy contest rules and the take-over bill. There is no doubt about that and I think the representatives of the Stock Exchange plan to deal with them. Nevertheless, we believe that this requirement is important. It would place a burden on the Commission, quite frankly, but we are, nevertheless, willing to assume it because we believe it will serve best the interests of the shareholder.

The second major respect in which the Senate bill differs is that that bill exempts offers made by means of a registration statement under the Securities Act of 1933. I adverted to this earlier.

Registration under that act will be required if the offeror seeks to acquire securities in exchange for new securities of his own rather than for cash. And in recent months and in the past year this particular moder of tender offer has become more and more popular. The House bill contains no such exemption.

The exemption in the Senate bill was presumably based on the conclusion that registration under the Securities Act will provide full disclosure to investors. That is true as to one side of the equation.

The pending legislation, however, applies not only to solicitations on behalf of the offeror but also to solicitations in opposition to the offer. Such solicitations are commonly made by the management if they elect to contest the tender offer. Under both bills the use of false or misleading statements by anyone in such solicitations is prohibited. But the exemption for registered offerings would mean that, although the offeror would be limited in his solicitations by the disclosure requirements of the Securities Act, solicitations in opposition would be unregulated except to the extent that the general antifraud provisions of the securities laws might apply. I think that this inequality is unjustified.

There are many situations as to which it would be difficult to mount a case of fraud but, as this committee decided back in 1934 with respect to proxy solicitations, this type of industrial warfare, if I may use that expression, should be subject to affirmative requirements which would be developed by the Commission to implement this legislation even if the activities do not rise to the level of fraud.

Our experience in the past 2 or 3 years indicates that this is very important.

(3) Under the House bill, securities deposited pursuant to a tender offer may be withdrawn at any time until they are accepted by the offeror, subject to such terms and conditions as the Commission may prescribe, and if the offer is for less than all the outstanding securities, they will be required to be taken up pro rata rather than on a first-come-first-served basis, again subject to rulemaking power in the Commission. Under the Senate bill, securities deposited under a tender offer may be withdrawn only during the first 7 days or after the expiration of 60 days, and pro rata acceptance is required only during the first 10 days of the offer. We think the House bill provides additional protections for stockholders in this respect and that, in view of the almost infinite variety in the terms of most tender offers, which are limited only by the ingenuity of the offeror and his counsel, some flexibility through rulemaking is needed.

I would like to speak to the No. 4 item. The House bill applies to tender offers for the securities of closed end investment companies registered under the Investment Company Act of 1940. The Senate bill does not. We believe that this difference in merely an oversight for which we are, in part if not wholly, responsible. Both bills apply to securities registered under the Securities Exchange Act of 1934. In drafting this provision, the fact that closed end investment companies are exempt from registration under the Securities Exchange Act because they are subject to comparable, and indeed somewhat more detailed, disclosure requirements under the Investment Company Act of 1940 was overlooked. But there is no reason why shareholders of closed end investment companies should not enjoy the same protections to be provided by this legislation.

While, as I have indicated, we prefer the provisions of the House bill to those of the Senate bill, insofar as the two differ, we regard these points as of lesser significance compared with the importance of enacting this needed legislation at this session of Congress. If this committee accepts the Senate version, we believe we could live with it. If experience demonstrated that there were serious problems, we could and would come back to you.

In closing, I should like to point out that the need for this legislation has increased rather than diminished since the Senate acted last year. The pace of tender offers accelerates and we have received from numerous Members of Congress, many businessmen, lawyers, and State and local officials expressions of serious concern with respect to various takeover bids which have been attracting so much attention. Allegations of fraudulent or improper practice are frequent. In fact, they are usual, and litigation alleging fraud by one side or the other in a contested tender offer occurs almost weekly. It is almost standard operating procedure.

We have had to respond that we will investigate allegations of fraud to the extent that they fall within our jurisdiction, and indeed we have. But, owing to the time required for such investigations, it may be that the tender offer will be all over before the investigation is completed.

We have had difficulty in some situations in reaching a decision that we could mount a fraud case. While I would not like to convey the impression that enactment of this legislation would cure all of these problems, it would certainly help. If there were an orderly, supervised process of disclosure and if some ground rules were laid down, not only would investors be better protected but everyone would know where he stands.

I think I should add one further point which is found in my written statement. When we appeared before the Senate we referred to a practice which had developed, called short tendering, which resulted in some disadvantage to investors and substantial advantage to certain people in the securities business.

The Senate committee though that this was a matter within the antifraud authority of the Commission and that the Commission should deal with it. We have. We have adopted a rule which deals with that problem.

Thank you, Mr. Chairman.

Mr. Moss. Thank you. I would like to ask just a few questions here. Has the Commission collected data regarding the number of character offers made within any recent given period.

Mr. COHEN. We don't have any statistics on any systematic basis but I did testify—and I think it has been accelerating since then—that in 1960 the aggregate of cash tender offers was less than $200 million if I remember correctly, and that in 1965 it was almost $1 billion. The pace since 1965, in 1966, 1967, and 1968, has quickened. This is an aspect of a situation that apparently is going on all over the world.

Unfortunately, we don't have the tools to deal with them whereas other countries of the world have developed tools. By way of interest, in England they first began to deal with this problem some 7 years ago on a voluntary basis. They have since revised the rules three times. The rules they have today are pretty tough rules. The rules have been in effect only 2 or 3 months and on my recent visit to Europe I discussed them with the chairman of a special panel that was created to administer these rules. It appeared to me that voluntary compliance with such a code will probably not last very long. Only this past week, in a case involving one of the largest companies in Great Britain, there has arisen a problem which indicates some difficulties with this voluntary arrangement. It relates to Courtald's attempt at a takeover bid for International Paints and there is quite a bit of stew about it.

In fact, the chairman of that outfit has since suggested that there be created in Great Britain an SEC to administer the takeover rules and other matters. I was leading up to that, Mr. Chairman.

Mr. Moss. Well, to the extent that you have the data on the number of tender offers, do you have anything showing how many of the transactions have been consummated?

Mr. COHEN. I can't answer that question at this moment. We can supply that for the record to the extent we have it, but I must say we have not collected information of that kind since no filing requirement now exists. I think that recent times have demonstrated that many offers are made and they are very frequently frustrated by another offer which may be more pleasing to or arranged by the management. Very often this results in a situation where the shareholder may be faced with two or three different kinds of offers, some cash, some partly cash and securities, some in securities and sometimes securities of several kinds. The ordinary problem that an investor faces in determining whether to buy or sell a security is multiplied manifold.

So far as your question with respect to success is concerned, a great many of them are successful, but more and more of them are not successful principally because management has opposed them. There is no regulation of the manner in which management does this. I am not suggesting that there is anything wrong with such activities by management but they have brought onto the scene other offerors with the result that the investor, because he is forced to tender promptly in order to take advantage of certain provisions of the offer, is faced frequently with an impossible situation in terms of determining which is in his best interest.

This is true not only of the investor but of the person who advises him. But we will, if the chairman wishes, submit such information as we have compiled. But I am afraid we don't have any systematic information

(The information requested follows:)

SECURITIES AND EXCHANGE COMMISSION,
Washington, D.C., July 1, 1968.

Hon. JOHN E. MOSS,
Chairman, Subcommittee on Commerce and Finance, Committee on Interstate and Foreign Commerce, House of Representatives, Washington, D.C.

DEAR MR. MOSS: As I indicated to you at the hearing on H.R. 14475 and S. 510 this morning, persons making cash tender offers are not required to file any statments with the Commission. After a review of our records, I find that we have no information on the total number of tender offers made during any recent period, on the spread between the tender prices and the market prices at the time the offers were made, on the number of offers which were successful during any recent period, or on the number of persons who made tender offers and thereafter sold their holdings to persons making counter offers.

As far as we are aware, the study by Professors Samuel L. Hayes III and Russell A. Taussig, published in the April 1967 issue of the Harvard Business Review and included as Appendix 2 to the Senate hearings on S. 510, covering the period from January 1, 1965 to December 31, 1966, contains the most complete compilation of information currently available concerning cash and stock tender offers. We know of no comparable compilation of data for more recent periods.

Sincerely,

MANUEL F. COHEN, *Chairman.*

Mr. Moss. Do you have any data showing the price at which the acquiring person is ready to accept tenders? If so, what is the spread between this price and the quoted market price?

Mr. COHEN. I don't have any specific information. I am sorry to sound so disorganized in this area, but we just don't have the information since there is no requirement that we be informed. But experience indicates that the price offered is usually a substantial premium over the market price, and this has been pointed to as enough to satisfy any shareholder. The problem that I have with that argument is that if someone is willing to pay, let's assume, 5 percent more than the market price, obviously he thinks it is worth more than 5 percent or else he would not offer it; and offers are made for a variety of reasons. I should go back a minute. Very often these offers are not for all of the shares. Therefore, a shareholder has a number of questions to decide:

One, does he want to remain with the company under the new and inspiring leadership which is sometimes offered; two, does he think that, in any event, even if he tenders all of his shares and they are not all taken he is going to continue as a member of that company. This raises the question whether he should sell his shares in the market which sometimes adjusts to these offers. Thirdly, he is not in a position to make the kind of analysis as among competing offers that he needs to make.

It is for all of these reasons that I think this bill, which would provide the Commission with a modicum of rulemaking authority, would permit us to develop appropriate rules.

If I may again go back to the analogy of the proxy rules, it should be recalled that we do have an elaborate scheme of proxy regulation which springs from a single sentence in the 1934 act, which, paraphrased in very plebian terms, merely says: "Mr. Commissioner, please adopt a scheme of regulation in the public interest."

Now, since we first started in this area we have had seven major revisions of the proxy rules with the assistance and cooperation of industry generally, the securities industry in particular and of the bar associations and other interested groups. I am repeating myself, but I

think it is accepted as being a model of a disclosure scheme. This is an area, this area of industrial warfare—based on my own experience I can say this—an area in which the greatest ingenuity has always been employed. The Government's ingenuity is frequently no match for it and there is a lag. I must confess that. But we do catch on after while and adopt the appropriate regulation to deal with the problems—at least the major problems.

Mr. Moss. Do you have any data which would show in the case of transactions which are not completed how many of the share tenders were actually accepted and, is there any information as to whether the acquiring person during the course of receiving these tenders may have unloaded shares that he possessed prior to making this offer?

Mr. COHEN. We don't have any systematic information, but we do have some information in particular that the last item may have occurred. We have such a situation under investigation. I would rather not speak further to it. This is an area where darkness very often serves the purposes of many, but certainly, not that of the investor.

Mr. Moss. As long as you have the matter under investigation——

Mr. COHEN. There have been other situations, Mr. Chairman, which you may have in mind.

There has been enough experience in the past 2 years for any sophisticated takeover bidder to know that, unless management joins him, management will seek another partner and that other partner probably will make a slightly better offer. We have the feeling that many of these people are doing it for the short-term gain, or, to use the vernacular, to make a fast buck. We have a number of variants of that. We have a situation where almost overnight particular individual or company made several millions of dollars in a situation of this kind.

We have the feeling that some of these offers are made only to initiate that activity.

Now, there is one thing about that.

Mr. Moss. I was going to ask you that. Has this device been used in your judgment for the sole purpose of pushing it up?

Mr. COHEN. I can say that I think it has been, but I cannot say that we have a case in which we have proven it. I think there has been a good deal of discussion of this in the newspapers and I think the newspaper people, who are frequently very sophisticated about these matters, think so. I believe it has happened. We have had other kinds of problems. In fact, there is one which occurred recently where there is a question which has been raised about whether or not some of the profit, if not all of it, may be subject to some recovery action by the company involved.

Mr. Moss. There again you anticipate a question. I was going to ask whether there should be some kind of mechanism provided for this type of manipulation to be made unprofitable, that is the profit be recapturable by the corporation, or, in the absence of a suit, by the corporation or its stockholders by the Commission.

In this connection I think we should take note of the recent transactions of Crane Co. and the proposed acquisition of control of Westinghouse Air Brake Co. When this failed Crane sold its holdings for around $75 million and presumably made a profit of some $5 million to $10 million, and I have a series of recent press clippings, which I am

going to ask unanimous consent to be made a part of the record at this point, which illustrate a series of cases where this appears to have happened.

(The documents referred to follow:)

[From the Wall Street Journal, May 16, 1968]

TOM EVANS' TAKE-OVERS BUILD A VAST FORTUNE, STIR HOT CONTROVERSY

CRANE, PORTER FIRMS GROW AMID EXECUTIVE TURMOIL; KEY VOTE AT WABCO TODAY

Make Profits Quick—Or Else

(By John Barnett)

PITTSBURGH.—Thomas Mellon Evans grows suddenly solemn as he discusses his latest corporate battle. "Talk about business ethics," he says. "I've never seen anything to match the unethical way that damn Westinghouse Air Brake outfit operates."

Executives of Westinghouse Air Brake Co. (Wabco) retort, in effect: Look who's talking about ethics. In a court brief, company lawyers have described Mr. Evans' original offer to purchase Wabco stock, in exchange for debentures of Crane Co., of which he is chairman, as an attempt to pull off a "dishonest swindle."

That exchange is a fair sample of the acrimonious nature of the battle for Wabco (1967 sales: $305 million), which heads for a key stockholder vote today. It's also typical of the fierce controversy that Tom Evans now 57, seems to create almost as naturally as he makes money.

Over the last three decades, Mr. Evans has been embroiled in battles for control of many companies. In nearly all, he has been cast in the unpopular role of a bumptious outsider trying to bull his way past a reluctant management.

Moreover, Mr. Evans has become something of a legend for his tough methods of operating a company once he wins control. He demands prompt profit performance from both assets and men, if he doesn't get it, he sells the assets or fires the men. Some sample reactions to these methods: Pickets marched outside the 1959 Crane Co. annual meeting, at which Mr. Evans was elected chairman, carrying signs berating: "Money-Mad Evans." And at the Evans-run H. K. Porter Co., a favorite quip defines an optimist as a Porter executive who brings his lunch to work.

Tom Evans' methods, however, have enabled him to build not one but three business empires. Besides his brokerage firm, he runs Crane, a maker of plumbing and heating supplies with 1967 sales of $403 million, and Porter, a Pittsburgh-based conglomerate with 1967 sales of $280 million, as entirely separate companies; the other concerns he has won control of have been merged into these firms. Besides being chairman of both concerns, he owns 15% of Crane's outstanding common stock and 67% of Porter's.

Mr. Evans formed the brokerage house, Evans & Co., 11 years ago to save brokerage fees on his extensive stock deals. Through it, he, his wife and three grown sons have made personal investments in scores of companies he doesn't control—at least not yet. Altogether, starting with little more than an inheritance of about $15,000 (despite his middle name being Mellon), he has amassed a personal fortune estimated at $80 million to $100 million.

The Wabco Fight

Now Mr. Evans is seeking to merge Crane and Wabco, an old Pittsburgh-based concern that, besides air brakes, makes railway switch gear, train-control systems, earthmoving equipment and mining machinery. (It and Westinghouse Electric Co. were both founded by George Westinghouse, inventor of the air brake, but there is no connection today between the two Westinghouse concerns.) Meeting bitter resistance from management, he has sought to have Crane acquire enough Wabco common stock to force a combination. At first he attempted to obtain this stock through cash purchases by Crane. Then he turned to the Crane-debentures-for-Wabco-common offer, which has been extended three times; it now expires May 24. Mr. Evans says that as of Tuesday Crane owned nearly 31% of Wabco's common.

Wabco management's response has been to accept a merger offer from American Standard Inc., Crane's chief rival in the plumbing-fixtures field. Wabco stockholders vote today on this proposal, but whichever way this ballot goes, the

outcome of the fight probably will not be definitely known until several lawsuits concerning the battle are decided.

Mr. Evans contends Wabco management acted unethically by turning down Crane's merger proposal after insufficient consideration and then turning to American Standard before Crane had enough time to come up with a better offer. Wabco management replies that Mr. Evans sought to pull off a "dishonest swindle" by trying to induce Wabco shareholders to exchange their common stock, which carried an ownership interest in the company, for Crane debentures that would have given them no ownership interest in the merged concern (Crane later modified the proposal to make the debentures it is offering partially convertible into Crane common stock).

Getting Personal

As happens frequently in an Evans fight, the battle has gotten into personalities. A. King McCord, Wabco chairman, has accused Mr. Evans of offering him "inappropriate" financial inducements, including stock options in a merged company, in an effort to win his backing for combination with Crane. "I was shocked" at this offer, he says.

Mr. Evans, in reply, tells an inquirer with a chuckle that he sees nothing wrong with the offer—except that, since Mr. McCord rejected it, "I guess it wasn't inappropriate enough, wouldn't you say?"

The mixture of banter and bluntness in that reply is indicative of the personality that makes Mr. Evans so controversial. To an interviewer, he seems a curious blend of boyish enthusiasm and steely calculation. He is a stocky, nervously active man of medium height whose round face is habitually twisted into a grin—sometimes apparently out of simple good humor, sometimes in obvious relish over victory in a business deal.

Friends find him a pleasant and even charming social companion, whose seemingly boundless energy can be engaged by a discussion of politics or early American art as well as by business. He delights in showing a visitor the 19th-century prints of New York scenes that decorate his Park Avenue office in that city, and he confides that although he is a lifelong Republican—he was a Taft-pledged delegate to the Republican National Convention in 1952—he has contributed money this year to Senator Eugene McCarthy's campaign for the Democratic nomination because he thinks the U.S. involvement in Vietnam is "immoral."

But his best friends concede that this chatty acquaintance becomes a very different person in business deals. An associate who describes Mr. Evans as "quite shy and proper on the personal side" says that "on the business side he's extremely bellicose—rough, hard-driving, a tough guy." George Moore, chairman of First National City Bank of New York, puts it this way: "Tom Evans is a tough, realistic, competent businessman whom you don't want to run afoul of unless you know precisely where all the aces are."

Former Aide's View

To many of his employees, Mr. Evans seems a shouting tyrant whose wrath is apt to erupt at any time. A confrontation with him can be a nerve-shattering experience for a subordinate, says one former Porter executive: "He'll call somebody a dumb bastard or an ignorant son of a bitch, and the guy has no choice but to put up with it—until he can find another job."

In any case, friends, adversaries and employes agree on two traits, Mr. Evans shows to everyone. He is blunt—to the point of creating problems for himself says one associate: "Sometimes I think he needs a personal public-relations counselor." And he has displayed uncommon determination in taking over companies; some 43 have been absorbed into H. K. Porter alone in the last 19 years, many over the resistance of their managements, and nearly all have been profoundly transformed under his stern make-money-quick-or-else demands.

Though, like the Mellons, he comes from Pittsburgh, Mr. Evans is only distantly related to the banking family whose money launched Mellon National Bank & Trust Co., Gulf Oil Corp., Aluminum Co. of America and other giant concerns. (In the Wabco fight, in fact, four company directors associated with Mellon Bank are among his opponents; he refers to one, the bank's chairman, as "my ex-friend Johnny Mayer," and he has had Crane Co. take $2 million in deposits out of the bank.) After graduating from Yale in 1931, he began his career inconspicuously as a clerk in the chairman's office at Gulf Oil.

An Early Conglomerate

He made some money investing in Gulf Oil stock, and in the mid-1930s began investing those profits and his inheritance—pocket money, by Mellon-family standards—in bonds of H. K. Porter, then a troubled maker of steam locomotives. Because Porter had defaulted in paying interest on the bonds, he was able to pick up those securities for as little as 10 cents per dollar of face value. Result: When creditors threw the company into bankruptcy proceedings, Mr. Evans emerged as the major bondholder, with enough bargaining power to come out of a court-supervised reorganization as Porter's 29-year-old president—over the objections of several older directors.

World War II helped Porter to recover, bringing profits to a subsidiary producing artillery shells. By 1948, though, it was still recording sales of only $11 million a year. At that point, Mr. Evans decided to diversify, and in succeeding years he built Porter into the kind of company that is now called a conglomerate. As the locomative business was phased out, acquisitions pushed the company into production of steel, industrial rubber products, electrical equipment, hardware, paint and refractory brick.

By 1959, Mr. Evans was ready to undertake a new venture. He bought a substantial block of Crane Co. stock as a personal investment. He then hired Alfons Landa, the most feared proxy fighter of the day, as his lawyer and confronted Crane management with a demand that he be made chairman. After a stormy, but brief, battle, he won—and began a transformation somewhat similar to the one he had carried out at Porter. Since he took over, Crane has acquired 30 companies, though it hasn't diversified quite so widely as Porter; it has tended to stick to meters, valves, purification gear and other devices in the "fluid-control" field.

The methods by which he has expanded both companies have generated fierce controversy. To avoid diluting the equity of shareholders (meaning, at Porter, chiefly himself), he has always insisted on making acquisitions for cash rather than by issuing stock. To get the cash, he has sold less profitable assets (including, at Crane, most of the company's once-extensive warehouse system), held inventories to a minimum and insisted on a prompt profit return from any capital investment. He is frank in stating that he also has held down spending on research and new-product development. "When we develop a new product from scratch," he says, "its because we can't buy somebody who already makes it."

Reply to Criticism

All this has given him a reputation for ruthless wilingness to liquidate plants and fire workers wholesale if he can see a financial gain in doing so. Friends say he is sensitive to such criticism and regards it as unjust. Mr. Evans himself says only that rapid expansion of Porter and Crane was possible because "there were a lot of badly run companies that we could buy cheap" and that "some of these companies gave us a lot of trouble" after acquisition.

In any case, Mr. Evans' companies are still using the same methods. In July 1966, for instance, Crane bought Glenfield & Kennedy Holdings Ltd., a British concern that makes water purification equipment and that D. C. Fabiani, Crane president, says was on the verge of bankruptcy at the time of acquisition.

"After we took over, there were a lot of firings," says Mr. Fabiani. "It involved cutting the payroll very substantially because a lot of people had been kept on with nothing to do." By October 1966, three months after acquisition, he says, the company was breaking even, and by the end of the year it was making a profit.

Mr. Evans' methods as an operating boss—and, in particular, his relations with subordinates—also stir much dispute. Several Crane vice presidents were fired immediately after he became chairman, and around Pittsburgh businessmen speak of the executive turnover at H. K. Porter with awe. Only three of the eight division general managers listed in the 1963 annual report are still with the company; some of the others have been replaced not once but sveral times in the intervening five years. At lower levels, the turnover is said to be even more rapid.

To be sure, many executives leave of their own accord or are lured away. Mr. Evans has a policy of hiring relatively young men for such responsible jobs as division general manager or sales manager; executive recruiters frequently go after such men after they've had a bit of seasoning in what has been referred to as "the Evans School of Business." One former Porter executive is said to have kept two telephones in his office—one for regular business purposes. the other, a private line, for calls from recruiters.

But Porter doesn't deny that many executives are simply fired, abruptly and without apology, because they don't meet Mr. Evans' exacting standards for profit performance. "We are totally ruthless with people who can't handle the job," says J. Stuart Morrow, president.

The executives who last are handsomely rewarded. B. Campbell Blake, vice president and general manager of Porter's Connors Steel division, last year drew $195,556 in salary and incentive bonuses—nearly twice the $100,000 salary Mr. Evans himself took from Porter.

But though the pay can be high, the pressure from Mr. Evans is constant and intense, those who have worked for him say. Some contend it occasionally backfires, too.

When a general manager discovers he can't turn a profit as fast as he's supposed to, he starts looking for another method," says one former Porter executive. "He can fudge his figures, but he knows Evans is sharp and that won't work long. So he has to find something else." He implies this creates a temptation to cut corners on product quality as a method of improving profit margins.

Several sources offer such an explanation for the troubles of BPS paint, a product line that Porter acquired in 1960 but sold in 1964 after the paint had acquired a reputation for uneven quality. Mr. Evans grins ruefully when this product is mentioned. "That was one of my mistakes," he says. He concedes Porter lost money on the paint operation—but adds that it got some tax benefits from selling the line.

Overall, the profit performance of Mr. Evans' companies recently has been somewhat uneven. Porter's net income hit an all-time high of $7.4 million in 1966 but dropped last year to $4.3 million, its lowest net since 1961. Crane has done somewhat better; though its 1967 profit was down to $10.2 million, from $11.3 million in 1966, earnings for the two years taken together represent a substantial improvement from the early 1960s, when it and other plumbing-fixture makers went through a deep profit slump.

On the Move

Mr. Evans runs Crane somewhat less closely than he does Porter; he leaves much of Crane's day-to-day operation to President Fabiani. But he still keeps a close eye on both companies. He logs about 100,000 miles a year in business flights around the country in his personal four-engine jet ("That doesn't include the fun trips to Europe or South America," he says), visiting companies he is thinking of having one or the other concern buy or dropping in on the 100-odd Crane and Porter plants.

On such visits, Mr. Evans probes into small details; he has a penchant for reading salesmen's call reports and checking up on direct-mail advertising operations. "He makes no effort to follow the chain of command," adds Porter President Morrow. "He will walk through a plant and tell a foreman what to do, even though the plant manager may be standing right next to him." But, Mr. Morrow says philosophically, "It's his company, and he can run it any damn way he wants."

Even sitting in his office on Park Avenue, Mr. Evans puts on a show of the energy that admirers say is his greatest executive talent—and that leaves a visiting reporter dazed. He twists and turns restlessly in his chair, his eyes darting occasionally to a closed-circuit television screen opposite his desk that flashes a constant flow of stock quotes piped in from the adjacent offices of Evans & Co. And, during the one-hour interview, he conducts this business:

A chat with Crane Co. vice president and controller James O'Brien, who reports some figures on the Crane-Wabco fight.

A discussion with son Ned of Ned's efforts to buy a Massachusetts apartment building as a personal investment for his father.

A discussion with Crane President Fabiani of merger talks Mr. Fabiani is conducting with executives of a boiler-making company in an office across the hall.

A brief personal visit to those merger talks.

A telephone call to George Champion, chairman of Chase Manhattan Bank and a director of Travelers Insurance Co., to ask his help in getting Travelers to abstain from voting its sizable block of Wabco shares against Crane ("Say, George," Mr. Evans begins the conversation, "you probably know we're having a problem with this damn Westinghouse Air Brake").

Another phone call to a mutual fund executive to set up an appointment to try to persuade him to sell the fund's stock in American Standard, Crane's rival

in the fight to take over Wabco, and buy Crane debentures instead ("I'd like to come up and show you some figures on a better investment than that turkey," Mr. Evans says).

Between these conversations, Mr. Evans remarks that if he had known the Wabco fight "would be this much damn trouble, I would never have got involved." But one of his aides questions this assertion. Despite the acrimony of the battle, the aide says, "I would guess that Tom Evans is having more fun than he's had in a long time."

[From the Wall Street Journal, June 14, 1968]

CRANE'S INTEREST IN AMERICAN STANDARD SOLD

BATTLE FOR WESTINGHOUSE AIR ENDS WITH LARGEST BLOCK SALE ON BIG BOARD RECORDS

Trade Amounts to $76 Million

NEW YORK.—The spectacular six-month fight of Crane Co. for control of Westinghouse Air Brake Co. ended yesterday in an appropriately dramatic fashion as Crane sold its block of 730,312 shares of American Standard Inc. preferred stock for $76 million.

The transaction, in dollar value, represented the largest single-block trade on the records of the New York Stock Exchange. It also effectively ended a corporate battle that has produced a series of verbal and legal fireworks.

The winner of the struggle was American Standard, the aggressively expanding plumbing-supply maker that last week successfully consummated its acquisition of Westinghouse Air Brake. While Crane Co. lost out, it was left with what it thinks will be a rather healthy consolation prize—a substantial, but as yet unspecified profit on its investment in Westinghouse Air Brake.

Thomas Mellon Evans, Crane's chairman, acknowledged Crane's sale of the American Standard preferred stock shortly after sale of the huge block appeared on the stock exchange tape. Asked why Crane had sold, he replied simply, "Oh, we thought we might as well let it go." Crane had received the American Standard preferred in exchange for its holdings of 31% of the outstanding common stock of Westinghouse Air Brake.

Blyth Handles Sale

Ironically, the Crane transaction was handled by Blyth & Co., the underwriters that helped American Standard obtain proxies in its battle with Crane. Crane had sued both American Standard and Blyth to bar them from voting certain shares, but the suits were dismissed. American Standard said yesterday that the preferred stock was purchased by several private and institutional investors. None of the buyers was named.

The question of how much of its profit from the sale Crane will be able to keep probably won't be resolved until after litigation, Mr. Evans stated. He said that the "majority" of the Westinghouse Air Brake stock had been purchased more than six months ago, and that "there's no question" Crane will get the profit from these shares. As for the stock kept less than six months, Mr. Evans said that "we think we can keep the profits" but that the question "might have to be settled by litigation."

Because Crane owned more than 10% of Westinghouse Air Brake, Crane qualified as a corporate "insider." Insiders who sell their stock within six months after purchase must return the profit to the issuing corporation.

Involuntary Exchange

The question is complicated, however, by the fact that Crane exchanged its Westinghouse Air Brake stock for American Standard preferred rather than selling it outright. Mr. Evans also notes that the action was involuntary as Crane voted against the merger.

Mr. Evans declined to estimate how much of the $76 million sale price represented Crane's profit. He said only that it was "fairly substantial but nothing tremendous."

Yesterday, on the New York Stock Exchange, Crane Co. closed at $48.50, off 25 cents, while American Standard dropped 75 cents to $37.75. American Standard's new $4.75 convertible preference stock, which Crane sold at $104.25, closed as the most active stock at $106, up $1.75, on a volume of 782,100 shares.

Crane's $76 million transaction was the largest single block trade in dollar volume by a large margin. The previous record holder was 1,153,700 shares of Alcan Aluminium Ltd. valued at about $26.5 million last Oct. 31. The American Standard preferred block is the third largest in terms of share volume.

Crane's Key Card

Crane's holding of the large Westinghouse Air Brake block became its key card after a Federal judge two weeks ago dismissed Crane's attempt to invalidate proxies voted in favor of the merger with American Standard. In exchange for its Westinghouse Air Brake holdings, Crane received a block of American Standard preferred stock convertible into almost two million shares of the company's common. Thus, even after complete conversion of the preferred issue, Crane could have owned 11% of the outstanding common stock of American Standard its largest competitor in the plumbing-supply field.

The antitrust implications of this situation drew inquiries from the Justice Department. Presumably, Crane had hoped the department would move to block the American Standard-Westinghouse Air Brake merger and eliminate the antitrust problem. But American Standard was contemplating eliminating it in another way—by filing suit to force Crane to divest itself of its American Standard holdings.

One Crane suit against the merger still remains pending in Federal court in Pittsburgh. Mr. Evans said yesterday Crane hadn't decided whether to drop the court action.

[From the New York Times, June 14, 1968]

MARKET PLACE: TOES BRUISED IN GIANT TRADE

(By Robert Metz)

What more fitting day for it to happen? The same day the Big Board tore up the record book as volume pushed through the roof to 21.35 million shares, brokers put together the biggest deal in the history of the exchange.

There was competitive spirit and flamboyance in abundance surrounding the transaction and not a few toes were bruised at Walter Frank's post on the floor where 730,312 shares of American Standard preferred stock sold in a single massive trade for $76 million.

The biggest previous trade was almost puny by comparison. While more shares were involved then—1,153,700—those Alcan Aluminum ducats were valued at just $26,535,100 last October. So yesterday's deal was nearly three times as big.

Tied up in the tidy $76 million was a profit estimated at $9 million for the Crane Company which got the 4.75 percent preferred shares after the company's ardently sought bride, Westinghouse Air Brake, merged instead with American Standard, the rival plumbing company.

Thomas Mellon Evans, the colorful man behind Crane's attempted take-over of Wabco, evidently paid $65.88 million in cash and securities and perhaps $2 million more for expenses to establish his position in the Pittsburgh industrial giant. He still owns about 10,000 of the American Standard preferred shares which closed yesterday well above the 104¼ he got for them—specifically at 106, up 1¾.

But informed Wall Street sources were guessing that Mr. Evans would be challenged for his profits. American Standard would not comment as to whether it intended to battle for return of the profits, but others with a grasp of the situation did. One legal expert said that as an insider—an owner of more than 10 percent of Wabco's shares—Crane would have to return all the profits to American Standard.

On the other hand, there was a "question of law as to whether profits on all the shares or just on those in excess of 10 percent would have to be returned. If the court ruled that the first 10 percent was exempt from the insider rule, Crane Company would have $5 million in profits. If not, Crane would get nothing for its efforts.

Meanwhile, back on the floor there was at least one company that evidently thought it had been setting up the biggest cross in history. The firm—Tyne, Kendall & Hollister—hoped to make the commissions on both the buy and sell sides. No comment came from Tyne, Kendall.

In fact, Blyth got the seller's commissions. Tyne, Kendall shared the buyer's commissions with Salomon Brothers & Hutzler, and, to a smaller extent, with Blyth.

Wall Street sources said, Tyne, Kendall had been "up night and day working on the deal since the beginning of last week" and thought it was theirs.

The firm reportedly found out during actual negotiations on the floor that the pie was being sliced into several pieces. The floor discussion lacked some of the diplomatic niceties—or so an observer said. "It was certainly not a nursery school tea party," he commented. There was a lot to fight over. The commissions totaled $750,000—half on the buy side and half on the sell.

[From the Wall Street Journal, June 17, 1968]

AMERICAN STANDARD SET TO SUE CRANE, ASKING FOR RETURN OF PROFIT

GAIN CAME ON CRANE'S DISPOSAL OF STOCK RECEIVED IN RETURN FOR WESTINGHOUSE AIR HOLDING

NEW YORK.—American Standard Inc. plans to sue Crane Co. this week, asking for the return of Crane's profit on the disposal of its holding of Westinghouse Air Brake Co. stock, William D. Eberle, president of American Standard, said in an interview.

Last Thursday, Crane sold a block of 730,312 shares of American Standard $4.75 convertible preference stock for $76 million, the largest single-block trade in dollar value in history on the New York Stock Exchange. Crane had received the stock in exchange for its holding of 31% of the outstanding common stock of Westinghouse Air Brake, which has merged into American Standard.

Because Crane owned more than 10% of Westinghouse Air it qualified as a corporate insider. Insiders who sell their stock within six months after purchase must return the profit to the issuing corporation.

However, the Crane transaction is complicated by several questions: Can the company keep its profit on the portion of Westinghouse Air Stock bought more than six months before the merger? Can it keep all its profit because it exchanged Westinghouse Air for American Standard preferred rather than selling it? Can it keep the profit on the shares it bought before it had acquired a 10% interest and become an insider?

Mr. Eberle said the questions didn't have any clear answers and that "probably the only way it can be clarified is through court action."

Thomas Mellon Evans, chairman of Crane, declined to say how much profit the company actually made. But he said a published figure of $9 million was too high.

According to Mr. Eberle, court testimony showed that Crane paid slightly less than $66 million for its Westinghouse Air holdings. But Crane's additional expenses—including the cost of selling, brokerage fees, and financing costs are an unknown factor, he stated. "Their profit could be anything from nothing to $9 million," Mr. Eberle said.

In another area, Mr. Eberle predicted that the acquisition of Westinghouse Air Brake would add 15 cents a share to American Standard's net income this year. But he said he felt that Wabco in future years could do at least as well as its record $16.8 million earnings in 1966, which would have added more than 50 cents to American Standard's net.

American Standard manufacturers plumbing and heating supplies and, through it Mosler Safe division, security equipment. Westinghouse Air Brake is a Pittsburgh-based producer of braking equipment, railway signal and control gear, heavy equipment for construction and mining, and electronic gear for defense uses.

Mr. Eberle said Westinghouse Air's earnings would be consolidated with American Standard's for the second quarter on a pooling-of-interest basis.

The American Standard executive, who has pledged to embark on a diversification program that will produce sales of $2 billion in 10 years and lessen the company's dependence on housing, said sales this year, including Westinghouse Air, should approach $1 billion, with only about 60% tied to the housing market.

Mr. Eberle said he couldn't precisely project American Standard's 1968 earnings because "the whole last half of the year is up in the air" due to uncertanties over taxes and interest rates. He said, however, that he still is sticking with his forecast six months ago of 1968 net somewhere in the area of $1.70 a share.

Speaking about plans for Westinghouse Air Brake, Mr. Eberle said there wouldn't be any major changes of management with one exception: The retirement of Chairman A. King McCord next spring when he reaches age 65. Mr. McCord's successor, Mr. Eberle stated, will come from within the company. The most likely candidate is considered to be Lawrence W. Walkley, Westinghouse Air president.

Mr. COHEN. Those press clippings, Mr. Chairman, have given rise to my personal feeling—I don't know that I am prepared to speak for the Commission only because we have not sat down to evolve an official position, but I think all of my colleagues share my view—that many of these offers are made in order to achieve a short-term profit on this basis.

Now, that particular situation to which you referred involving Crane may become the subject of some litigation in which the Commission may or may not be involved and for that reason alone I would prefer not to speak to it, but I think the clippings indicate that the parties involved were not unaware of the possibilities.

To answer your question specifically, we do have antimanipulative authority under the statute. I am not sure that there is any real lack in this area.

I think that this bill, which will provide the Commission with the right to develop affirmative rules which are not necessarily antifraud, will serve to obviate many of these situations that might otherwise occur.

The second part of your question related to our right to seek recovery. The statute provides that any officer or director and any person who owns more than 10 percent of the shares of any equity stock of a listed company, and of certain other companies, who makes a profit in the purchase and sale or sale and purchase of stock of that company within a 6-month period, is subject to suit at the hands of the company, or by a shareholder on behalf of the company.

Now, that perhaps is not as complete a remedy for some of the takeover situation to which you have referred because some of them are made by persons who either were not more than 10 percent holders at the time of the acquisition or perhaps never quite reached that point but who nevertheless are engaged in this form of short-term trading. This is an area that merits attention by the Commission and by the committee. Indeed, I have an unanswered letter from a member of the committee which relates to that problem.

(For further information subsequently submitted, see letter dated July 9, 1968, p. 75.)

Mr. MOSS. Now, Mr. Chairman, I have one last question.

The Federal Reserve Board has written expressing its support in general for the legislation but objects to the exemption from disclosing the financial arrangement where funds are provided by means of a loan made in the ordinary course of business by a bank.

The Board says that it is not aware of any reason why the same disclosure requirements should not apply to banks as to other lenders. The Board accordingly recommends the deletion of the exception which starts on page 2, line 22, of S. 510 and continues through line 25.

In the alternative the suggestion of confidential treatment is made. My question is what is your opinion with regard to this matter?

Mr. COHEN. First, let me say, Mr. Chairman, that I have never been in any disagreement with the Federal Reserve Board, certainly not publicly. Nor have I ever placed myself in the position of being for sin or against virtue. Quite obviously the suggestion of the Federal Reserve Board is not only a meritorious one but one which should receive very careful consideration.

I would like to explain how the exemption got there and perhaps that may in part answer your question and if it does not I will answer your question directly on my own behalf.

The provision was put in there because it was felt that if the names of the banks were disclosed economic pressures being what they are in our real world that this might make it difficult for either management or someone who wishes to make a takeover bid to acquire the necessary financing in a perfectly legitimate arrangement.

I think the proposal of the Federal Reserve Board, as you read it, meets that problem directly and on that basis the Commission I am sure, although I cannot speak for the Commission because it is the first I have heard of this particular suggestion, would have no objection to an amendment of the bill along the lines suggested by the Federal Reserve Board.

Mr. Moss. I ask unanimous consent to place in the record a letter from the Federal Reserve Board setting forth its views.

(The letter referred to appears on p. 8.)

Mr. Moss. Mr. Keith.

Mr. KEITH. Thank you, Mr. Chairman.

Besides the fraudulent aspects of this that you hope to attack, have you any personal views, or does the Commission have any views with reference to the purpose of the proposed taker-over? What I have in mind specifically is that I have been concerned for a long time with the concentration of power in fewer and fewer corporations and the lessening of competition in the marketplace. I recognize that the antitrust provisions speak to that particular point and where there is a tendency to create monopoly that there is statutory authority with which to proceed. But do you by chance know of any conglomerates or acquisitions, the primary purpose of which was to pick up a tax loss that in a way gives, by reason of the operation of our tax law, an advantage to one corporation over another if they merge?

Mr. COHEN. Mr. Keith, I appreciate that question because you remind me that I left out some important points that I would like to bring to the attention of the committee.

Mr. KEITH. That is always a hazard that I take when I probe your mind.

Mr. COHEN. Right. Please don't think that I was deliberately holding back for your question, although I am tempted sometimes. Seriously you are raising a very important and a very significant question for the American economy.

I could not express that more seriously and with more concern. We at the Commission, of course, are not involved in and we have no role to play in the general antitrust considerations as you suggested. These bills are not designed to deal solely with the antifraud aspects of

takeover bids. They are designed to provide a form of regulation as I indicated somewhat comparable to the proxy contest situation.

As far as conglomerates is concerned, this is a growing phenomenon. The antitrust people have recently issued some statements which deal specifically with this problem and it appears to me that they are growing more interested in it and more concerned with the effects of this development.

But as I say, this is not my field. I have been concerned with conglomerates and I have been speaking out to this for some 3 years now because of two things. First, if I may digress to point this up, this bill is not directed solely to the situation where there is a takeover bid for dormant, sleepy, unimaginative management which is usually the argument made. Many takeover bids are made by people who find it cheaper to pick up a bright, vibrant company than to go about setting up their own competitor and to this extent they limit competition but they also hope to pick up, at a fairly reasonable price, a company where the possible future value is not yet reflected in the marketplace because the company is in a growing stage. They also unfortunately pick up lemons here and there but when they drop them you don't hear about them. They go out the back door. It is for that reason that I have been concerned for some time now as to the adequacy of the disclosure that is made by these companies most of whom as you corrected me, Mr. Keith, are engaged in disparate businesses which have no relationship to one another.

Very often they are put together not because the businesses go well together but because the financial statements go well together, whether because of provisions of the tax laws or for other reasons. We have had some problems this year in which that has occurred and we have had to insist that a very large conglomerate company revise certain financial data it published in its annual report before the Commission would make effective a registration statement under the Securities Act. I have been after this disclosure problem for some time.

About a year and a half ago the Financial Executives Institute, and this is a marvelous instance of the statesmanship that industry brings to bear on these problems on occasion, came to me and suggested that we await a study that they would undertake and finance in this area.

That study has been completed, and I think the book which reflects the study and the conclusions drawn is just now reaching the bookshops. They make suggestions for important changes.

The American Institute of Certified Public Accountants at my request, and based on their own realization that there is a problem here, have been looking at this.

The National Accounting Association has just issued a report, so recent that I don't have a copy yet, but I have been informed generally what it is. These are reflections of a view by people who represent or work for management, as well as investors and creditors, that changes are required.

Now, the analysts and the investors have been asking for information in this area for a long time in order to determine better the situation of a particular company and to assess its future prospects in the context of its past history. But it is true, Mr. Keith, that there may be a larger problem involved in all of this and that is the growing

concentration of financial and economic power. That is not involved in this bill and it goes a bit beyond our jurisdiction.

In the proposed institutional investment study, we will deal with another type of growing concentration of economic and financial power which has its effects in the area of the problems to which you have adverted. Beyond that, I don't think it would be appropriate for me to express a view, Mr. Keith.

Mr. KEITH. Thank you.

You mentioned that you had ways to get at certain situations where stockholders with 10 percent or more of the stock——

Mr. COHEN. Not we, the courts. There is a provision of the statute.

Mr. KEITH. Who brings the action?

Mr. COHEN. Either the company, or upon failure of the company a shareholder on behalf of the company, and the recovery goes to the company to be shared by all of the shareholders.

Mr. KEITH. You have no authority to move.

Mr. COHEN. No, sir. We do not.

Mr. KEITH. And you are not requesting it.

Mr. COHEN. We are not. I think implicit in Mr. Moss' question—and I probably did not answer it—was whether or not the Commission should have authority in this particular area.

I hesitate to say yea or nay to that because whenever I do I am accused of engaging in the latest version of Mr. Parkinson's law, reaching out for power, but quite obviously I would have to say that, provided you vest this power in the Commission after I am gone, this would be a most effective way of dealing with problems of this kind.

Mr. Loomis wants to add to that.

Mr. LOOMIS. There are quite a number of cases pending now under section 16 of the Securities Exchange Act, at least five or six of them involving a situation where a person made a tender offer, got 10 percent of the stock and then there was a so-called defensive merger and the person who had made the tender offer then sold the securities he acquired as a result of the merger for a substantial profit.

The courts have not yet decided any of these cases, and it will be interesting to see what happens.

Mr. COHEN. There is one further thing to complete my answer to Mr. Moss, with which I did not deal.

In these 16(b) cases, the courts, at least at the appellate level, frequently call upon the Commission to file a brief as amicus curiae with respect to interpretation of the statute.

As I say, we have no enforcement powers and for that reason normally we don't even engage in interpretation of 16(b). We do have authority with respect to 16(a), which requires the filing of information with respect to holdings and transactions by certain persons. In this area we have not been too bashful about issuing interpretations. In some of the 16(b) bases we have gone in where there has been placed in issue a question which seems to be important in the overall administration of the statute and may involve adversely the interests of investors. I do not believe we have invited in these particular cases to which Mr. Loomis has adverted.

Mr. LOOMIS. They are not on trial yet.

Mr. KEITH. Thank you, Mr. Chairman.

Mr. Moss. Mr. Watkins.

Mr. WATKINS. I have no questions, Mr. Chairman, but Mr. Cohen, I want to thank you for bringing in testimony here which cetainly will be helpful to us in making a decision.

Mr. Chairman, I would like at this time, with unanimous consent, request that the statement from Johnson & Johnson by their counsel, Mr. Arthur S. Lane, be made a part of the record.

Mr. Moss. Without objection, it will be. The Chair has the original of the letter and had intended making that part of the record.

Mr. WATKINS. That is all.

Thank you, Mr. Chairman.

(The letter referred to follows:)

JOHNSON & JOHNSON,
New Brunswick, N.J., June 28, 1968.

Re S. 510, H.R. 14475.

Hon. JOHN E. MOSS,
Chairman, Subcommittee on Commerce and Finance, Committee on Interstate and Foreign Commerce, House of Representatives, Washington, D.C.

DEAR REPRESENTATIVE MOSS: We have today been informed by Washington counsel that the Subcommittee on Commerce and Finance will be holding hearings on Monday, July 1, 1968 on the above legislation. Unfortunately, we will not be able to attend and would appreciate it if you would accept this communication as a statement of our views and have it entered as part of the official record of the hearings.

Johnson & Johnson has in excess of eighteen million shares of common stock outstanding, held by approximately thirteen thousand shareholders. Our shares are listed and traded on the New York Stock Exchange. The purpose of this letter is to present to the Subcommittee our qualified opposition to that portion of the legislation under consideration which seeks to regulate purchases by an issuer of its own shares.

We are generally in accord with the objectives of this legislation as enunciated during the Senate hearings on S. 510. We feel, however, that the legislation under consideration is much broader than necessary to accomplish these objectives. Specifically, there are three aspects which we feel go beyond what is needed: (1) the requirement for advance publication of corporate intentions; (2) the application of the legislation to every purchase no matter how small; and (3) the extension of coverage to persons other than the corporate issuer itself.

The various terms of pre-publication of the issuer's intention to purchase, as required by paragraph (e)(1) of S. 510, not only present problems in compliance, but also may operate to defeat the objective of insulation of the market price from the effects of the purchase. We suggest that, at least in some instances, such advance publicity may cause an increase in the market price. This in turn could affect corporate purchase plans and indeed prohibit accomplishment of the purchase without a further pre-publication. We suggest, except in instances where a substantial proportion of the outstanding shares is to be purchased, such advance publicity is just not necessary to accomplish the legislative objectives.

As to our second objection—the Bill's application to every corporate purchase no matter how small. The proposed legislation exempts from the other requirements of this Bill annual purchases of corporate securities in an amount not in excess of two per cent of outstanding shares. No such exemption, however, is applicable to purchases by the issuer. The legislative objectives do not require regulation of all purchases by an issuer no matter how small the amount. Without such an exemption, many companies, including ours, might be forced to abandon their practice of making small purchases at periodic intervals. Because of the expense and difficulties involved in compliance with legislation, corporations would of necessity have to make larger purchases at less frequent intervals. It is questionable whether this is desirable when viewed in light of its impact on an orderly market for the shares. In addition, this would present our company and others similarly situated with a difficult choice. The volume of trading of our shares on the New York Stock Exchange is comparatively small, considering the number of shares we have outstanding. For example,

during the last week of five-day trading on the New York Stock Exchange, the volume of our shares traded was just over fifteen thousand shares. Thus, any large purchases of shares by us on a single purchase basis could have an effect on the market price. Must we then abandon the practice of purchasing shares on the Exchange for our treasury for uses such as our employee benefit and stock option plans? Nor is it likely that we could find relief through private purchase of our securities. Any shareholders interested in selling could not be expected to maintain interest throughout the period required to prepare and publish information complying with the terms of this legislation.

As to our third concern—the extension of coverage to persons other than the corporate issuer. The scope of this extension is so broad that it would include purchases by the independent trustee under our issuer's pension plan, over whose investment decisions the issuer has no control, as well as purchases no matter how small by any person deemed for purposes of the Securities Exchange Act to be a controlling person. With regard to the independent trustee, the severe restrictions on the exercise of its discretion imposed by this legislation could well result in its decision not to purchase any of the issuer's shares, a situation which we do not believe would be either in the interests of the pension plan or of the corporate employees. With regard to the application of the legislation to a controlling person, the time and money required to comply with the legislative mandates would, we suggest, in effect prevent any future purchases of issuer's shares by such person.

I wish to thank you for the opportunity to submit our views and, in closing, let me strongly urge that your Subcommittee adopt an amendment to this legislation which would exempt annual purchases by an issuer, however defined, of an amount of shares not in excess of two per cent of the outstanding securities.

Very truly yours,

ARTHUR S. LANE.

Mr. COHEN. I am not familiar with that letter, Mr. Chairman, but I had heard that there was a telegram which had been received by the committee from another company and if the Chair wishes I can sort of respond to that off the top of my head.

Mr. WATKINS. Mr. Chairman, I would like to know who the other company is.

Mr. COHEN. American Home Products, I think. That telegram, as I recall it, suggested that it would be unwise to require the management of a company to be subject to the bill and in this regard they mean the reporting of information to the Commission with respect to repurchase by the company of its own shares; that is, at least up to the extent of 2 percent a year.

First of all, I think there may be some misconception unless I have not been properly informed as to the nature of the telegram. The provision of the statute which deals with that point as I understand it contains no prescription. It allows to the Commission authority to develop appropriate rules and in developing any rules as I indicated earlier, we do this by noticing a proposed rule so that we can get the comments from all persons concerned before we adopt a rule. It would be pretty much the same practice that we have engaged in under the proxy rules and, therefore, I do not see any problem that is raised by the American Home Products Co. that can't be adequately dealt with administratively.

Mr. WATKINS. Mr. Chairman.

Mr. MOSS. Mr. Watkins.

Mr. WATKINS. Mr. Cohen, if you have any information why don't you file that with the committee here and make it part of the record.

Mr. COHEN. I don't have the information. I just heard about this, Mr. Watkins.

Mr. WATKINS. Let's don't put in anything that we heard about. Let's make it part of the record.

Mr. COHEN. I don't have any document.

Mr. Moss. A copy has been directed to me from American Home Products Corp. If there is no objection the telegram will be included in the record at this point.

Mr. WATKINS. No objection.

Mr. Moss. With no objection the telegram is made a part of the record.

(The telegram referred to follows:)

[Telegram]

AMERICAN HOME PRODUCTS CORP.,
New York, N.Y., June 28, 1968.

Hon. JOHN E. MOSS,
Rayburn House Office Building,
Washington, D.C.:

Understand Subcommittee on Commerce and Finance has scheduled hearings on H.R. 14475, S. 510 and companion bills for Monday, July 1. As major listed corporation, find provisions which would require us to give advance disclosure of number of shares to be purchased and price to be paid therefore are totally unreasonable. They would have effect to setting a floor on market price and therefore would compel guaranteed market price fixing.

This seems contradictory of alleged antimanipulation purposes of legislation. Request you consider exempting from purview of proposed subsection issuer's purchase of own securities which do not in any 1 year exceed 2 percent of its then outstanding shares of class involved. Such provision already in subsections 13(d) and 13(f) of S. 510 and would remove our objections to proposed subsection 13(e) if such exemption incorporated therein. If this not possible, respectfully request opportunity on reasonable notice to testify or file statement opposing this legislation.

GILBERT S. MCINERNY,
Vice President and General Counsel, American Home Products Corp.

Mr. WATKINS. Mr. Chairman, I yield to Mr. Keith, if I have any time left.

Mr. KEITH. Mr. Chairman.

Mr. Moss. I will see that you have the time.

Mr. WATKINS. Thank you.

Mr. KEITH. Are there other witnesses that are going to appear and comment critically on the proposal that might speak to the point that is made by American Home Products Co.?

Mr. Moss. None requested to appear.

Mr. KEITH. I understood that Johnson & Johnson did not request to testify but just to put the information in the record.

Mr. WATKINS. If the gentleman will yield, Johnson & Johnson were unable to be here and asked that their statement be filed.

Mr. COHEN. If I may interpolate here, with the chairman's permission, we have not been aware of any opposition to the bill except from a couple of professors and I was not altogether sure whether opposition was the right word to describe their position. I think the bill has been supported by all segments of the securities business and representatives of industry generally. This point that was raised I thought I might advert to because I had heard about it. It may also be in the Johnson & Johnson letter. I think Phil Loomis can speak to it and give you the provision of the bill.

Mr. LOOMIS. I think both American Home Products and Johnson & Johnson are under the impression that the bill would require corporations to give advance public notice if they were going to purchase shares, stating how much, and what price. The bill does not so provide.

Mr. KEITH. It is a very short telegram, and perhaps you could speak more to the point if I read it, if I may, Mr. Chairman.

Mr. MOSS. You certainly may.

Mr. KEITH. This is from American Home Products.

(The text of the telegram read by Mr. Keith appears on p. 36.)

Mr. KEITH. Would you comment to the points they make?

Mr. COHEN. I think that was essentially what I heard. First, I should point out that that telegram is addressed to only one subsection in the bill.

No. 2, they want exemption for purchases by the company for up to 2 percent.

Now, I have this to say.

One, the bill does not require the information which they seem to suggest is required by the bill. The bill merely authorizes the Commission to adopt appropriate rules to deal with a number of problems, and that is one of them, to the extent that the Commission considered it appropriate.

That is the No. 1 item. Maybe it is inappropriate for me to deal with the merits of some such suggestions which may be the subject of rulemaking. Nevertheless, I think experience has shown that, with respect to some companies where the floating supply of securities is rather limited, the purchase of stock even up to 2 percent may have manipulative effects if as suggested in the telegram, with which apparently the writer agrees, the bill is designed to be antimanipulative. I think Mr. Loomis has something to add to that.

Mr. LOOMIS. The bill does not require advance notice of the price and incidentally the Continental Insurance Co. which is perhaps the largest casualty company in the United States has been engaged in purchasing its own shares over the last couple of years.

The New York Department of Insurance requires that they furnish a notice of their intentions. This has been done in each of the last 2 years and there has been no manipulative consequence.

Mr. COHEN. In fact, under the Investment Company Act with which you gentlemen are familiar, adopted in 1940, there is a specific requirement which relates to closed end companies essentially that at least

6 months before the company proposes to engage in these activities, I think it is 6 months, there be some notice to shareholders. This has never been viewed as manipulative. Actually, these are designed to be antimanipulative because of the exposure to daylight of the intentions of various parties.

Mr. KEITH. Would you tell me if there is any significance to the use of the treasury stock in attaining these objectives?

Mr. COHEN. No. I don't think the bill deals with treasury stock as such because the bill requires information with respect to the purchase of stock, outstanding stock. Stock held in the treasury I am not sure is affected by this bill or by any rules conceivably at the moment that the Commission might adopt under this particular section.

But I think your question is significant in the light of the point I made earlier that there are many companies that do hold a substantial amount of the outstanding shares in the treasury and in addition other people hold the shares so that the market is very thin. In such situations the acquisition of 1 percent, not talking in terms of a year, but the acquisition of a concentrated block of stock of 1 to 2 percent within a narrow period of time could have an effect.

I don't think anyone could predict without the context whether or not it is manipulative or nonmanipulative, but I want to emphasize that there is nothing in the bill that requires that disclosure in the case cited by the person that sent that telegram.

Mr. KEITH. I am not certain that I see the problem in the same way you do. I am completely unfamiliar with it except for this morning's discussion, but I would think that a company like American Home Products in the business of picking up smaller companies to increase their capability of serving the public with a larger inventory for the salesman to sell might be using their treasury stock to pick up smaller companies.

Mr. COHEN. That is true. That happens. Mr. Keith, as a matter of fact, but there is nothing in the bill here which affects that one way or another. It would be subject to the same requirements.

For example, if it was a stock for stock exchange, the issuance of treasury stock or newly issued stock would be subject to the registration and prospectus requirements of the Securities Act so that I don't see that anything in the bill affects that situation one way or another unless there is some aspect of it concerning which I cannot now address myself.

Mr. LOOMIS. Except if, as the House bill provides, such transaction is subject to the bill. Then solicitations by anyone for or against acceptance of such a treasury stock offering could not be false, misleading or deceptive.

Mr. COHEN. I guess I overstated the situation.

I think I understand the point now. Forgive me. It is not uncommon and the bill is directed to that. It was just the status of treasury stock on which I said the bill had no effect, but, quite often, we find companies faced with a takeover bid, or a worry that one was coming along, will attempt to buy up such available stock as they think may put them in a more strategic position with regard to any person who is engaged in a takeover.

Sometimes they will buy it directly and it becomes treasury stock, but that is just the legal status of it. Frequently the stock is put in the name of another entity so that the stock can be voted because in almost all States a company is prohibited from voting its treasury stock and this, too, is the subject of litigation from time to time.

Sometimes the stock is bought in friendly hands. It is the acquisition of the stock and its use in the contest that is dealt with in the bill, but its particular status, once the company acquires it, I think, is unimportant here.

Mr. KEITH. How much notice was given with reference to these hearings, Mr. Chairman, to the industry as such?

Mr. MOSS. I think that they have been anticipating the hearings for some time, and specifically this was probably sent out Wednesday or Thursday.

Mr. KEITH. Late last week. Apparently Johnson & Johnson is a Washington-based firm and should have expertise in this area. I wondered.

Mr. WATKINS. Would the gentleman yield?

Mr. KEITH. I yield.

Mr. WATKINS. I can say to you, Mr. Keith, that I think and agree with our chairman that they expected hearings on this bill, and to pass on the information that I have had from Johnson & Johnson and also with the permission of the chairman, I would like to add the name of Wyeth Laboratories in concurring, the information that I received from Mr. Elias as the vice president of the Wyeth Laboratories was that he concurs in the thinking of Johnson & Johnson's statement filed by counsel, Mr. Arthur S. Lane.

I would say that not in defense of anyone that they did anticipate hearings, but this was rather put to surprise.

I would perhaps concur with our chairman that we are drawing to the end, and if this is an important matter, perhaps it should be acted upon with more expediency than we intended. I don't like to protect John Moss.

Mr. KEITH. I would just like to ask if there is anybody here from Johnson & Johnson, American Home Products, or Wyeth International.

Mr. COHEN. There must be some coincidence. All three companies sell drug products. Maybe they are thinking of another committee or some other subject.

Mr. KEITH. I don't think so.

Mr. COHEN. I am kidding.

Mr. WATKINS. I think they are very much interested from the information I received.

Mr. COHEN. Seriously, Mr. Keith, in order to put your mind at rest, this matter has been the subject of discussion with the industry. I have discussed it with them—in fact, with most of industry—and I am talking about the securities industry, as well as industry generally, have felt that in this area this legislation is not only desirable, but it is essential and the sooner the better, and they have been aware of it for at least 3 or 4 years.

Mr. KEITH. I concur in your objectives, but if we can uncover a flaw——

Mr. COHEN. But there is none here because there is no requirement of the statute that deals with this problem.

Mr. KEITH. I am glad that in your view there is no flaw.

Mr. COHEN. I will cite you the section.

Mr. KEITH. Never mind.

Mr. WATKINS. Would the gentleman yield, because I judge you have the floor.

Mr. Cohen, that is a broad statement that there is no objection. I assure you that I shall have an amendment in the marking-up time of this bill to offer to the committee. I don't think you should speak for everybody. You speak for the SEC, and that is it. If you haven't talked to these other people, how can you express their views?

Mr. COHEN. With all due respect, Mr. Watkins.

Mr. WATKINS. How can you express the views of Johnson & Johnson or Wyeth Laboratories, if you haven't consulted with them?

Mr. COHEN. May I finish, Mr. Watkins?

Mr. WATKINS. Yes.

Mr. COHEN. I haven't consulted with each company separately, but I have spoken to the American Society of Corporate Secretaries and various other industry groups on this subject and the only thing that I have heard is in many cases that this bill is long overdue and should be adopted as promptly as possible.

Now as to a specific point of it, I can see that there may be differences of opinion, and undoubtedly there are some. I was only trying to tell Mr. Keith something I am sure he already knew anyway, that this has been exposed very widely to all industry and indeed this is not a Commission bill. This bill was suggested to the Congress by industry.

Mr. WATKINS. We are not denying that. No one has to cover for Mr. Moss, but I said that I knew that they were aware that there were going to be hearings, but it came quickly, and I can understand why the chairman perhaps is pressing it now.

But don't speak for these other people if you haven't talked to them because I shall offer an amendment to the committee in behalf of Wyeth and Johnson & Johnson.

Mr. COHEN. Mr. Chairman, do you have anything further you wish to ask me?

Mr. Moss. Mr. Stuckey.

Mr. STUCKEY. Mr. Chairman, how are you today?

Mr. COHEN. Fine, thank you.

Mr. STUCKEY. It is always good to have you before the committee.

I have two minor questions. Don't you have to disclose now if you have over 10 percent of the control of the stock?

Mr. COHEN. Yes, you do.

Mr. STUCKEY. That is what I thought.

Mr. COHEN. If you have over 10 percent.

Mr. STUCKEY. Could a person go out and under a street name purchase 9 percent and——

Mr. COHEN. The statute requires the disclosure of beneficial ownership. There have been a few situations, not many, in our knowledge where that has not been disclosed, but we have been able, I think, generally speaking, to catch up with them and require disclosure. The requirement is beneficial ownership and therefore holding the

shares in street name or any other nominee name is not any basis for exclusion from or exemption from the statute.

Mr. STUCKEY. But your interpretation would revolve around the term of what was beneficial?

Mr. COHEN. Yes, sir.

Mr. STUCKEY. So that a person could actually under a street name purchase 9 percent and go to another firm and purchase 9 percent?

Mr. COHEN. Under the present law he could, yes.

Mr. STUCKEY. Is that needed to be clarified in this bill?

Mr. COHEN. Up to 10 percent the present law doesn't require anything, but if he goes beyond 10 percent under the present law, he would be required to file a report with the Commission that he now owns more than 10 percent of the stock.

Mr. STUCKEY. But a person could get around it through this method, right?

Mr. COHEN. No, because beneficial ownership is the test. He might try to get around it, and that would be a violation of law, but the legal requirement is beneficial ownership.

Mr. STUCKEY. So it revolves around that?

Mr. COHEN. Yes, sir.

Mr. STUCKEY. Secondly, would there be any strong objections from the Commission as to the size of the corporation that this would apply to because I could see where this could be some type of handicap to a small firm.

Mr. COHEN. I think that perhaps when you are dealing with small firms, they might need more protection, talking about the shareholders, than a large firm because they don't have the financial or other resources to deal with some of the big fellows that come along and try to gobble up some of the smaller firms.

So that, if you had to make a judgment, it seems to me that you need the protection more there than with the big firms that have all the sophisticated counsel and finance that are necessary in this form of industrial warfare.

My position is that all shareholders, whether in small or large or medium-sized companies, need this protection.

Mr. STUCKEY. So you all would have objections?

Mr. COHEN. Yes, sir.

Mr. LOOMIS. Could I add that this bill applies only to shares which are registered under the Exchange Act so that the really small companies are not subject to it.

Mr. COHEN. These are companies with a public interest. That is made clear in the statute.

Mr. STUCKEY. One final question: Do you think that 5 days is sufficient time?

Mr. COHEN. Well, actually I said earlier, Mr. Stuckey, that under our proxy rules which have evolved over a considerable period of time and with the assistance of industry and the bar associations and such, we now have a requirement that material be filed with the Commission 10 days before it is to be released, but we also provide that that period can be shortened by the Commission and we frequently do where that seems to be important and particularly in proxy contests we frequently will clear material filed in the morning within 2 hours

after it is filed so that no one can get an advantage because of the fact that some of our people may not be moving as rapidly as possible.

Mr. STUCKEY. I am not talking about the time necessary for the Commission. I am talking about the public at large.

Mr. COHEN. Oh, the public, no, there is nothing in the statute which limits the public examination of the situation to 5 days.

Mr. STUCKEY. I am saying: Do you think 5 days is sufficient time for them to be completely aware and in a sense educated as to what is involved in one company making a tender to another?

Mr. COHEN. Based on experience in the past couple of years I would say no, Mr. Stuckey.

Mr. STUCKEY. This has been my concern, that the 5 days seems rather short.

Mr. COHEN. We have seen situations and in fact I testified in the Senate about one particular smaller company that was involved in five takeovers coming along at different periods, and the shareholders didn't have the information and 5 days would have made it impossible.

Mr. STUCKEY. For the protection of the public, if we are going to get a bill through similar to the one that we have before us, would not the Commission favor, say, instead of 5 days, to say 5 trading days or 10 days?

Mr. COHEN. There is no such provision in the bill.

Mr. STUCKEY. I know that. That is the reason I am asking the question. Would this not be more beneficial to the public at large to have more time?

Mr. LOOMIS. There is no limitation in the bill of the time to 5 days for the public to consider the tender offer. In our view they do need more than the 10-day provision that is in the Senate bill.

Mr. STUCKEY. That is what I am saying.

Mr. COHEN. I have to explain about that. That 10-day provision that is in the Senate bill relates to revocation of deposits pursuant to tenders, pro rata arrangements and similar matters. As I testified in the Senate, we objected to that provision because we did not think that it was protective of the investor. It might be protective of one of the parties but, after all, our interest here is the investor. We are not trying to seek to help one or the other parties to the contest.

I am sorry I didn't understand the purport of your question earlier. We would be against any such limitation.

Mr. STUCKEY. No further questions.

Thank you, Mr. Chairman.

Mr. Moss. Are there any further questions?

If not, gentlemen, I want to thank you for your appearance here this morning.

Our next witness will be Mr. Donald L. Calvin, vice president of the New York Stock Exchange. He will be accompanied by Mr. Phillip West, vice president and director of the department of stock list.

STATEMENT OF DONALD L. CALVIN, VICE PRESIDENT, NEW YORK STOCK EXCHANGE; ACCOMPANIED BY PHILLIP WEST, VICE PRESIDENT AND DIRECTOR, DEPARTMENT OF STOCK LIST

Mr. CALVIN. Thank you, Mr. Chairman.

We at the New York Stock Exchange appreciate the opportunity to appear here this morning. What I plan to do, with your permission, is to read a brief, prepared statement and then answer any questions you might have. We also would be willing to attempt to answer any questions that you have as we go through the prepared statement.

I might take a moment and introduce Mr. Phillip West, a vice president of the exchange and the director of its department of stock list.

His function among other things, is to supervise and to administer the policies of the New York Stock Exchange relating to the activities of companies whose shares are listed on the exchange. He has great familiarity with this area.

I would also say, before I get into the statement, that we agree with Chairman Cohen in what he said this morning. There is a great need for this legislation, and the New York Stock Exchange and other organizations in the securities industry have supported the objectives of this legislation. I am sorry that more of them aren't here this morning, but I would mention that in the Senate hearings the New York Stock Exchange was joined in supporting the legislation by the American Stock Exchange, the Investment Bankers Association of America, and the National Association of Securities Dealers, Inc.

The problem that we have is basically with two provisions in the House bill. I will now begin reading our statement.

The exchange supports S. 510 but opposes H.R. 14475, because it contains provisions which would be disruptive to market practices which have been demonstrated to be in the public interest.

In our view, the primary objectives to be accomplished by this legislation are to provide full and fair disclosure to shareholders—

(1) In connection with cash tender offers or through open market or privately negotiated purchases; and

(2) When a corporation repurchases its own equity securities.

The exchange has followed the development of this legislation since the first bill in this area was introduced by Senator Harrison Williams, in the last session of the 89th Congress. We have supported the objectives of these bills from the outset. A number of suggestions that we made as to specific provisions of S. 510, in the extensive hearings before the Senate Banking and Currency Committee in March 1967, are now incorporated in S. 510 as passed by the Senate.

The New York Stock Exchange has had policies regarding tender offers for almost 14 years. Because of the absence of any Federal legislation, the exchange has been the only regulatory authority active in this area. A number of witnesses at the Senate committee hearings testified and endorsed the exchange procedures.

Our analysis of H.R. 14475 is that it is basically the same as S. 510 as prior to amendments by the Senate Banking and Currency Committee.

Parenthetically, I would say, after reading this sentence again, it is not totally accurate. There were changes made in H.R. 14475 that paralleled many of the changes that were made in S. 510, as amended. We are really talking about the two provisions that we will get to in a minute.

These amendments were adopted after hearings on the bill in March 1967. The amendments removed features which the hearings showed to be highly objectionable.

The two major differences between the two bills are: one, the timing of the filing with the SEC; and two, the period for pro rata acceptance of tender offers.

1. Timing of filing with the SEC

Both bills require that a statement disclosing pertinent information be filed with the SEC, an objective with which the exchange agrees. S. 510 requires that the statement be on file with the SEC at the time the tender offer is announced to the public. H.R. 14475 would require the filing on a confidential basis with the SEC 5 days prior to public announcement.

Some background on how tender offers are conducted is important to explain the problems created by the 5-day advance filing requirement. Tender offers are invitations to shareholders to sell all or part of their shares at a price which is usually substantially above current market levels. Corporate management is bypassed, and shareholders are asked directly to sell their shares to the offeror.

The course of a typical tender offer is somewhat as follows:

(1) The offeror makes a public announcement that it is willing to purchase a specified number of a company's shares at a price above the current market.

(2) The offer is open for a specific period, usually 10 days or more.

(3) The offer usually requires that the shares must be irrevocably deposited by the specific expiration date.

(4) The offeror is not obligated to purchase any shares, if the number sought is not received.

(5) If more shares are received, the offeror need not purchase the excess.

(6) Some offers provide that the period may be extended. If so, the shares previously tendered are still irrevocably deposited.

Obviously, a company intending to make a tender offer strives to keep its plan secret. If word of the impending offer becomes public, the price of the stock will rise toward the expected tender price. Thus, the primary inducement to stockholders—an offer to purchase their shares at an attractive price above the market—is lost, and the offeror may be forced to abandon its plans or to raise the offer to a still higher price. The cost of an offer to purchase hundreds of thousands of shares might prove prohibitive if the price had to be increased only a few dollars per share.

A legislative requirement that increases the chance of premature disclosure of an impending offer can only serve to discourage the use of tender offers. These offers may be of great benefit both to the shareholders whose stock is being sought, and those of the company making the offer.

To insure secrecy and avoid leaks and rumors, and because t relationship between the tender price and the market price is

critical, tender offers are normally made to shareholders immediately after a decision to make the offer is reached and a price has been determined. In spite of all precautions, there have been cases where tender offers have been preceded by leaks and rumors, which caused abnormal market problems. We believe the 5-day prefiling requirement will lead to the premature disclosure of impending tender offers and, therefore, result in market disruptions. We base our opinion on our experience with tender offers and our related market surveillance.

I would add, at this point that, if the committee would like, at the conclusion of this statement, Mr. West can recite some examples of where market disruptions have occurred in comparable situations.

Let us examine some practical problems which would result from this 5-day advance filing requirement. Suppose a company listed on our exchange wishes to acquire 10 percent or more of another listed company's stock by a tender offer. Its board of directors must authorize the filing of the advance statement with the SEC.

Presently, under the disclosure policy of the exchange, the company should make a public announcement of its intention as soon as the board of directors has acted. In order to maintain a market fair to all investors, the exchange can then temporarily halt trading in the stocks concerned, pending a public announcement of the offer. If, however, the prefiling requirement in the House bill is enacted a company would be prohibited from providing this information to the public, since to do so prior to the expiration of the 5-day period would be a violation of the Securities Exchange Act of 1934.

Since the advance statement must be held in confidence by the SEC, the Commission would paradoxically prohibit a public announcement informing shareholders that within a few days there may be an offer to purchase their shares at a price in excess of the current market. This would work to the disadvantage of investors.

For example, a small shareholder anywhere in the country may decide to sell 100 shares of his stock on the fourth day after a statement is filed with the SEC. The next day the tender offer is announced at a price of $7 a share above where this small investor sold his stock. His shares were sold for $700 less than he would have received as a result of the offer. Thus, because of the prefiling requirement, the shareholder is prevented for 5-days from learning of the desire of another to buy his stock at a premium.

In some situations, insiders having the benefit of advance information during the 5-day period could take advantage of shareholders who sell their shares unaware of the impending offer.

No matter how diligent a company may be, it cannot guarantee that news of its approaching offer will be held in confidence for 5-days. We cannot escape the fact that people talk. Their motives may be innocent. Nonetheless, purchases by persons knowing of the imminent tender offer might drive the price of the stock up to the tender price. This could have the effect of forcing the abandonment of a tender offer which would have been beneficial to shareholders.

During these 5 days, market activity would be taking place while the SEC was reviewing the information statement. The SEC could accelerate its review. Nevertheless, it would have to accelerate in every

case to avoid the basic unfairness to shareholders. Therefore, the only fair approach from an investor's standpoint is immediate disclosure as is required in S. 510. Otherwise, the public's receipt of important information would be delayed to its detriment and legitmate market offers would be unduly impeded. And both results would be in direct conflict with the stated objectives of the bill.

Trading is normally halted in a stock where there are rumors linked to a tender offer. If the 5-day provision in the House bill became the law, the exchange might be forced to halt trading in the stock for the period during which the SEC was conducting its confidential review of the information statement.

The exchange would be in the anomalous position of having to halt trading due to market disruptions occasioned in large part by the operation of a law designed to provide full disclosure to investors. Thus a law and the enforcing agency could operate contrary to the best interests of shareholders.

The prefiling proposal might also provide an opportunity for market manipulations. An information statement might be filed solely to provide the basis for rumors of an impending offer for a company, without any intention of making the offer. The price manipulation could then take place, and it would be difficult, if not impossible, to prove that such manipulation was intended.

For these reasons, the exchange endorses section 2 of S. 510, which provides that an information statement containing the provisions now itemized in both bills be filed with the SEC at the time a tender offer is publicly announced.

Further, S. 510 permits a shareholder to withdraw any shares he has tendered within 7 days after commencement of an offer. Thus, the bill gives a shareholder 7 days in which to become familiar with the information in the statement, or to be informed of any SEC action which might convince him to withdraw his shares.

I would like to speak to that provision for a moment, if I may, Mr. Chairman. That provision of the bill, as we understand it, provides that if I tender my shares in response to an offer, and then some development occurs, or I have a change of heart, or some greater disclosure is made, I may still withdraw those shares during the 7-day period.

In other words, I am not committed during that period of time.

We think this is an important safety valve that is in both bills. And it is particularly important if you adopt the S. 510 approach, and have immediate disclosure, because it still gives shareholders tendering their shares 7 days to decide whether they want to make this an irrevocable act on their part.

It also gives the SEC time to examine these statements and, if additional disclosure is required, they can have this disseminated and shareholders can act in response to that.

Mr. STUCKEY. May I ask a question, Mr. Chairman?

Mr. MOSS. You certainly may, Mr. Stuckey.

Mr. STUCKEY. Let us say that Company A makes a tender offer t Company B, at $10 above the market price, and they can put their stoc up and take it out within the 7 days, right?

Mr. CALVIN. Yes.

Mr. STUCKEY. All right. What if Company C comes in and makes an offer to Company B, knowing that within the 7 days they can take it out at $11 a share, and a lot of this is happening now. Actually you could encourage bidding among companies trying to take over Company B.

In this I think you are getting yourself into a lot of trouble because we have a problem with it now.

Mr. CALVIN. I think it is written into the bills now that if there is a subsequent offer, the 7-day provision begins to run again. I think that is the way the bill is drafted now.

Mr. STUCKEY. Say that one more time.

Mr. CALVIN. In other words, if there is a subsequent offer at a higher price, then the 7-day provision, the right of withdrawal during the 7 days, runs again. They are not committed after the expiration of the first 7 days. This is, in effect, a new offer.

Mr. STUCKEY. I know, but I am saying that this is what you are encouraging, and I think this is something we ought to get away from.

Mr. CALVIN. What we are interested in here is that shareholders have ample time to make an informed decision. That is the reason for the 7 days.

Mr. STUCKEY. I am for the same thing, but I am still saying, let's say that the person has 5 or 6 or 7 or 10 days to know of the offer and you will never stop the rumors. In fact, it is probably better that you can't, but let's say a person does have notice of an offer. He puts his stock up, and another company says, "Look, for $1 more we can take it away from him."

So that really you are encouraging this because they know that within that 10 days they can pull out their stock and take the higher offer.

Mr. CALVIN. That is true.

Mr. Moss. Does Mr. West want to comment?

Mr. WEST. We think competition is the life of trade, and if they want to increase it, let them do it. It is a healthy thing.

Mr. CALVIN. We did object to one thing on the Senate side. It was a proposal that the tender be revocable during the whole period of the offer. In other words, if it was made to run for 60 days, any shares deposited could be withdrawn during that whole period.

We objected to that because it would lead to the point I think you are making, total uncertainty and no commitment at all. We thought the 7-day requirement was a realistic one and a reasonable period of time for people to become informed.

Mr. STUCKEY. Would it be in order to ask the Chairman of the SEC to comment on some of this at this time?

Mr. Moss. Without objection.

Mr. KEITH. I have no objection.

Mr. WATKINS. I have no objection.

Mr. Moss. Mr. Cohen, would you respond to this?

FURTHER STATEMENT OF HON. MANUEL F. COHEN

Mr. COHEN. I would be glad to.

We think that competition is the life of trade, too. We don't always
d that statement coming from the industry, but I have to admit that
believe in that very, very firmly.

In this particular situation we are troubled with the Senate bill for the following reason. We had urged that the deposit be revocable, as Mr. Calvin indicated, for a substantial period of time, for a number of reasons, including those Mr. Stuckey pointed out. This goes to another point, and I will deal with it, if you wish.

The rumors with regard to the possibilities become rife long before anything happens and there are situations where people, knowing that negotiations are going on between two parties, will run in with a bid in the hope that, under this bill, for example, if the 7 days expire, they have an automatic profit because when the other fellow comes in they pick up the shares deposited even though the other fellow is offering twice as much. It doesn't even require going to the bank to make a profit. That has happened.

That is why we felt that it ought to be open because the shareholder is the fellow who is caught. That is why we think the 10-day period also compels people to rush and deposit before they have the benefit of information with regard to competing offers.

The history in this area has been that there have been competing offers and it is more so all the time. On this problem about rumors, as I indicated earlier, many offers are made by stock for stock exchanges, which are subject to registration under the Securities Act.

They have to file a registration statement at least 20 days before it becomes effective. The price is usually determined the day before effectiveness in the ordinary offering.

I think Mr. Stuckey is right. The sooner there is information about a prospective offer, the better, but that doesn't mean that they couldn't submit the information to us ahead of time even without the price as they do in registration and proxy statements today and in many other areas of the Commission's work.

We have enough flexibility to allow them to come in at the very last second with the price. We have permitted them to put the price in the material after they file it with us. I don't see any problem here. But we are seriously concerned that these things would work to the disadvantage of the investor rather than to his advantage.

I must say that I am sure my colleagues on both sides of me (Mr. Calvin and Mr. West of the New York Stock Exchange) believe just as firmly and sincerely that the 10-day limitation is in the best interests of the shareholders. I don't think they have any other motive. There is just a difference in our experience and attitude toward what is in fact possibly in the best interests of the investor.

Mr. STUCKEY. This also could work a disadvantage to the corporation making the tender.

Mr. COHEN. That is exactly right. This is exactly why we want to keep this bill completely free of any influence by the Government or otherwise or by action of the Congress so that the forces in contention can have full play. Anybody who feels he would like to make an offer can do so with full information and the shareholder will have a fair opportunity to consider them all and to arrive at an informed decision.

As it is right now, and as it may be under this bill in this respect, the poor shareholder may become a pawn. That is what we are worried about, I am sorry.

Mr. STUCKEY. Thank you, sir.

Mr. Moss. Thank you, Mr. Cohen.

Mr. CALVIN. May I make one very brief comment?

Mr. Moss. Certainly.

Mr. CALVIN. We agree with Chairman Cohen, obviously, that there is a need for the legislation. We have an honest disagreement as to approach. In our experience—and Phil West has been with the New York Stock Exchange for 40-some years, and has been head of the Department of Stock List and active in this area for most of that time—you have to have immediate disclosure. This is basic. This is a cardinal principle of the New York Stock Exhcange. Even though the price was not filled in in the information statement, if the word got out that it had been filed, everyone knows it is going to be at a higher price than the current market. Whether it is $2 more or $5 more is not going to be that important. They know it is going to be more.

What we want and what we are interested in is in the Senate bill. It is in accord with our basic disclosure philosophy.

With that, I will continue with the statement.

Mr. COHEN. Mr. Chairman, may I interrupt?

Mr. Moss. If there is no objection.

Mr. COHEN. If it is merely disclosing that they have filed something with the Commission, we would certainly have no objection to that.

Mr. CALVIN. But that isn't the problem. I say that it isn't sufficient to disclose the filing. You will know that these people cannot act in response to the offer. They know that it is going to be at a price higher than the current market price. The only thing to do is make the offer immediately, and file with the SEC at that time.

That is our disagreement. I think it is obvious to the committee.

If I may go on, Mr. Chairman.

Mr. Moss. Certainly you may.

STATEMENT OF DONALD L. CALVIN—Resumed

Mr. CALVIN. In addition, all statements filed with the SEC would be subject to current provisions of State and Federal securities laws, which would protect those shareholders whose shares are being solicited by a tender offer from fraudulent and deceptive practices. These penalties should, in our opinion, normally be sufficient to insure that the information statements filed with the SEC will be accurate and complete in the first instance.

2. Period for pro rata acceptance of tender offers

Another of the exchange's suggestions to the Senate Banking and Currency Committee was that the period during which an offeror was required to prorate his acceptance should be limited to 10 days. This requirement was adopted and is now incorporated in S. 510, H.R. 14475, however, requires that the offeror must purchase on a pro rata basis for the full period of the offer. I would add, in the interests of full disclosure, it does give the Commission rulemaking authority, as pointed out this morning. We urge the subcommittee to adopt the limitation embodied in section 2 of S. 510, requiring pro rata acceptance of shares offered for the first 10 days of the offer period.

Some pro rata period is essential to permit shareholders to consider the offer and still have time to tender their shares.

A lengthy pro rata period works to the disadvantage of both the offeror and the tendering shareholder. The offeror cannot determine the percentage of shares which will be accepted. The tendering shareholder's entire holdings may be "locked in" for months only to have a major portion returned at the end of the pro rata period.

In other words, there is no certainty for either side. Our argument is that you have to cut it off at some point in time.

We believe that a combination of a 10-day pro rata period, followed by a first-come first-served period, is fair to all concerned. This has been the policy of the exchange which has stood the test of time in practical use.

Under this method, the original offer provides that if the number of shares tendered during the 10-day pro rata period is fewer than the number sought, shares will be purchased thereafter in the order in which they are received.

Market disruptions would also be more likely under a requirement that all tender offers must be made on a pro rata basis for the entire period.

Had there been such a requirement in the past, it would have increased both the length of tender offers and the time in which large blocks of stock would have been tied up. Withdrawing a sizable amount of a company's outstanding securities from the market for an extended period can drastically reduce the supply of stock available for trading. A limited supply of stock can produce abnormal price fluctuations.

We believe that the minimum 10-day pro rata procedure, as provided in S. 510, is fair to all concerned, while the unlimited pro rata period in H.R. 14475 will work to the detriment of the investing public.

In conclusion, the exchange supports S. 510 but opposes H.R. 14475.

Again for these two basic reasons: Accordingly we suggest that the committee report out S. 510.

Thank you, Mr. Chairman.

Mr. Moss. Mr. Keith.

Mr. KEITH. Suppose that we go along with H.R. 14475. Would you rather have no bill than H.R. 14475?

Mr. CALVIN. May I give you my opinion first. That is a tough question because there is a need for legislation in this area. I would say, however, that we feel that the 5-day advance filing period is going to be very, very disruptive to the maintenance of a fair and orderly market. For that reason, we would rather have no bill at this time, and then try to get a bill that we think is workable. S. 510 provides for the 10-day pro rata period that we think is a workable procedure and that we have had for years. We think everyone agrees that it should not be pro rata for the whole period of the offering. The SEC does have rulemaking authority in the provision in H.R. 14475, but we think that some degree of certainty would be more desirable, like the S. 510 provision. But our problem with H.R. 14475 is basically the 5 days' advance filing with the SEC.

Mr. KEITH. So that in the absence of compromise you would settle if you got one of your two objectives.

Mr. WEST. I think so.

Mr. KEITH. Particularly if you get the 5-day provision.

Mr. CALVIN. Yes.

Mr. KEITH. Now, Mr. Cohen.

Mr. COHEN. I testified this morning that although we think that is wrong the legislation is important and, if this committee decided in its wisdom to adopt S. 510, we would do our darndest to make it work. Therefore, we would not interpose any objection. But I do want to point to one thing that I think was probably not intended, which is an inconsistency. Mr. Calvin suggested that having this pro rata situation for a longer period of time can have an effect on the market because stock would be locked up so to speak. I think those are the words.

Well, if a tender can be revocable at all times it is not locked up and if the market price adjusts, as it does, the shareholder will have a choice whether or not he wants to wait until the end of the tender period or sell, whereas with the provision that after 10 days you are locked up there is no question about it that the offeror can keep that stock locked up and not available to the market for as long as his underlying provision permits him to.

In other words, he says, "I will make an offer for 30 or 60 days with the right to extend it," and he could look it up for months.

Mr. STUCKEY. Would the gentleman yield.

Mr. KEITH. Certainly.

Mr. STUCKEY. While I think your responsibility goes to protect the investor I think you are really putting a heck of a hardship on a corporation under the assumption of even 20 or 30 days.

Mr. COHEN. Not on the corporation. The problem would be on the offeror if there is one.

Mr. STUCKEY. However, you want to put it. If he makes a tender and does not have some cutoff point then he does not know whether he has the stock to go ahead with it or not and it puts him in a bad situation and you are talking about some price fluctuations. In fact, I would love for someone to make an offer every 30 days for our corporation with no intention of purchasing it because I can assure you I would benefit from it or know how to.

Mr. COHEN. I suppose the fellow who did it for that purpose would probably wind up in some jail.

Mr. STUCKEY. What I am saying is we are leaving this open for this to happen.

Mr. COHEN. No, sir. I don't quite agree. As I indicated earlier, and this deals with both points, and I want to repeat what I said earlier, many more offers are made by stock for stock exchanges which require the filing of a registration statement with the Commission.

Mr. STUCKEY. And you have 20 days.

Mr. COHEN. That is right, and sometimes a little longer unfortunately. Then the offer is out for a specified period which is specified in the prospectus. During the first 20-day period no price is fixed at all in the sense that the terms of the security are not firmed up. Usually it is fixed at the very end of the 20-day period.

I don't see the distinction between the cash tender offer and the stock for stock exchange offer and yet the rules are different. Nor do I see that the situation of the company or the offeror, or, say, proxy contestant is different than exists in the proxy contest. You are getting votes and you do get proxies but you don't know how many have been rejected or torn up or replaced by later dated proxies given

to others. This is a facet of this type of industrial warfare. Really it is the hard economic facts which make them possible. They see what the market is and what the price is and they know pretty well what is going on if they have the information necessary to arrive at a judgment.

I don't think that is that kind of problem. I want to emphasize that this is not a problem for the company. If it is a problem, it is for the offeror, and, therefore, I sympathize with any proposal which would equalize that situation. But, I think that, in trying to take care of either the company or the offeror, we have to remember that the exercise here is to protect the investor. I used the word pawn. Maybe that was injudicious but he does become the person to which this whole game is directed and he is the one who should have a fair opportunity to make a choice.

Mr. STUCKEY. Mr. Chairman, I think we are doing this but I also think we have an obligation to the corporations of the United States.

Mr. COHEN. I could not agree with that more.

Mr. STUCKEY. I think that really we could be working with a long extension of time to where it works to a disadvantage to the person making the offer, the tender.

Mr. COHEN. I think there is a cutoff point of 60 days in any event.

Mr. STUCKEY. I think with 60 days you have some problems but this is just a matter of opinion.

Mr. COHEN. I don't want to belabor the point but I want to reemphasize as I stated at the very beginning that although we have some difficulties with the Senate bill the legislation is important from the point of view of the investor that if the committee decided to adopt S. 510 in lieu of H.R. 14475, and there is one change that I understand no one has objected to and that relates to the closed end investment company which was an inadvertence, certainly there would be no problem from the Commission.

Mr. MOSS. Mr. Keith would like to have your views, Mr. West.

Mr. WEST. I think we should keep in mind that this bill is intended to cover in principle cash tender offers, not exchanges of securities that might take place and be registered under the 1933 act, although there is a provision here to cover that as well. With a cash tender offer that means we are talking in terms of millions of dollars—that the corporation, or whoever is making this tender offer, must be prepared to put up that cash, because it is a firm commitment. And since it is a cash tender offer, the regulations will be fairly simple under the circumstances. I feel certain that any corporation that is going to make a cash tender offer will have the regulation of the Commission very much in mind when it puts out an announcement. The only thing we are speaking of is this 5-day confidential treatment, you might say, which, undoubtedly, if it passes, is going to have an effect on the market. Therefore, since all that represents is the possibility of embarrassment, as Chairman Cohen indicated, to the company making the cash tender offer—the Commission has to go after him because he did not disclose something—I think that immediate publicity of the tender offer is preferable to any embarrassment to the person making the offer. With the registration under the 1933 act, in practically every offer that I have seen, the terms of the exchange offer have been publicly stated before any registration statement is filed with the Commission, so that the public is on notice. And it has been disclosed what

is intended to be, and what effect it possibly might have on the market, so that under these circumstances the market can continue, and there is no necessity of holding up trading even for a temporary period of time.

I think this is the problem to which we are directing ourselves.

Mr. STUCKEY. Would the gentleman yield for one short time.

I think the two statements by Chairman Cohen and you, Mr. West, really clarify it because I think the past shows that we have not had any trouble with stock for stock offers.

Mr. COHEN. We have.

Mr. STUCKEY. Basically it has been fairly smooth.

Mr. COHEN. The reason for that is that there is an advance filing with the Commission and the materials are scrubbed up before they are actually used.

Mr. STUCKEY. But we are talking about two completely different situations, where with the cash for the stock offer we have had some problems, and I appreciated the two statements in bringing out the difference in basically what we are dealing with here. But basically over a period of time there has not really been too much of a problem as far as the SEC has been concerned with stock for stock.

Mr. COHEN. I think Mr. West at the very end really put his finger on it. We are not insisting on the 5-day provision because we want to have the first look at it. I think this business about rumors is beside the point. There always have been rumors and the clippings that the chairman introduced earlier today I think will make eminently clear that it is true today even when there is no SEC in the picture. I think that our concern really stems from our sensitivity that the Government should stay out of involvement in these contests as much as possible. We recognize that if materials are filed and we have to take exception to them this is embarrassing to the people who used them and, therefore, may interfere with an objective consideration of the merits by the shareholders. That is all that is involved.

If it is felt that the people who do these things should suffer whatever consequences flow from whatever they file, so be it. We just did not want the Commission to be in the position perhaps of compelling changes or going to court because once you do that no matter how well you qualify what you are doing it is going to be used by the other parties as an argument that "The Government is against you." This is the reason why the Commission hesitates, unless no other course is possible, to go to court on these situations. That is why in the present proxy rules which relate to as important matters as this, mergers, consolidations, reorganization and recapitulations which are very, very important from a dollar point of view to all investors, there is a requirement that material be filed with us before it goes to the public.

Mr. Moss. Mr. Keith.

Mr. KEITH. I would like to ask the triumvirate here just briefly the answers to these two questions. How often are these matters informally discussed with the SEC? Prior to their actually——

Mr. COHEN. When it is a stock for stock exchange offer it is always discussed with the SEC. In a cash tender offer there is no discussion. If it has happened, it has not come to my attention.

Mr. KEITH. The attorneys doing this kind of business.

Mr. Moss. Do either of the other gentlemen have a comment?

Mr. CALVIN. Would you like to hear Mr. West's reply?

Mr. WEST. Sometimes they discuss it with us on a confidential basis in the first instance because of the time period. This 10-day period, for instance, for pro rata, which we have absolutely insisted upon many of the offerors want to reduce that period, let's say, to 7 days because of the commitments they have. They want to know exactly where they stand and where their commitments will follow, and we have refused to accept that. With the 10-day period for the pro rata, this is relative. We found that, by and large, it gives everyone in the United States an opportunity, with our rapid means of communication today, to know about the offer and make a decision. Because we also go after the management of the company and say, "You must make a statement to your stockholders, and we feel you should notify them as well that this tender offer is present." And, therefore, the stockholder will have an indication from the other side of the picture, whether the management is willing to go along with this tender offer and feels it is good or whether they have something else in their mind and will make a statement and feel that the price is too low.

We feel this should be done and is fair to the security holder.

Mr. KEITH. Just a minute, Mr. Cohen. You almost made me forget what I was going to say. I think the point I was going to make is would you not under S. 510 have sufficient authority to cause considerable embarrassment to those involved in any violation of the spirit of the law which we are considering?

Mr. COHEN. After the event. Yes.

Mr. KEITH. They learn darn fast.

Mr. COHEN. Let me explain. I have to, Mr. Keith. You want a full answer, I know.

Let's assume there is a 10-day withdrawal period, and that we got the materials the very same day they were filed, and examined them. By the time we crank up this machinery to try to get them changed, the 10 days would have run and people are locked in and we don't have any power to compel people to unlock the door. But I don't want to belabor this. I think the point has been made well that the stock exchange does get the benefit of a 5-day prefiling period. I don't know what the objections are to the SEC getting it.

Mr. KEITH. I know what you would do. You would make a speech somewhere and scare them all and it would be taken care of.

Mr. COHEN. Mr. Keith, I know you mean that in jest because I never do that.

Mr. WEST. When they have seen us it has been the night before and we have pounded the table at 8 o'clock at night and the tender offer was made the next morning. So it was not a 5-day period or otherwise. It has been the problem purely of the period to be covered in this relationship and we felt stockholders should be served.

Mr. Moss. Mr. Stuckey.

Mr. STUCKEY. I think all my questions have been answered, Mr. Chairman, and I appreciate the remarks of Mr. Calvin and Mr. West and, of course, Chairman Cohen.

Mr. Moss. Mr. Watkins.

Mr. WATKINS. I have no questions, Mr. Chairman.

Mr. Moss. You quite obviously would like to make further ser vations and I think you are entitled to equal time.

Mr. CALVIN. Thank you, Mr. Chairman. I agree with the point of Mr. Keith's last question and this is what we at the exchange call moral suasion. If these people know that if they don't meet the requirements imposed by the Commission, they are going to have trouble with the Commission later, that might prove not only embarrassing but disastrous to this particular offer. They are going to do their utmost to see that they meet the requirements before they make the final decision and make the public announcement. I would like Mr. West to comment on delays in trading which is important throughout all of this and particularly if you do report out H.R. 14475. I would call on Mr. West for that.

Mr. Moss. Mr. West.

Mr. WEST. Chairman Moss, in the past year we have held up trading in 290 stocks in relation to important pending announcements. What we do is to advise companies that they should make immediate disclosure of any matter which affects security decisions or might affect security prices. And we urge them—prior to announcement, as soon as the board of directors has taken any action—that they call us on the phone at the same time they are releasing it to the news services, Dow Jones, and others, and let us know about it. When they do that we immediately call the floor. I have a direct line to the floor and I say "Stop trading in the XYZ stock pending a news announcement." If we hold up more than 20 minutes we send a notice over the tape that we have halted trading pending a news announcement because Dow Jones does not get it out as quickly as we would like because it comes from all over the country. We hold trading until the news announcement does appear on the broad tape, and wait at least 15 minutes, if not longer, to permit the price of the security to adjust the price before we commence trading again.

Then we have problems as well of leaks and rumors that may occur from time to time. In the recent takeover of Jones & Laughlin Steel we had to hold trading in J&L stock until an announcement could be made in relation to the price at which they were going to make the tender offer, because there were rumors. Because of those rumors of the tender offer, and it appeared from both sides that they were sitting down and discussing it, they could say that they were going to have an offer but could not give the price.

We thought there should be no trading on the exchange until they could announce the price, until investors could be informed. This meant holding trading for a day and a half, which in reality was a disservice to security holders, to take away their market for such a long period of time. We are trying to take steps to see that something like that does not happen in the future.

This is the first time we have had to hold it up that long. We have had to hold it up on occasion for 2 or 3 hours but not a day and a half.

We are going to do our best to keep that from happening. How, I don't know. This legislation will be very helpful, providing immediate publicity is given to a decision in these matters so that the public knows about it.

Mr. Moss. Mr. Calvin, do you have further comment?

Mr. CALVIN. No, I do not; just to thank you, Mr. Chairman, and members of the committee for your time and attention. I hope have stated the issues. I think you have seen them.

Mr. Moss. I think you have been very helpful and certainly demonstrated the facts, in the two areas of particular concern with emphasis on the one area of the disagreement between the texts of the Senate bill and of the bill which I offered, of the depth of your feeling and of your concern. I assure you the subcommittee will give most thoughtful consideration to those views when we mark up the bill which I hope will be at a very very early date. We would like to move. I also have a feeling of urgent need for one or the other of the bills. You have no adverse feeling at all toward the proposal in 14475 covering the closed end investment.

Mr. CALVIN. None at all.

Mr. Moss. You do not address yourself to that point of difference.

Mr. CALVIN. We have no problem with that at all.

Mr. Moss. The two that you have carefully defined for the committee constitute the only two areas of concern.

Mr. CALVIN. That is right. We have some problems with some other sections of the bill, but we are willing to waive those.

Mr. Moss. Thank you.

Mr. WEST. We might add that we thought the investment companies were covered under the original bill. I am sorry to admit that.

Mr. Moss. I believe Chairman Cohen has identified that as an inadvertence and I am confident that that was the case. I ask unanimous consent at this time that the record receive the communications addressed to the committee on this subject.

Is there objection? Hearing none, it will be so held and the committee is now adjourned.

(The following correspondence was subsequently submitted for the record:)

SECURITIES AND EXCHANGE COMMISSION,
Washington, D.C., June 18, 1968.

Hon. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: I am enclosing a staff report of our investigation into the unusual trading situation in Chicago and North Western Railway Company stock on August 7 and 8, 1967. As you will note, the report concludes that, although certain technical violations are attributable to the specialists in the stock, such activity was not the cause of the substantial price drop in the securities. We have sent the attached letter to the New York Stock Exchange, requesting the Exchange to take steps to insure that openings will be properly supervised, and, if necessary, delayed until an accurate and complete evaluation of the market is possible.

Sincerely,

MANUEL F. COHEN, *Chairman.*

MEMORANDUM PREPARED BY THE DIVISION OF TRADING AND MARKETS IN RESPONSE TO A COMMUNICATION FROM THE HONORABLE HARLEY O. STAGGERS

The Commission staff has completed its investigation into certain aspects of the trading in the securities of Chicago and North Western Railway Company on August 7 and 8, 1967. Briefly, the facts were as follows: on August 8, trading in the common and preferred[1] securities of Chicago and North Western Railway Company (C&NW) on the New York Stock Exchange (NYSE) was opened on the closing bell, down 39 points from the previous day's close; the specialists involved in this opening were ultimate net short-sellers of 1,900 shares. (Trading on Augus

[1] The preferred is convertible into the common on a share for share basis.

7 had been halted at 1:55 P.M. because of the heavy influx of orders following a news release that merger negotiations between C&NW and Essex Wire Corporation had been terminated.)

In the course of its inquiry, the Commission staff interviewed the specialists and Exchange Officials [2] directly concerned with this opening. Upon our request, the NYSE submitted a detailed report of its investigation into this situation. The Commission staff acquired copies of all market order slips left with the specialists on August 8, and a copy of the specialists' book at the time of the opening showing all limit orders left with the specialists for execution. (A limit order is an order to buy or sell a stated amount of a security at a specified price, or at a better price, if obtainable after the order is represented in the trading crowd.) There are no records of the condition of the specialists' book at any time other than 2:00 P.M.

ANALYSIS OF ORDERS AT THE DELAYED OPENING, AUGUST 8, 1967

Analysis of orders and the specialists' book shows that at the time of the 2:00 P.M. opening, the specialists had market orders to buy 21,400 shares and to sell 14,900 shares of common stock. In addition, the book showed that, up to a price of 150, limit orders to sell totaled 77,400 shares of common. Most of the limit orders to sell (58,800) were at 130 and above. Limit orders to buy on the book totaled 65,200 shares (common) down to a price of 108. The majority of the limit orders to buy, however, (49,800) were at 119¼ and below. Therefore, in order to utilize the limit buy orders on the book to support the price, the specialists would have had to open the stock below 120. If the stock had opened at 130 or above, the specialists could have been obligated to buy slightly more than 50,000 shares (net). Between the prices of 120 and 130, limit orders to buy at 120 and above totaled 15,400 shares, 6,600 of which were at 120. Limit orders to sell below 130 totaled 18,600, 12,200 of which were at a 125 limit. Thus, this placement of limit buy and sell orders indicates that the specialists would have been encouraged to open the stock below 125 in order to match as many buy and sell orders as possible, and to avoid the last of the large limit sell orders on the book (i.e., 12,200 at 125). Adding to the difficult situation in the common stock was a great imbalance in the limit orders in the convertible preferred (17,700 to sell; 100 to buy). The opening price of the preferred would be approximately the same as that of the common due to the share for share conversion ratio.

Exchange rules do not require any particular rate of specialist participation; specialists, however, are expected to maintain a fair and orderly market and not to participate when this would be detrimental to the market. The placement of the buy and sell limit orders, outlined above, created price levels which would have demanded an extraordinary investment by the specialists should they have opened above any of these levels. For example, the staff estimates that the specialists would have had to buy (market and limit orders of common and preferred combined) the following approximate amounts at the following prices: 125—approximately 23,000 shares ($2,875,000); 130—approximately 60,000 shares ($7,800,000); 135—approximately 72,000 shares ($9,720,000). Therefore, barring such an extraordinary investment on the part of the specialists, the placement of these orders indicates the probability of an opening below 125 and above 115. At these levels, the specialists could expect to more nearly match buy and sell orders and to participate as buyers for between 8,000 and 10,000 net, requiring an investment of approximately $1 million.

About a half-hour before the opening, a price range of 110 to 125 was circulated to the trading crowd; at this range, the specialists were to have been estimated buyers of up to approximately 10,000 shares. In response to this circulated price range, a great number of new orders was received (especially orders to buy), and some existing orders were altered (in particular a 10,700 share market order to sell was changed to a limit order at 130—in the confusion no one handling the book was aware of this change until *after* the opening had taken place). In other words, following the circulation of the price indications, the character of the market began changing rapidly from one with an excess of sell orders to one where buy orders predominated. Due to the confusion, however, no one in charge of the book was aware of the changing character of the market. It does not appear

[2] Although Floor Officials are responsible under NYSE rules for supervising Floor procedures, in practice Floor Governors participate in serious situations. The term "Exchange Officials" in this report refers both to Floor Officials and Floor Governors.

that Exchange Officials contemplated delaying the opening; on the contrary, all those interviewed indicated that they considered it imperative for each stock to be opened every day, if possible, and that a full day's delay for this opening, even with the prevailing confusion, would not have been appropriate.

Thus, in an atmosphere of considerable confusion, Exchange Officials allowed C&NW common and preferred to be offered at 120, relying on the "educated guess" of the specialists that they would be buyers. The specialists were ultimately made short-sellers on balance of 4,800 shares. Conversion of all of the preferred stock owned by specialists would have left them short a net 1,900 shares. It is the view of the Commission staff that this violation was technical in nature and based on inadequate information concerning the nature and amount of all of the orders at the time of the opening. In the opinion of the staff an exact count of these orders would not necessarily have materially changed the opening price; after-the-fact analysis shows that the short selling violation could have been avoided without a significant change in the investment projection of the specialists had the re-opening price of C&NW been 1 to 4 points higher.[3]

At present, Exchange Rule 47 allows Floor Officials to supervise and regulate active openings. Under Exchange Rule 79.30 transactions made at 2 points or more away from the last previous sale (for stocks selling at 120 or more) may not be published on the tape without the prior approval of a Floor Official. Since 1965 the Exchange has had a written policy which clearly outlines procedures to be followed at delayed openings. This policy requires that Floor Officials have an accurate count of all orders on the book and in the crowd before the opening may take place. The delayed opening form filled out for C&NW, supposedly to aid the Officials in obtaining a count, contains very little of the necessary information. (Interviews indicated that, according to standard practice, this form was not filled out until after the opening had taken place.) Had the Exchange Officials obtained the required count, they would have had knowledge that the opening would cause the specialists to commit a short-selling violation; the Officials, under such conditions, could not have permitted an opening to take place.

The Exchange Officials decided the opening would be held on the closing bell, even though the specialists testified that they would have preferred an opening which allowed them some time to trade, and even though the Officials knew by the time of the opening that it was impossible to obtain a count of orders and were relying on the specialists' "educated guess." Had an accurate count been obtained, Exchange Officials would have been faced with two choices: they could have changed the opening price, or they could have delayed the opening to the following day. Exchange Officials, however, allowed the opening to occur at 120 on the closing bell, estimating that the specialists would still be buyers of 10,000 shares at this price. Our analysis supports 120 as the best estimated price under the circumstances of the opening, barring an extraordinary investment on the part of the specialists. The specialists performed adequately according to what the Exchange asked of them. It is our view, however, that the opening should not have taken place under circumstances where it was not possible to determine the extent of the specialists' commitment. Indeed, in this case the estimate was incorrect and resulted in an inadvertent violation of the short selling rules. A delay to the following day would have clarified the situation, permitted a more careful evaluation of prices by the public and others, and in all probability, avoided a short selling violation.

---

[3] In its memorandum concerning this reopening, the Exchange stated that at an opening of 120⅛ the short selling violation would have been avoided. Our interviews with the specialists and Officials, however, revealed that a price of 120⅛ would never have been selected; securities of the price and volatility of C. & N.W. are characteristically traded in whole or half point differentials. One specialist indicated that he viewed this as a bit of hindsight technical analysis on the part of the Exchange; he stated that he would not have opened C. & N.W. at 120⅛ simply to avoid 6,600 shares of buy limit orders.

SECURITIES AND EXCHANGE COMMISSION,
Washington, D.C., June 26, 1968.

HON. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: Thank you for your letter of June 20 with further reference to the activity in the stock of Chicago and North Western Railway Company on August 7 and August 8, 1967.

Without expressing a conclusion as to whether anyone was guilty of improper conduct in the particular case, I agree with you that situations of this kind are extremely disturbing. The tremendous drop in the price of this stock dramatically illustrates the harm which could be done by inadequate or misleading disclosures with respect to mergers and takeover bids.

I also believe that existing controls in this area are inadequate. In the first place, it was held in *Mills* v. *Sarjem Corp.*, 133 F. Supp. 753 (D. N.J., 1955), that a person making a tender offer has no affirmative duty to disclose to the people from whom he is buying, material information known to him and unknown to them, this on the ground that a takeover bidder is not an "insider." In the second place, the law with respect to misleading corporate announcements is unsettled if, as is commonly the case, the corporation making the misleading announcement has not itself been trading in securities. A majority of the district courts which have considered the question have concluded that the antifraud provisions of the Securities Exchange Act do not apply because the misleading announcement was not issued "in connection with" trading in securities by the corporation. We believe that this is too narrow a construction and have taken that position in connection with appeals in three cases now pending in the Court of Appeals for the Second Circuit. It appears that the Court is having some difficulty with the question, since two of these cases were argued 15 months ago and are still undecided.

Enactment of S. 14475 or S. 510, both pending in your Committee, would result in a substantial improvement in this situation. These bills would impose certain affirmative duties of disclosure on the part of persons making takeover bids. They would also prohibit any person from making false or misleading statements or engaging in fraudulent, deceptive, or manipulative acts or practices in connection with tender offers, or solicitations for or against tender offers. This would resolve the existing unsettled state of the law in connection with corporate announcements in this field. I believe, and have testified in the Senate, that there is a need to correct the existing gap in investor protection in this area. Your letter illustrates the possible operation of this gap in a particular case.

Sincerely,

MANUEL F. COHEN, *Chairman.*

(The following material was submitted for the record:)

STATEMENT OF RALPH W. HEMMINGER,[1] REPRESENTING THE CHAMBER OF COMMERCE OF THE UNITED STATES

The Chamber of Commerce of the United States appreciates the privilege of presenting this statement to the Subcommittee on Commerce and Finance as its studies proposed amendments to the Securities Exchange Act of 1934. The National Chamber is the largest association of business and professional organizations in the United States, and is the principal spokesman for the American business community. The Chamber represents 3,700 trade associations and local chambers of commerce. It has a direct membership of over 33,000 business firms and an underlying membership of approximately 5 million individuals and firms.

This statement is directed solely to a discussion of one proposed subsection of the bill (H.R. 14475–S. 510). The bill contains a new subsection (e) to be added to Section 13 of the Securities Exchange Act of 1934. Paragraph (1) of new subsection (e) provides that it "shall be unlawful for an issuer, to purchase any equity security which it has issued 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 or in order to prevent such acts and practices as are fraudulent, deceptive, or manipulative." Paragraph (2) thereof, however, would define a purchase by the issuer of its own securities to include a purchase by "any bonus, profit sharing, pension, retirement, thrift, savings, incentive, stock purchase, or similar plan of the issuer."

[1] Ralph W. Hemminger, Senior Vice President of Bankers Trust Company of New York.

We oppose the inclusion of "any bonus, profit sharing, pension, retirement, thrift, savings, incentive, stock purchase, or similar plan of the issuer" in the new subsection (e) (2). This subsection was not included in the original Senate Bill (S. 510) and is not pertinent to the purposes of the bill.

This statement emphasizes the harmful effects of subsection (e) (2) on employee benefit plans and summarizes briefly some of the existing law that is already applicable. We recommend that the phrase "any bonus, profit sharing, pension, retirement, thrift, incentive, stock purchase, or similar plan of the issuer" be eliminated. If this phrase of the subsection is not eliminated, then we recommend that the Bill exclude from regulation by the Commission, through its rules or otherwise, the purchase of stock by employee benefit trusts by a trustee that is independent of the employer, such as a corporate trustee, and where the trustee performs the function of purchasing the stock at its discretion without any direction or instructions of the employer.

HARMFUL EFFECTS OF SUBSECTION (e) (2) ON EMPLOYEE BENEFIT PLANS

The Securities Exchange Commission has already drafted rules and regulations (Rule 10b–10) which it proposes to apply under this legislation. The indiscriminate application of such rules and regulations and the general application of private letter rulings, which the SEC has already issued without the authorization of Congress as set forth in S. 510, would interfere with the orderly accumulation of stock for employees in many profit sharing, savings and stock purchase plans. In addition, the rules and regulations could tend to increase the price of the stock paid by the employees and the price that a pension trust may have to pay for stock.

Employees savings plans best illustrate the harmful effects to which we refer. The employee savings plan is currently one of the fastest growing types of employee benefit plans. These savings plans are very popular with both union and non-union employees. The employer contributions have given employees a very real incentive to save and to accumulate funds which are available at retirement, or for disability, family emergencies, or death, and for other personal circumstances. This growing and valuable employee benefit is good for the employee, the employer and the economy.

The plans usually make available employer stock as one of the investments for the employes' account. Incidentally, if any employee contributions are invested in the employer stock the plan is registered with the SEC and the employee is periodically given a detailed prospectus.

It is estimated that savings and similar plans that make available employer stock as one investment medium cover over 3,000,000 employees. The employee funds and the company contributions are usually turned over to the trustee from time to time throughout each month and the purchase of the employer stock that is required is bought on a dollar averaging basis throughout the month. The price paid by an employee for his stock for the month is the average cost of all stock purchased during the month.

The effect of SEC's proposed rule 10b–10 and of SEC's private letter rulings on the savings plans used for this illustration is as follows:

1. The amount of employer's stock which a plan purchases in any week may not exceed 10% of average weekly volume in the four calendar weeks preceding the current week, and the amount of employer's stock purchased in one day may not exceed 15% of the average daily volume in the four calendar weeks preceding the current week. This is an undesirable arrangement, since it limits the stock that the trustee may purchase in two ways: both by the percentage rule applying to total purchases and by the amount of employer purchases.

2. In addition, all purchase orders of the employer and the trustee in any day must be placed with the same broker or dealer. This means that the trustee can lose control of the executions. It can deprive the trustee of the ability of supervising the buying of stock throughout the day and of using his discretion in an effort to obtain the stock at the best price for the trust. It also raises questions as to potential discrimination by the broker both as to amount and price in the allocation of shares to the employer and the trustee.

3. The price limitations in the proposed rules also create problems. The trustee should have discretion to purchase the required amount of stock at such price as he regards as reasonable. In a rising market, the proposed rules on price might prevent the trustee from buying any stock or, at least, reduce materially

ability to buy stock even when the employer is not buying stock. The trustee should not be limited to the last independent bid price or the last sales price.

4. If recent SEC private letter rulings are made applicable on a general basis, the trustee would not be permitted to buy when the employer is prohibited from buying employer stock. This could include periods in which mergers or acquisitions are being negotiated which involve the employer's stock, and periods in which the employer may be selling new stock or convertible securities. It is not to be expected that a trustee making its own independent investment decsision would be informed of the beginning of merger negotiations. It is not logical for such a trustee to suspend purchases for employees during such periods, which may be lengthy.

The above illustrates the effect of the proposed rules and regulations on savings plans. The effect in a profit sharing plan where the employer stock is purchased for an employee's account is similar. In a pension plan, the employer stock, when purchased, usually becomes part of the portfolio and stock is not bought for the account of individual employees but for all employees as a group. The proposed rules and regulations and the general application of the private letter rulings would actually prevent the trustees from performing their duty, which involves buying the employer's stock at such time, at such price and in such amounts as may operate to the greatest benefit of the trust beneficiaries.

EXISTING LAW AND REGULATIONS

We urge the Subcommittee to recognize that all qualified pension trusts, profit sharing trusts and savings plans trusts are true trusts. They involve a fiduciary relationship in which one person holds title to property subject to an equitable obligation to preserve and use the property for the benefit of other persons. It is not an ordinary business relationship, but a *fiduciary* relationship, in which the law charges the trustee with certain duties: to preserve the trust property and to make it productive, and to use such reasonable care as an ordinarily prudent man would in investing and reinvesting the trust property. The trustee's duty of loyalty is to the beneficiaries for whom he holds the property.

There is already an abundance of controls over these trusts. All qualified trusts are required to report the details of purchases of employer securities to the Internal Revenue Service. An improper purchase can result in the severe penalty of the loss of the tax exempt status of the trust. In addition, under the Welfare and Pension Plans Disclosure Act, the details of the purchase of employer securities must be reported and this information is available to the Secretary of Labor and the public. Furthermore, Congress is currently considering a Federal Fiduciary Responsibility Act for trustees under pension, profit sharing and other employee benefits plans (H.R. 5741 and S. 1024).

Underlying all this federal law is the common law of trusts. Under trust law, the loyalty of the trustee runs to the employees and their beneficiaries in these plans. Every transaction undertaken by the trustee must be measured in terms of this loyalty. Any trustee who acts improperly becomes personally liable. Obviously, no corporate trustee can afford the injury that would result to its reputation from improper or irregular acts in its capacity as trustee.

SUMMARY

In summary, the National Chamber recommends the elimination of the phrase, "any bonus, profit sharing, pension, retirement, thrift, incentive, stock purchase, or similar plan of the issuer" from Subsection (e)(2) of S. 510 and H.R. 14475. Alternatively, this subsection should be so modified as to exclude trustees that are independent of the employer, such as a corporate trustee, and where the trustee perfroms the function of purchasing the stock at his discretion without any direction or instructions of the employer.

The time limitations on this hearing did not afford us an opportunity to present oral testimony on this one subsection which has such serious implications. We will be happy to elaborate further if the Subcommittee desires additional information.

STATEMENT OF JORDAN H. ESKIN, ATTORNEY, NEW YORK, N.Y.

My name is Jordan H. Eskin. I am an attorney at law practicing in New York City. I have been the Chairman of the Stockholders' Committee for Better Management of the *Boston and Maine Corporation*, the securities of which are listed on the New York Stock Exchange. As such Chairman, I conducted a proxy contest with a number of other persons to secure control of the Boston and Maine Corporation ("B&M") at the April 1966 annual meeting, at which time the Committee's nominees received approximately 46% of the vote cast. At the April 1967 meeting the Committee solicited proxies to prevent management from securing a quorum and to stop the election of management's nominees and for a period of almost one week management was unable to secure a quorum. By February of 1968 half of the Board of Directors of B&M was chosen by me and persons friendly to me.

I am making this statement after having experienced two proxy contests and with knowledge of why they are conducted and the problems involved. I have the scars to prove it.

Before your Committee for consideration is S. 510 which deals with three areas or types of transactions:

I. Where any person acquires or obtains the right to acquire beneficial ownership of 10% or more of any class of equity securities registered under the Securities Exchange Act of 1934. [Section 1 adding new subsections (1)–(4) inclusive to Section 13 of that Act.]

II. Where an issuer proposes to make purchases of its own registered equity securities [Section (1) adding new subsection (5) to Section 13 of the Act]; and

III. So-called "Tender Offers" [Section 2, adding new subsections (1)–(7) to Section 14 of the Act.]

I intend to deal only with Area I. There have been many spokesmen who have discussed the other facets of the proposed legislation. I discuss Area I because it contains the provisions that relate to acquisitions of stock on the open market which may lead to the seeking of control probably through a proxy contest.

As S. 510 is presently constituted it calls for amending Section 13 of the Securities Act of 1934 by requiring every person who acquires beneficial ownership of more than 10% of any class of equity security within seven days to send to the management and to each Exchange where the security is traded and file with the Commission a statement containing the following information: (i) the background and identity of all persons involved in the purchases; (ii) the source and amount of funds to be used in making the purchases, and if the purchase involved borrowed funds, a discription of the transaction and the names of the parties, except with respect to loans made in the ordinary course of business by a bank; (iii) if the purchasers are to acquire control of the business of the company, any plans which such persons may have to liquidate the business or to sell the assets or to merge it or to make any other major change in its business or corporate structure; (iv) the number of shares of such security which every such person (including his associates) owns and which he has a right to acquire; (v) information as to any contracts, arrangements or understandings with any person with respect to any securities of the issuer. When two or more persons act as a partnership, limited partnership, syndicate or other group for the purpose of acquiring, holding or disposing of securities of an issuer, such syndicate or group is to be deemed a "person" for the purpose of the subsection.

It is my opinion that if the foregoing provisions of this bill are passed by the House of Representatives, and the proposed legislation is enacted and becomes law, such action will sound the death knell for proxy contests. The provisions place additional obstacles in the path of the insurgent and give management even more weapons than it already has with which to fight.

Let us review the specific information required when a person or group has acquired more than 10% of any class of securities and its effect:

(i) In compelling the insurgent to state the background and identity of all persons involved in the purchases, management will have more time, with its greater monetary resources, to analyze and disparage the foe. The 10% figure in stock ownership might be reached by an insurgent many months before the annual meeting, while the filing of a 14B proxy contest form might be effected shortly before an annual meeting. An insurgent, generally with limited resources is forced into a prolonged war rather than a short contest. Isn't it sufficient th this information as regards proposed directors and participants in the fight mu

now be submitted when the insurgent actually elects to conduct a proxy contest? Furthermore, the average Wall Street broker will avoid helping an insurgent, as they already do, because they dislike any filings with the Securities and Exchange Commission. Thus, the vital help from Wall Street will disappear.

(ii) Should the insurgent reveal his source of funds to give management time to pressure the suppliers of such funds to withdraw the aid.

(iii) It is difficult for the insurgent to set out specifically plans to liquidate, sell assets or merge, etc. when not in a policy making position. Such a revelation may impair the corporation's tax planning. The stockholder is protected in any event because any contemplated major change must generally be submitted for his approval under corporate law. This information only helps management which can set up more stumbling blocks for the new group. Management, on the other hand, does not have to reveal its plans in these areas.

(iv) By compelling the new group to reveal its stockholders, management is enabled to assess the strength of the group and to attempt to divide it.

(v) By requiring the new group to reveal, many months before the annual meeting, information with respect to contracts and understandings between the persons with respect to the securities, all of which is required on the 14B form when the group elects to fight, management is again afforded the opportunity to harass the insurgents for a lengthy period of time.

I fail to see how any of the foregoing revelations at the time when a group acquires 10% ownership aids the stockholder whom everyone is trying to protect. Such revelations hurt him because they materially impair a change in control through a proxy contest.

Anyone contemplating the acquisition of control, which may require or result in a proxy contest, must firmly believe that the securities to which he has committed his funds, his time and his efforts are undervalued and that the present management of the company has not been able to bring out, for the benefit of the stockholder, the true values of the company. It is relatively impossible to go forward in any such enterprise unless the prime mover is convinced of this and unless he is able to convince many other people of the wisdom and advisability of this action.

I take the firm position that allowing and even encouraging proxy contests is vital to corporate vitality. Instead of making the task of the insurgent more difficult, legislation should rather make the road easier.

The flow of new ideas and new men into public companies can be achieved by existing Boards of Directors and officers if they recognize the need and act on it. However, public companies often have been lax in doing this. There is frequently tremendous internal resistance to changes.

The other approach is for new men with new thinking to acquire control of a public company. This can be very beneficial to security holders. The term "raider" as sometimes applied to insurgents is a word behind which many incompetent managements have ducked to preserve the security of their own positions. Too often incompetent and corrupt chief executives have been retained in office in order to preserve the security of other management personnel.* Within reason, the average stockholder can do nothing about it unless someone conducts a proxy fight to change the Board of Directors.

There are certain fundamental principals in proxy contests:

(1) In almost all instances, in order to conduct a successful proxy contest, new men with new ideas and vitality must purchase the required stock to gain control. Such a group will not commit money to the enterprise unless it is thoroughly convinced that it can do a better job than the current management and it can reasonably expect to succeed in gaining control.

(2) For an insurgent to wage a proxy contest in which he can hope to prevail, at least 35% to 40% of the stock of the company must be purchased by individuals friendly to him. *This is extremely difficult for a private group to accomplish.* The independent stockholder's vote cannot be relied on.

Proxy contests are extremely difficult and costly. The number of proxy contests conducted compared to the number of public companies is minuscule. Successful contests result in only a small fraction of those conducted. The reason is not that the existing managements are performing so capably, but that the task is onerous and expensive.

---

*In the Boston and Maine Corporation, in 1966, the President after being convicted misappropriating B&M corporate property was given a raise in salary and an extension his employment contract at the time extensions of employment contracts were given to r officers and directors.

It is a problem of the insurgent to equalize management's initial big head start. Management can generally rely on the vote of almost all he existing stockholders since the American investor habitually signs management's proxy almost without reading it, even though (a) the insurgent's plans and action may be in the best interests of the stockholders, and (b) the new group, to evidence its faith in its plans and people, is prepared to purchase millions of dollars in stock and expend tremendous sums in connection with the expenses of acquiring control to improve the security values. The insurgent must use his own funds. He and his volunteer workers receive no salaries for long difficult work. Management can use the corporate treasury and receive salaries during the fight. It can also use the corporate employees to help its cause.

The bill calls for the insurgent to reveal all of his plans to management. These plans can be very valuable. Under the proposed legislation, management can claim the plans, or a modification thereof, as its own, defeat the insurgent, and never carry them out, thereby preventing new people with new ideas from actively proceeding with them and directing the affairs of the public company. Although the insurgent's plans may be beneficial for the company and its stockholders, management will do everything within its power to stop the insurgent from getting control.

In a football contest is one team compelled to give its playbook to the coach of the other team in advance of the game? Is this a way to conduct the contest?

At some point in a corporation's life, changes should be made which can benefit the stockholders. Does corrupt or inefficient maangement have the right to run down a company during its tenure and not expose itself to loss of control and positions?

I submit that the job of the insurgent is tremendous and can result in substantial benefits to the stockholder of a company which is the subject of a proxy contest. I point to the few successful ones in the past few years: U.S. Smelting, Sunshine Mining, Penn-Dixie.

I do not intend here to detail all of the ways in which a management could defeat an insurgent once it knew that control was in jeopardy when the insurgents reached 10% of the stock. The ways are myriad and management's ingenuity endless (with corporate funds) in preserving its own power, even though it may have limited managerial competence.

The corporate proxy fight starts the football game with management ahead 90 to 10, and the insurgent is on his own 10 yard line. The proposed legislation then compels the insurgent to give his secret plays to the management and to grant management months to watch the insurgent in practice, time to break up the insurgent team and cut off the sources of supply from the training table. Obviously, no football coach would take on the job of coaching the insurgent team under these conditions. If you wish by legislation to end proxy fights, then this legislation should do it. If you wish to give incumbent management the green light to do anything with corporate assets, this will do it. If you wish to keep vested interests perpetually vested, this will do it.

Certainly, most investors who have held their stock through a proxy contest have benefited by virtue of the work, efforts and money of the insurgents. Managements have no monopoly on doing right. The scale should be somewhat balanced so the insurgent has a chance.

Passing this legislation will stop the flow of new ideas into corporations from the outside through proxy fights. I doubt if any self-respecting attorney, after examining the significance of the proposed legislation, would in his professional judgment advise a client who seeks control of a public company through a proxy contest to proceed to purchase stock on the open market. The risk is too great to justify the commitment of time, money and effort. This new legislation would effectively eliminate any possibility of success.

Consequently, the proposed bill should not be enacted into law, or subsections (1)–(4) to be added to Section 13 of the Securities Exchange Act of 1934, as contained on line 6 of page 1 to line 22 of page 5 of S. 510 should be limited to tender offers and invitations for tenders.

I trust that these views are helpful to the Committee and I am glad that I have had this opportunity of expressing them.

STATEMENT OF HERMAN C. BIEGEL AND JOHN A. CARDON,
ATTORNEYS, WASHINGTON, D.C.

This memorandum is submitted by Herman C. Biegel and John A. Cardon in opposition to Section 2 of H.R. 14475 and S. 510 as pending before the Subcommittee on Commerce and Finance of the House Committee on Interstate and Foreign Commerce.

The undersigned are members of the law firm of Lee, Toomey & Kent, 1200 18th Street, N.W., Washington, D.C. 20036, and have for over 25 years specialized in the Federal income tax and other legal aspects of pension, stock bonus and profit sharing plans. During that period we have handled all types of legal problems for employers, both large and small, representing a cross-section of American industry.

In view of this experience we desire to bring to the attention of the Committee certain aspects of the proposed legislation which we feel will be detrimental to pension, profit sharing and stock bonus plans if adopted in their present form.

PURPOSE OF THE PROPOSED LEGISLATION

The Bill, S. 510, as introduced in the Senate, was intended primarily to regulate the acquisition of large blocks of the stock of publicly held companies, when control of such companies might be at stake. In particular, the purpose was to regulate efforts to gain control of such companies through tender offers made without sufficient disclosure of the purposes, background, and resources of the persons making the offer. As a corollary, measures were also proposed to regulate counter efforts of corporate insiders to prevent loss of control, by causing their companies to acquire their own stock.

As introduced in the Senate, S. 510 contained no reference to employee benefit plans. In testifying before the Senate Committee on Banking and Currency, Manuel F. Cohen, Chairman, Securities and Exchange Commission, pointed out the problems concerning SEC when issuers reacquire their own securities and then observed that:

". . . purchases . . . by a welfare or pension fund subject to the influence of the issuer's management, give rise to similar problems. . . ." (Hearings, p. 28)

Section 2 of S. 510 as reported by the Senate Committee on Banking and Currency and Section 2 of H.R. 14475 as introduced in the House of Representatives propose to amend Section 13 of the Securities and Exchange Act of 1934 by adding a new subsection (e). Paragraph (1) of the proposed subsection (e) provides that issuers of equity securities may purchase such securities only upon compliance with rules prescribed by the Securities and Exchange Commission. Paragraph (2) of proposed subsection (e) defines "issuer" for this purpose to include

> "* * * any bonus, profit sharing, pension, retirement, thrift, savings, incentive, stock purchase, or similar plan of the issuer."

SEC PROPOSED RULE 10b–10

Although the legislation has not been adopted, the SEC has proposed a rule, designated as Rule 10b–10, to implement the power which would be granted to it by the legislation. Since the full implication of proposed subsection (e)(2) of Section 13 of the Securities and Exchange Act of 1934 can be seen only by an examination of the rules the SEC proposes to issue thereunder, it is relevant at this point to examine briefly the SEC requirements:

(1) *Disclosure.*—Within a reasonable time before any securities are purchased, the issuer must furnish to security holders, or make publicly available, information about: reasons for the purchase, the number of shares to be purchased, the method of purchase, whether purchases will be made from insiders, and whether any prior arrangement exists for the purchase.

(2) *Price.*—If the purchase is made on a national exchange, or the principal market for the security is a national exchange, the price must not exceed the higher of (a) the highest current independent bid price, or (b) the last sale price on the exchange. If neither the specific purchase nor the principal market is on a national exchange, the price must not exceed the highest current independent bid in the existing principal market.

(3) *Volume.*—If the purchase is made on a national exchange, the total volume purchased may not exceed either 10% of average weekly volume on the exchange for the four calendar weeks preceding that of the purchase, or

15% of the average daily volume on such exchange for the same period. In addition, the broker must be instructed to endeavor not to purchase more than 10% of the current week's, and 15% of the current day's volume. If the purchase is made other than on a national exchange, from or through a broker or dealer:

(*a*) if the principal market for the security is a national exchange, then total purchases in any market may not exceed 10% of average weekly, or 15% of average daily, volume for the previous four weeks on all exchanges; or

(*b*) if the principal market is other than a national exchange, then total purchases in any market may not exceed 10% of the average weekly volume transferred in the preceding four calendar weeks, as determined from transfer records of the issuer.

Presumably, for purposes of computing the volume limitations, acquisitions by parent and subsidiary groups and their benefit trusts must all be included.

(4) *Use of Brokers or Dealers.*—Purchases on a nationual exchange may be under the supervision and control of no more than one broker on one day. Purchases not on an exchange must be made by no more than one broker on one day, and from no more than one dealer on one day, unless the issuer establishes that such purchases were not solicited.

(5) *Purchase by Solicitation of Tenders.*—Notwithstanding the foregoing provisions, no purchase of a security by solicitation of tenders would be permitted unless: (a) the same offer is made to all holders of the security or all holders of less than a specified number of shares of the security, (b) the formula for price and number of shares to be purchased is uniform, (c) no special advantages are given to specific holders, and (d) no securities are purchased other than by such tender for a period before and after solicitation and purchase.

CONSIDERATIONS PARTICULARLY APPLICABLE TO EMPLOYEE BENEFIT TRUSTS

In many respects, some of which are hereinafter noted, the proposed rule would have impractical and unduly restrictive effects on any purchases by an issuer of its own securities. We wish to emphasize, however, considerations that are particularly applicable to purchases for employee benefit plans and trusts. Among such considerations are the following:

(1) *Purchases by an Independent Fiduciary or at the Direction of Employee-Beneficiaries.*—In many instances the trustee of an employees' trust is an independent fiduciary, often a corporation. In many other cases employees, who will have an investment position in the stock when purchased, direct the purchases. In either case there may be almost complete independent control over the methods, timing, prices and other conditions for purchase of the employer's stock and no opportunity for the improper influence of management in determining the need and conditions for such acquisitions.

(2) *Large or Recurrent Purchases under Established Policy.*—The terms of many employee benefit plans require the acquisition of large volumes of employer securities in order to carry out their purposes. Although these purchases would be seriously affected by the proposed restrictions, such purchases are not in fact adaptable to the *ad hoc* manipulation that the rule attempts to prevent.

(3) *Multiplication of Regulatory Power.*—The grant of power to regulate the terms and conditions for purchase of an employer's securities would vastly increase the presently somewhat limited SEC control over personnel and retirement policy, without sufficient justification. Employee pension plans that are qualified under the Internal Revenue Code already meet stringent requirements under the tax law. Any investment by a qualified employee benefit trust must be for the "exclusive benefit" of the employees covered. Accordingly, the administrator of a plan would risk loss of the favorable tax benefits for qualified plans if unwise investments were made in employer securities, or if artificially inflated prices were paid. In addition, employee trusts currently are required to disclos their operations, pursuant to the Welfare and Pension Plans Disclosure Act.

Any proposed new legislation that has such far-reaching effects upon the bas operations of benefit plans must deal directly with the complex problems in th area and receive thorough study and discussion in that context. For examp such consideration is now being given to the Administration's recommendati embodied in H.R. 5741 and S. 1024 for establishing Federal fiduciary stand by amendment to the Welfare and Pension Plans Disclosure Act. If those re mendations are enacted, they would also limit investment in securities of ployer corporations by certain kinds of plans. Hearings have been held on

5741 by the General Labor Subcommittee of the House Committee on Education and Labor.

In view of the extensive present and proposed legislation, any extension of this regulatory pattern to reach a peripheral aspect of abuses largely unrelated to the benefit plan area seems unwaranted and unnecessary.

RECOMMENDATIONS

In view of the foregoing considerations, it is unnecessary to extend the legislation and the proposed SEC Rule 10b–10 to purchases of employer securities by employee benefit trusts. We recommend deletion from Section 2 of the pending bills of the proposed subsection (e)(2) of Section 13 of the Securities and Exchange Act of 1934.

If application to employee trusts cannot be entirely eliminated by amending Section 2 of the bills, we recommend that the proposed subsection (e) and proposed SEC Rule 10b–10 be modified as described below to avoid possible adverse effect on the legitimate operations of pension, stock bonus and profit sharing plans. To the extent these modifications cannot be incorporated in the pending legislation, it is suggested that the Report of the Committee clearly delineate the authority intended to be conferred on the SEC so that they may be incorporated in Rule 10b–10 as finally promulgated by the SEC.

(1) *Exemption for Plans Investments of Which Are Not Subject to Control by Management.*—The legislation and the SEC Rules issued thereunder should specifically exempt employee benefit plans in any case where the purchase of employer stock is not subject to manipulation by management. Such an exemption would be perfectly consistent with the following statement regarding the amendment of Section 1(5) of S. 510 filed by the New York Stock Exchange before the Senate Committee on Banking and Currency (Hearings, p. 94):

> "The proposed SEC amendment would greatly expand the scope of this provision by including purchases made for bonus, profit sharing, pension and other employee benfit plans.
>
> "As we stated in our testimony, the Exchange believes that the disclosure philosophy of the bill can be served by limiting this requirement to the specific items of information currently set forth in Section 1(5).
>
> "We have no objection to including purchases made for various company benefit plans in the information statement we proposed, but *we would not require truly independent trusts of such plans, who normally make purchases without the knowledge of company management, to file such statements.* The Commission's concern that issuers may use these employee benefit programs for purchasing shares 'under circumstances which have introduced improper influence into the market,' is not applicable to plans administered by independent trustees." (Emphasis added.)

In this connection, reference is again made to the prepared statement filed by Chairman Cohen, a portion of which is quoted on page 2 above, in which he stated that it is plans "subject to the influence of the issuer's management" which give rise to problems similar to those found in purchases by an issuer of its own securities.

Specific examples of where there should be no problem are:

(*a*) Plans in which employee-beneficiaries direct the purchases of employer stock, and will have an investment position in such stock.

(*b*) Plans in which an independent fiduciary (corporate or otherwise), or an independent investment committee, control purchase of employer stock. (The mere fact that the employer corporation retains power to remove a trustee should not be regarded as affecting his independence.)

(*c*) Plans the terms of which specifically require purchase of employer stock, and in which recurrent day to day acquisitions of stock are required to meet plan requirements.

(2) *Exemption for Purchase of a Small Percentage of Average Volume.*—An exemption should be granted for daily purchases that do not exceed some specified small percentage of average volume. Such an exemption would permit relatively small purchases for benefit plans of large companies without affecting market behavior in any way.

(3) *Modification of Price Requirements.*—The price restrictions of Rule 10b– would severely limit an employer's ability to acquire stock needed to meet commitments in a rising market. Moreover, in some situations—for example, re securities are not actively traded or where purchases are being made in rent places and in different markets by an issuer, its subsidiaries and

affiliates—accurate determination of maximum prices within the prescribed limits would be almost impossible. The price rules are extremely impractical and must be changed.

(4) *Modification of Volume Requirements.*—Where purchases by benefit plans are recurrent, are within volume limits established over a significant period of operation and are needed to maintain the established plan requirements, the volume restrictions should not apply or should be made considerably more liberal. Indeed, if the present restrictions found in Rule 10b–10 were put into effect, *it would be impossible for employee benefit programs of many employers to acquire sufficient stock to meet their obligations.* Again, the effect is particularly acute when the combined needs of large companies and their affiliates and subsidiaries are taken into account. As minimum improvements, (a) the volume restrictions that refer to average volume for previous weeks should be modified to permit acquisition of stock at the time of an *initial* offering, (b) the 10% limitation should be raised to 20% of a week's volume, without a daily volume limitation, and (c) any percentage limitation for total purchases on exchanges and otherwise should be applied to total volume, not just the volume on all exchanges. Additional revisions are required to permit purchase of large blocks of stock at bargain prices.

(5) *Modification of Broker and Dealer Rules.*—The rules limiting the use of brokers and dealers should be modified to accommodate market practicalities, without permitting manipulation. For example, unsolicited purchases from dealers must be permitted. In addition, adjustments must be made (under appropriate safeguards) to permit purchases by more than one broker when large volume acquisition are necessary to meet plan commitments (including the combined commitments of affiliated parent and subsidiary groups).

(6) *Modification of Disclosure Requirements.*—Disclosure in a proxy statement, or in an annual report, of planned regular purchases in the future, should be regarded as fulfilling the requirement for information "furnished" in a "reasonable time" to security holders. In addition, if an issuer furnished the required information to the SEC in an annual 10–K report or in an 8–K report, such information should be regarded as fulfilling the alternative requirement to make information "publicly available".

(7) *Modification With Respect to Inclusion of Subsidiaries.*—Throughout the foregoing discussion, the impact of the proposed rule upon benefit plans of large, geographically disparate groups of parent and subsidiary corporations has been mentioned, but the modifications of the rule suggested herein do not begin to solve the staggering problems involved. Even if it were possible for the administrator of one of the many plans of affiliated corporations to determine the number of shares being acquired by all the others, and to determine the prices and number of brokers involved, numerous questions would remain.

For example, if a parent and its subsidiaries each needed employer stock for their respective plans and one or more such companies also needed stock for purposes unconnected with employee benefit plans, how would the choice among these needs be made? If, through inadvertence or failure of communication, the total volume limitation were exceeded, which corporation or trust in the affiliated group would be deemed to have violated the rule?

Consideration also must be given to the acquisition of employer stock by foreign subsidiaries. Certainly, purchases by such subsidiaries on foreign exchanges not regulated by the SEC should not be covered by the rule. Even if this were done, the coordination of international pension plan operations would be almost impossible under the proposed rule.

In summary, the provisions of the legislation and rule which lump together purchases of parents, subsidiaries and all their benefit plans must be drastically modified.

(8) *Other Modifications.*—Rule 10b–10 should not apply to debt securities, sinc the purposes of the legislation are relevant primarily to equity securities, an the relevant part of the Williams Bill refers only to equity securities. In additio the statement required of purchasers by the second sentence of the propos rule should be eliminated. As presently drafted, that sentence requires purchas to state not only that the purchase complies with Rule 10b–10 but also that the r is "intended to prevent the issuer from raising the market price of the securi Such a statement carries the unwarranted implication that, but for the the purchaser might artificially raise the market price.

Respectfully submitted.

LEE, TOOMEY & K
HERMAN C. BIEGEL
JOHN A. CARDON

THE AMERICAN BANKERS ASSOCIATION,
Washington, D.C., July 1, 1968.

Hon. JOHN E. MOSS,
Chairman, Subcommittee on Commerce and Finance, House Committee on Interstate and Foreign Commerce, Rayburn House Office Building, Washington, D.C.

DEAR CONGRESSMAN MOSS: This letter is written for the purpose of expressing the views of The American Bankers Association with respect to H.R. 14475, a bill providing for full disclosure of corporate equity ownership of securities under the Securities Exchange Act of 1934.

The American Bankers Association believes that the overall objective of this bill are sound, constructive, and necessary. One specific provision of this bill would however, present serious difficulties for our member institutions in serving as trustees of corporate pension, retirement, and other employee benefit plans. We refer to paragraph 2 of the proposed new subsection (e) which the bill would add to section 13 of the Securities Exchange Act of 1934.

As drafted, this new paragraph (e) (2) provides that a purchase by any bonus, profit-sharing, pension, retirement, thrift, savings, incentive, stock purchase, or similar plan of the issuer or any person controlling, controlled by, or under common control with the issuer, shall be deemed to be a purchase by the issuer and such a purchase would be required to comply with the rules and regulations to be adopted by the Securities and Exchange Commission under the proposed subsection (e). It is our considermed judgment that the scope of this provision, as presently drafted, is unnecessarily broad, and that its effect would be to needlessly circumscribe the investment administration by bank trust departments of many corporate pension, retirement and other employee benefit plans.

We do not quarrel with the purposes of this provision with respect to those employee benefit funds where the employer or someone in a control relationship with the employer has the power to control, direct or influence the investments made for an employee benefit fund. However, in many cases—if not most—bank trust departments, serving as trustees for the funds of employee benefit plans, act as full discretion trustees with the unconditional power to make all investment decisions. Were the proposed provision to be adopted in its present form, it would be extremely difficult, if not impossible, for bank trustees to effectively perform their investment responsibilities in connection with employee benefit funds for the ultimate benefit of the plan beneficiaries. This would be especially true in the case of collective trust funds, where the assets of many pension plans are commingled for the purposes of efficient and economical investment administration.

For the foregoing reasons, The American Bankers Association recommends that the language of the proposed new subsection 13(e) (2) be amended so as to narrow its application to only those employee benefit plans, in which the issuer or a person in a control relationship with the issuer exercises control, direction, or influence over the investment decisions for a plan. We earnestly hope that your distinguished Subcommittee will see fit to make this necessary modification in the provisions of H.R. 14475.

Sincerely yours,

CHARLES R. MCNEILL,
Director, Washington Office.

AMERICAN LIFE CONVENTION,
Chicago, Ill.
LIFE INSURANCE ASSOCIATION OF AMERICA,
New York, N.Y. July 1, 1968.

Hon. JOHN E. MOSS,
Chairman, Subcommittee on Commerce and Finance, House Committee on Interstate and Foreign Commerce, Rayburn House Office Building, Washington, D.C.

DEAR CONGRESSMAN MOSS: The American Life Convention and the Life Insurance Association of America are two associations with an aggregate membership 353 life insurance companies in the United States and Canada which have force approximately 92 percent of the legal reserve life insurance written he United States. These companies also hold over 99 percent of the reserves sured pension plans in the United States.

We are writing to request a clarifying amendment to paragraph (2) of the new Section 13(e) of the Securities Exchange Act of 1934 which would be added by H.R. 14475 and S. 510. Paragraph (1) of Section 13(e) would make it unlawful for a corporation to repurchase its own securities in contravention of such rules and regulations as the Securities and Exchange Commission may prescribe. These rules may require the corporation among other things, to provide holders of such securities with information relating to the reasons for such purchase, the source of funds, the number of shares to be purchased, the price to be paid, and the method of purchase. Paragraph 2 of Section 13(e) would provide that a purchase by or for any bonus, profit sharing, pension, retirement, thrift, savings, incentive, stock purchase, or similar plan of the issuer shall be deemed to be a purchase by the issuer. We believe that paragraph 2 should be modified to provide that a purchase by or for such a pension, profit sharing or similar plan shall be deemed to be a purchase by the issuer only where the issuer "exercises direction, control, or influence over the investments of such plan". A proposed amendment to accomplish this purpose is attached to this letter.

The clear purpose of new Section 13(e) is to provide shareholders of a corporation and other persons interested in the market price of its stock full information regarding the corporation's activities and intentions in repurchasing its own stock. We take no position here with respect to the need for such information. We do seriously question however, the assumption reflected in paragraph 2 of new Section 13(e) that a purchase of the corporation's securities by a pension, profit sharing, or similar plan is always to be considered the same as a purchase by the corporation itself. In the case of pension plans funded by life insurance companies, the issuing corporation will rarely, if ever, have any control or influence whatsoever over the securities purchased by the insurance company. The same is true for many pension and profit sharing plans funded by bank trustees and others. In such cases, there is no need to require the life insurance company, bank, or other funding medium to provide the information specified in new Section 13(e).

We shall appreciate your making this letter a part of the printed hearing record.

Sincerely yours,

AMERICAN LIFE CONVENTION,
WILLIAM B. HARMAN, JR.,
General Counsel.
LIFE INSURANCE ASSOCIATION OF AMERICA,
KENNETH L. KIMBLE,
Vice President and General Counsel.

SUGGESTED AMENDMENT TO NEW SECTION 13(e)(2) OF SECURITIES EXCHANGE ACT OF 1934, AS ADDED BY H.R. 14475 AND S. 510

"(2) For the purpose of this subsection, a purchase by or for (*a*) the issuer, or any person controlling, controlled by, or under common control with the issuer, or (*b*) any bonus, profit sharing, pension, retirement, thrift, savings, incentive, stock purchase, or similar plan of the issuer or any such person, *where the issuer or any such person exercises direction, control, or influence over the investments of such plan,* shall be deemed to be a purchase by the issuer."

NATIONAL ASSOCIATION OF MANUFACTURERS,
GOVERNMENT FINANCE DEPARTMENT,
New York, N.Y., October 31, 1967.

Hon. H. O. STAGGERS,
Chairman, House Interstate and Foreign Commerce Committee,
House Office Building, Washington, D.C.

DEAR MR. CHAIRMAN: I am writing as Chairman of the Money/Credit/Capital Formation Committee of the National Association of Manufacturers. Quite a few of our members have expressed concern over S. 510 relating to stock acquisition disclosures, which has been referred to your Committee.

The intent of the bill is to impose restrictions on those making tender offers by requiring specific disclosures such as their principals, source of financing, and plans for liquidation or changes in the corporate structure. However, it appears to us that the bill, in the form passed by the Senate, could be one import

respect operate to the disadvantage of existing management of firms for which the tender offers are made.

Paragraph (4) of Section 14 (d), as proposed, reads:

> "Any solicitation or recommendation to the holders of such a security to accept or reject a tender offer or request or invitation for tenders shall be made in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

This might be construed by the Securities and Exchange Commission as a license to require clearance by the Commission of material that management would want to communicate to stockholders in response to a tender offer. The very nature of tender offers, with their relatively short time limit, makes it imperative for management to respond immediately. If SEC clearance is imposed on such representations that management might make, the critical element in delay in virtually all cases would enure to the advantage of the interests making the tender offer.

Our aim is not to hinder the acquisition of stock by any interested party, but rather to ensure that neither party be placed in an unfavorable position by regulatory procedures. Without taking a position on the need for additional disclosure requirements to prevent misrepresentation, the NAM feels that S. 510 in its present form could produce inequities in regulation.

Therefore, if and when this bill is reported out by your Committee, we urge amendment so that it is clearly understood that management material replying to a tender offer may not be subject to delays by the SEC. This would not rule out minimum requirements for such answering materials, but would ensure that no stricter burden be placed on the party in opposition to the tender offer than on the maker of the offer.

The NAM would appreciate your Committee taking these thoughts into con-

Yours very truly,

MAURICE H. STANS,
Chairman, Money, Credit, and Capital Formation Committee.

ARNSTEIN, GLUCK, WEITZENFELD & MINOW,
Chicago, Ill., July 1, 1968.

Re H.R. 14475.

Hon. JOHN E. MOSS,
Chairman, Subcommittee on Commerce and Finance, Committee on Interstate and Foreign Commerce, House of Representatives, Washington, D.C.

DEAR MR. MOSS: On behalf of Sears, Roebuck and Co. and the 192,000 Sears employees who are participants in The Savings and Profit Sharing Pension Fund of Sears, Roebuck and Co. Employees, I take this opportunity to bring to your attention a serious problem for employe benefit plans, which H.R. 14475 presents in its present form. I wish to limit my comments primarily to that portion of Section 2 of the bill which would add a new subsection (e) (1) and (2) to Section 13 of the Securities Exchange Act of 1934.

Section 13 of the Securities Exchange Act relates to the "information, documents, and reports" to be filed with the Securities and Exchange Commission by publicly held companies (registered with the Commission under Section 12 of the Act) whose securities are traded in the over-the-counter market or on national securities exchanges. Section 14 of the Act relates to proxy solicitations with respect to securities of publicly held companies. Section 2 of H.R. 14475 would add new subsections (d) and (e) to Section 13 of the Act. Section 3, which would add new subsections (d), (e) and (f) to Section 14 of the Act, relates primarily to the solicitation of tenders and the dissemination of investment information deemed relevant to such solicitations. The first part of Section 2, which would add the new subsection (d) to Section 13 of the Act, similarly seems to be concerned with information which should be made public by persons who acquire substantial stock interests (i.e., in excess of 10%) in publicly held companies. On the basis of the historical record of the SEC's interpretation and administration of federal securities laws, it is not foreseen that the proposed Sections 13(d) and 14(d), (e), and (f) would affect the orderly and proper conduct of the daily affairs of publicly held companies or of their employee plans. No such conclusion, however, may be drawn with respect to the new subsection (e) which Section 2 of the bill would add to Section 13 of the Securities Exchange Act.

For the 34 years of its existence, Section 13 has dealt only with the reporting of investment and corporate management information about publicly held companies. Subsection (e) would depart from this concept and expand Section 13 to confer authority on the Commission to forbid employe benefit plans (including plans such as the Sears Profit Sharing Fund) to continue in the future with the investment policy which, for example, the Sears Fund has followed for more than 50 years, and for which, in fact, it was organized.

Subsection (e) would do two things. *One*, it would authorize the Commission to adopt rules which would make it unlawful for any company (whether or not a publicly held company in the sense of Section 12 of the Act) to employ any deceptive or manipulative practice in the purchase of shares of its outstanding stock. This proposal should not cause concern to any company or any employe profit sharing fund even though subsection (e) provides that a purchase of an issuer's stock by an affiliated employe plan shall be considered a purchase of such stock by the issuer. It may be well, however, to note in passing that this proposal does not seem to add anything to the existing authority of the Commission under Sections 9 (prohibiting manipulation) and 10 (prohibiting the use of deception in the purchase or sale of securities) of the Securities Exchange Act. *Two*, subsection (e) would confer authority on the Commission to forbid entirely (or place quantity restrictions on) the purchase of outstanding shares of stock by the company issuing it or by any employe benefit plan in which that company's employes participate even though such purchases do not involve any acts or practices which are "fraudulent, deceptive, or manipulative" or any of the non-investment management purposes which the Commission's Chairman has mentioned such as "preserving or improving the management's control position" or counteracting "a tender offer or other take-over bid."

To date the only basis advanced before the Congress for this additional authority is the Commission Chairman's assertion that "even where the management has no improper motive in repurchasing securities, substantial repurchase programs will inevitably affect market performance and price levels." This is all, nothing more, no offer of factual information; not even a claim that such market effect is bad or improper, or that purchases by an employe plan of the securities of the employer causes more harm than good and should in the public interest be subordinated to the purchases of other investors, including institutional investors (mutual funds, banks, insurance companies, foundations, or employe plans of other employers) whose substantial purchase programs could also be considered as programs which "will inevitably affect market performance and price levels."

There are many employe profit sharing plans with the basic policy of investing in employer stock for *bona fide* investment management and personnel policy objectives. Yet the proposed subsection (e) would confer authority upon the SEC to adopt rules which would put them out of business in the absence of drastic transformation of investment policy and abandonment of personnel policies deemed desirable. This the Commission could do by stating that such action was in the public interest, presumably without any more supporting evidence than the assertion of the Commission's Chairman quoted above.

Today is the 52nd anniversary of the founding of the Sears Profit Sharing Fund on July 1, 1916 "for the three-fold purpose (i) to permit eligible employes to share in profits, (ii) to encourage the habit of saving, and (iii) to furnish a means for such employes to accumulate their own savings, the employers' profit sharing contributions, and the earnings thereon, to provide themselves with retirement income." Today more than 192,000 employes are participants in the Fund. Throughout the years the Rules of the Fund have provided that the Fund was to be invested so far as practicable and advisable in the Company's stock to the end that participants "may, in the largest measure, share in the earnings of the Company." At December 31, 1967, the Fund held 36,040,698 of the Company's common shares representing 23% of the outstanding stock. Ten years ago, it held 26% of the outstanding stock. To date the operation of the Fund has been of substantial benefit to employes and as a factor facilitating the recruitment and retention of superior individuals as employes has been beneficial to the stockholders who now number more than 257,000 in addition to the 192,000 members of the Fund. Without any effort to show that operation over the years of the Sear Fund and other similar employe plans has, by way of impact on the securiti markets, adversely affected the stockholders of the sponsoring employers, t Commission urges that it be given broad authority to in effect terminate drastically alter these plans.

At this time the only indication we have of what the Commission could be expected to do under the proposed subsection (e) is the Commission's "draft Rule 10b–10" which apparently received some limited circulation for comment among representatives of the organized securities markets in February 1967. Under this draft rule an employe plan's weekly purchases of the employer's stock on the stock exchanges and from other sources through brokers and dealers could not, in substance, exceed 10% of the average weekly volume on the exchanges on which such stock is listed.

Enactment of proposed subsection (e) to Section 13 and adoption of Rule 10b–10 would on the basis of information presented to the Commission's Division of Trading and Markets in 1966 require substantial modification of the dominant historical investment policy of the Sears Profit Sharing Fund. It is believed that the investment management of many other employe plans would be similarly affected.

It would seem appropriate that action on subsection (e) be deferred until the Congress is presented in hearings before the Subcommittee on Commerce and Finance with evidence concerning:

(i) the number, nature, and importance of the employe plans which will be affected or might be affected by the proposed legislation;

(ii) the existence of adverse, undesirable or improper effects, if any, on securities markets or on investors attributable to the existence and operation of employee plans purchasing the securities of their employers;

(iii) the facts, if any, which tend to show that it would be in the public interest to subordinate the investment rights of employe plans to those of other institutional purchasers;

(iv) the extent to which appropriate and practical disclosure requirements should be considered in lieu of quantity restrictions;

(v) the factual basis for the Commission's assertion that the problems of market impact in this area cannot be met by a simple disclosure requirement;

(vi) a detailed analysis and identification of "the problems of market impact in this area";

(vii) the need for quantity restrictions for issuers not making public offerings of stock or using stock for acquisition purposes; and

(viii) the need for such legislation prior to completion, and Congressional review of, the projected study of institutional investors.

Respectfully,

LEO H. ARNSTEIN.

THE ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK,
COMMITTEE ON SECURITIES REGULATION,
New York, June 28, 1968.

Hon. JOHN E. MOSS,
Chairman, Subcommittee on Commerce and Finance, Interstate and Foreign Commerce Committee, Rayburn House Office Building, Washington, D.C.

DEAR CONGRESSMAN: This letter is submitted by the Committee on Securities Regulation of the Association of the Bar of the City of New York in connection with the consideration by your Subcommittee of the legislative proposals referred to above. We appreciate the opportunity to present our views.

While their common title suggests a more limited scope, all of the proposals would amend Sections 13 and 14 of the Securities Exchange Act of 1934 ("the Act") so as to provide regulation in situations involving:

(*a*) the acquisition (other than by an issuer) of more than 10% or, subject to certain exceptions, increasing an existing holding of more than 10% of any equity security which is registered under Section 12 of the Act;

(*b*) so-called "Tender Offers"; and

(*c*) acquisitions by issuers of equity securities issued by them (whether or not registered under Section 12 of the Act).

Our discussion will be directed largely to S. 510, H.R. 14475, and H.R. 15567 which are in most respects identical. H.R. 12210 corresponds to S. 510 before it was amended by the Senate.

Our principal comments relate to the proposal, referred to in (c) above, to add new Subdivision (e) (Subsection 5 in the case of H.R. 12210) to Section 13 of e Act. In our view, this proposal represents an unnecessary and unwarranted parture from the concepts of investor protection which the Federal regulatory wer has been traditionally designed to provide. Under it, the power and re-

sponsibility of the Securities and Exchange Commission ("the Commission") are not limited to requiring appropriate disclosures and to guarding against deceptive and unfair devices in respect of the securities of publicly owned companies (i.e., those having equity securities registered pursuant to Section 12 of the Act). On the contrary, it extends to all issuers, public and private, and it appears to give the Commission power and responsibility to pass on the substantive merits of a particular issuer purchase program if in the Commission's judgment it is in the "public interest".

The proposal is broad enough to permit the adoption of rules that would be in conflict with, and would override, the substantive state law which has traditionally governed questions of corporate repurchases of stock and it certainly will permit the Commission to substitute its judgment for that of the issuer's management in the area. Under it, the Commission appears to be given power to regulate the price and other terms of an issuer repurchase, the amount of the repurchase, and the timing and method thereof. On its terms, it arguably is broad enough to permit the Commission if in its judgment it is necessary or appropriate " . . . in the public interest or for the protection of investors . . ." to prohibit repurchases completely.

In addition, the proposals (except for H.R. 12210) introduce the "control" concept in defining issuer repurchases. This concept has a long history under the Securities Act of 1933 and the Commission and its staff have consistently avoided any concise definition of "control". Undoubtedly, this has been a sound approach from the standpoint of protecting potential investors by insuring full disclosure in doubtful cases even though a considerable burden of delay and expense has been imposed on the seller. Admittedly, there is also a disclosure problem in the case of acquisition by controlling persons but it is one of providing full disclosure rather than of restricting disclosure to prevent "overselling". This is an area in which the anti-fraud provisions of the Act already provide the Commission with adequate regulatory powers. And in any event the impact of the regulation should not be dependent on any vague concept of control but on the possession of "inside" information. If regulation of purchases is based on a control concept comparable to that applied under the Securities Act of 1933, it can only serve to restrict the market for outstanding securities to the detriment of the investor who desires to sell.

Finally, the proposals (except H.R. 12210) define issuer repurchases to include purchases by or for various employee benefit plans such as a pension plan, profit sharing plan, and the like. Admittedly, where the purchase programs under such plans are under the direction of the management of the issuer, there would seem no reason why they should not be treated as if they were purchases by the issuer and we understand this to be the case under existing law. However, where the programs are directed by independent entities such as trustees it seems doubtful that the considerations which might be applicable to repurchases by an issuer would have much relevance. More important in view of the substantive powers proposed to be given the Commission, this broad definition can create problems in other areas. For example, in the case of a pension or other plan which is the subject of negotiations with a labor union, the Commission could in effect be a third party at the negotiating table.

To justify the broad grant of new power which this proposal contemplates there should be substantial evidence that real regulatory problems exist. This seems to our Committee not to be the case. There is already a long history of application of the anti-fraud provisions to provide adequate disclosure of information pertinent to an investor's decision to resell his securities to the issuer or an insider. In the area of issuer repurchases intended for the purpose of manipulation of prices, the Commission, on its own statements, has certainly been successful on a case-by-case basis and it has the power under the anti-fraud provisions of the Act to adopt specific regulations to deal with this type of conduct. Finally, even in the case of programs which are admittedly for perfectly proper purposes but which might have an effect on "market performance and price levels", including programs under employee benefit plans operated under the direction of independent trustees, the Commission has had considerable regulatory impact on an informal basis. If the Commission finds that it is necessary or desirable, it has the power to adopt regulations to accomplish its purpose in this area.

Basically, the argument advanced for this proposal seems to be that it would be "helpful". This in our opinion in no way justifies the major extension proposed for the powers of the Commission, particularly when its existing powers by no means fully exercised.

With respect to the other two proposals, referred to in (a) and (b) above, it is the general view of our Committee that both proposals seem to go beyond any demonstrated need for additional statutory regulation of the kind of transactions to which such proposals relate.

The proposals appear to have been induced primarily by the fact of recent increases in activities in the "tender offer" and "take-over" fields, rather than by any substantial evidence that such activities are undesirable or involve any real threat of injury to investors. The absence of need for a major new statutory scheme of regulation in the areas covered by the proposals would seem to be evidenced by the fact that, in large part, the proposals merely grant to the Commission in a specific context regulatory powers which the Commission already has under more general provisions of the Act, particularly the so-called anti-fraud provisions of the Act. The suggestion sometimes made that the proposals merely fill "a gap in the provisions of" the Act in the area of planned acquisitions of controlling blocks of securities of publicly owned companies is, therefore, not entirely accurate.

We recognize, however, that the desirability of additional statutory regulation in the areas covered by the proposals raises questions of public policy which may not be within the purview of our Committee. Accordingly, except for the foregoing comment, our Committee does not express any view as to the merits of either of these proposals.

We hope that these comments will be helpful in your consideration of the proposals.

Respectfully submitted,

THOMAS A. HALLERAN, *Chairman.*

(The following additional correspondence was subsequently submitted by SEC:)

SECURITIES AND EXCHANGE COMMISSION,
Washington, D.C., July 9, 1968.

Hon. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This is in reply to your letter of June 20 with respect to the acquisition and subsequent sale by Crane Co. of a block of American Standard Inc. in connection with Crane's unsuccessful takeover bid. There have been a number of situations of this type in recent months. Essentially, the pattern is that a company accumulates more than ten per cent of the stock of another corporation as a result of a takeover bid, whereupon the company sought to be acquired negotiates what is referred to as a "defensive merger" with a third party, and the unsuccessful takeover bidder acquires shares of the third party in the merger and sells them. This presents the question referred to in your letter as to whether there is liability under Section 16(b) of the Securities Exchange Act, assuming that the original takeover bid and the merger occur within six months, or the sale occurs within six months after the merger, whether or not it is within six months after the original tender offer. There are a number of cases under Section 16(b) pending in district courts in various parts of the country which involve this question, but so far as we know, none of them has as yet been decided. The legal issues are two: First, whether the merger constitutes a purchase or a sale, or both, for purposes of Section 16(b), or, alternatively, whether the purchase of securities in a takeover bid may be matched against the sale of securities of a different company following a merger, for purposes of Section 16(b).

As you know, under the existing provisions of Section 16(b), actions thereunder may be brought only by the company whose securities are involved, or a stockholder of that company suing derivatively on its behalf, and the proceeds recovered go to the company. In most of the takeover bid situations, the dollar amount of potential recovery is quite large and there is thus adequate incentive for the corporation or a stockholder to bring an action. Since relationships between the unsuccessful takeover bidder and the management of the company whose securities were the subject of the bid are usually somewhat unfriendly, there is, if anything, a greater likelihood that the company itself will bring an action than is generally true in the case of trading by "insiders" in the stock of their own companies.

You raise the question, however, whether the Commission should be authorized to bring such actions in this particular type of case. This same question was put to me during the recent hearings before the Subcommittee on Commerce and Finance of your Committee on S. 510 and H.R. 14475. I replied that, while we had never sought this authority and were not seeking it now, it would be a most effective way of dealing with problems of this kind. I might add that, in connection with the possibility to which you adverted in your letter, we already have authority to bring an injunctive proceeding under the antifraud provisions and seek appropriate relief where a tender offer is used as a manipulative device to increase the value of existing stockholdings or for other purposes unrelated to a desire to acquire a controlling interest or a substantial investment position.

Sincerely,

MANUEL F. COHEN, *Chairman.*

(Whereupon, at 12:05 p.m. the subcommittee adjourned, subject to call.)

AGRICULTURAL COOPERATIVES EXEMPTION

HEARING

BEFORE THE

SUBCOMMITTEE ON TRANSPORTATION AND AERONAUTICS

OF THE

COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE

HOUSE OF REPRESENTATIVES

NINETIETH CONGRESS

SECOND SESSION

ON

H.R. 6530

A BILL TO AMEND SECTION 203(b)(5) OF THE INTERSTATE COMMERCE ACT TO CLARIFY THIS EXEMPTION WITH RESPECT TO TRANSPORTATION PERFORMED BY AGRICULTURAL COOPERATIVE ASSOCIATIONS FOR NONMEMBERS

S. 752

AN ACT TO AMEND SECTIONS 203(b)(5) AND 220 OF THE INTERSTATE COMMERCE ACT, AS AMENDED, AND FOR OTHER PURPOSES

JULY 1, 1968

Serial No. 90-45

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

U.S. GOVERNMENT PRINTING OFFICE
WASHINGTON : 1968

96-778

COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE

HARLEY O. STAGGERS, West Virginia, *Chairman*

SAMUEL N. FRIEDEL, Maryland	WILLIAM L. SPRINGER, Illinois
TORBERT H. MACDONALD, Massachusetts	SAMUEL L. DEVINE, Ohio
JOHN JARMAN, Oklahoma	ANCHER NELSEN, Minnesota
CHET HOLIFIELD, California	HASTINGS KEITH, Massachusetts
JOHN D. DINGELL, Michigan	GLENN CUNNINGHAM, Nebraska
PAUL G. ROGERS, Florida	JAMES T. BROYHILL, North Carolina
HORACE R. KORNEGAY, North Carolina	JAMES HARVEY, Michigan
LIONEL VAN DEERLIN, California	ALBERT W. WATSON, South Carolina
J. J. PICKLE, Texas	TIM LEE CARTER, Kentucky
FRED B. ROONEY, Pennsylvania	G. ROBERT WATKINS, Pennsylvania
JOHN M. MURPHY, New York	DONALD G. BROTZMAN, Colorado
DAVID E. SATTERFIELD III, Virginia	CLARENCE J. BROWN, JR., Ohio
DANIEL J. RONAN, Illinois	DAN KUYKENDALL, Tennessee
BROCK ADAMS, Washington	JOE SKUBITZ, Kansas
RICHARD L. OTTINGER, New York	
RAY BLANTON, Tennessee	
W. S. (BILL) STUCKEY, JR., Georgia	
PETER N. KYROS, Maine	

W. E. WILLIAMSON, *Clerk*
KENNETH J. PAINTER, *Assistant Clerk*

Professional Staff

ANDREW STEVENSON	WILLIAM J. DIXON
JAMES M. MENGER, Jr.	ROBERT F. GUTHRIE

SUBCOMMITTEE ON TRANSPORTATION AND AERONAUTICS

SAMUEL N. FRIEDEL, Maryland, *Chairman*

JOHN D. DINGELL, Michigan	SAMUEL L. DEVINE, Ohio
J. J. PICKLE, Texas	GLENN CUNNINGHAM, Nebraska
DANIEL J. RONAN, Illinois	ALBERT W. WATSON, South Carolina
BROCK ADAMS, Washington	DAN KUYKENDALL, Tennessee

CONTENTS

AGRICULTURAL COOPERATIVES EXEMPTION

MONDAY, JULY 1, 1968

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON TRANSPORTATION AND AERONAUTICS,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
Washington, D.C.

The subcommittee met at 10 a.m., pursuant to notice, in room 2123, Rayburn House Office Building, Samuel N. Friedel (chairman of the subcommittee) presiding.

Mr. FRIEDEL. The subcommittee will come to order.

This morning the Subcommittee on Transportation and Aeronautics is holding hearings on H.R. 6530, introduced by the chairman of the full committee at the request of the Interstate Commerce Commission, and a companion bill, S. 752, which originally was the same bill in the Senate but has come to us in substantially amended form.

These two bills have for their purpose the amendment of section 203(b)(5) of the Interstate Commerce Act to clarify the exemption respecting the transportation performed by agricultural cooperative associations for nonmembers.

Under section 203(b)(5) of the Interstate Commerce Act motor vehicles controlled and operated by agricultural cooperatives, or by a federation of such cooperatives, are exempt from the Commission's economic regulation provided the cooperatives meet certain qualifying criteria as defined in the Agricultural Marketing Act of 1929 (12 U.S.C. 1141).

The original exemption for agricultural cooperatives was included in the Motor Carrier Act of 1935. In 1940 this exemption was expanded to include a federation of such cooperative associations if such federation possesses no greater powers or purposes than cooperative associations so defined.

The number of groups and organizations claiming exemptions as agricultural cooperatives has grown considerably in the last 10 to 15 years. Also the transportation activities of agricultural cooperatives have changed greatly since the original exemption was adopted in 1935.

While this committee treated of a number of transportation services performed by motor vehicles which were of illegal nature or so-called grey area in our widespread amendments of 1958 and in those of 1965, this problem is one which at that time was not fully recognized. Rather, the problem has grown more acute in the last several years owing to the doubt cast on Interstate Commerce Commission interpretations as a result of certain court decisions, and owing to the increasing use by the Department of Defense of cooperative association transportation facilities in the handling of Government freight.

It is my understanding that since the legislation initially was intro-

duced last year, much progress has been made by the various segments of the carrier industry and governmental agencies as well as shipping groups, and that there is a general feeling that the bill as amended by the Senate affords a fitting resolution.

At this point in the record we will insert the legislation under consideration and agency reports thereon.

(H.R. 6530, S. 752, and departmental reports thereon follow:)

[H.R. 6530, 90th Cong., first sess.]

A BILL To amend section 203(b)(5) of the Interstate Commerce Act to clarify this exemption with respect to transportation performed by agricultural cooperative associations for nonmembers

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 203(b)(5) of the Interstate Commerce Act is amended by inserting immediately before "; or" the following: ", but, in transportation for nonmembers for compensation, only when those vehicles are being used in the transportation of farm products, farm supplies, or other farm related traffic".

[S. 752, 90th Cong., second sess.]

AN ACT To amend sections 203(b)(5) and 220 of the Interstate Commerce Act, as amended, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That at the end of section 203(b)(5) of the Interstate Commerce Act delete the semicolon and add the following language: ", but any interstate transportation performed by such a cooperative association or federation of cooperative associations for nonmembers who are neither farmers, cooperative associations, nor federations thereof for compensation, except transportation otherwise exempt under this part, shall be limited to that which is incidental to its primary transportation operation and necessary for its effective performance and shall in no event exceed 15 per centum of its total interstate transportation services in any fiscal year, measured in terms of tonnage: *Provided*, That, for the purposes hereof, notwithstanding any other provision of law, transportation performed for or on behalf of the United States or any agency or instrumentality thereof shall be deemed to be transportation performed for a nonmember: *Provided further*, That any such cooperative association or federation which performs interstate transportation for nonmembers who are neither farmers, cooperative associations, nor federations thereof, except transportation otherwise exempt under this part, shall notify the Commission of its intent to perform such transportation prior to the commencement thereof: *And provided further*, That in no event shall any such cooperative association or federation which is required hereunder to give notice to the Commission transport interstate for compensation in any fiscal year of such association or federation a quantity of property for nonmembers which, measured in terms of tonnage, exceeds the total quantity of property transported interstate for itself and its members in such fiscal year.

SEC. 2. Section 220 of the Interstate Commerce Act, as amended, is further amended by adding the following immediately after subsection (f):

"(g) The Commission or its duly authorized special agents, accountants, or examiners shall, during normal business hours, have access to and authority, under its order, to inspect, examine, and copy any and all accounts, books, records, memorandums, correspondence, and other documents pertaining to motor vehicle transportation of a cooperative association or federation of cooperative associations which is required to give notice to the Commission pursuant to the provisions of section 203(b)(5) of this part: *Provided, however*, That the Commission shall have no authority to prescribe the form of any accounts, records, or memorandums to be maintained by a cooperative association or federation of cooperative associations."

EXECUTIVE OFFICE OF THE PRESIDENT,
BUREAU OF THE BUDGET,
Washington, D.C., September 8, 1967.

Hon. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This is in reply to your request for the views of the Bureau of the Budget on H.R. 6530, a bill "To amend section 203(b)(5) of the Interstate Commerce Act to clarify this exemption with respect to transportation performed by agricultural cooperative associations for nonmembers."

This bill would restrict the current exemption of agricultural cooperatives from economic regulation by the Interestate Commerce Commission to those situations where the traffic is farm-related. The effect of this amendment would be to deprive agricultural cooperatives of revenues which enable them to provide more efficient and economic transportation services.

Since we believe that the present exemption, as interpreted by the courts, properly balances the interest of the public, the cooperatives, and for-hire carriers, we would be opposed to enactment of H.R. 6530.

Sincerely yours,

WILFRED H. ROMMEL,
Assistant Director for Legislative Reference.

DEPARTMENT OF AGRICULTURE,
Washington, D.C., July 24, 1967.

Hon. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your request of March 13, 1967, for comments with respect to H.R. 6530, a bill "To amend section 203(b)(5) of the Interestate Commerce Act to clarify this exemption with respect to transportation performed by agricultural cooperative associations for non-members."

This proposed legislation would, if enacted, limit the exemption of motor vehicles controlled and operated by a cooperative association as defined in the Agricultural Marketing Act, approved June 15, 1929, as amended, or by a federation of such cooperatives. The exemption from economic regulation would no longer apply to such motor vehicles when used in the transportation, for non-members for compensation, of property of any kind except farm products, farm supplies, or other farm related traffic. This provision for total elimination of certain kinds of cargo from the benefits of exemption would impair the efficiency and economy under which transportation is conducted by cooperatives in accordance with the existing provisions of law.

The Department does not favor enactment of this legislation.

The interpretation of the cooperative exemption in section 203(b)(5) of the Interstate Commerce Act has been the subject of much litigation. In a number of cases before the Interstate Commerce Commission and the courts, the Department of Agriculture has consistently taken the position that the language of the Interestate Commerce Act, when read in conjunction with the language of the Agricultural Marketing Act of 1929, should be given a liberal construction; that cooperatives should not be so limited in their motor carrier operations that efficient operation on behalf of farmer members would be stifled; that it was clearly the intent of the statute that a cooperative, in the conduct of its motor carrier operations, be permitted to transport in addition to its own and is members' property, incidental quantities of property belonging to others; and that backhauls of non-member property of a character which would otherwise be subject to regulation, should be permitted, provided the transportation of such property remained incidental to the transportation of property of the cooperative and its members.

Generally, the courts have ruled in favor of the Department's interpretation of the statutes and against the more restrictive interpretations which others have advocated. The decision of the Ninth Circuit Court of Appeals (350 Fed. 252 (1965), *cert. denied*, 382 U.S. 1011 (1966)), involving the Northwest Agricultural Cooperative Association supports the Department's view. In this case the Court held that a cooperative "does not lose its status by engaging in activity other than its primary statutory activity, so long as the other activity is inci-

dental to the primary one and necessary to its effective performance." Pursuant to the Court's decision a cooperative would be permitted to engage in the transportation of so-called "non-farm related" property to the extent that such transportation activity is incidental to its primary activity of transporting its own or member property and necessary to the effective performance of that activity.

We should like to emphasize that our position in cases involving the cooperative exemption has not been dictated solely by the belief that this is the proper legal interpretation of the statutes, but also by the conviction that the public interest would be appropriately served. Clearly, the interests of the cooperatives and their farmer members are served through the greater operating efficiencies made possible under the "incidental and necessary" test of the *Northwest* decision. Further, to the extent that the motor carrier operations of the cooperatives are efficient, the interests of the marketing system and of consumers are served. At the same time, Department statistics clearly indicate that the impact upon the regulated common carrier industry of transportation by the cooperatives of properaty which might otherwise be transported by the common carriers is quite negligible. Accordingly, we believe it would not be in the public interest to adopt the restrictive approach provided for in H.R. 6530.

Although the Department is opposed to H.R. 6530, there would appear to be merit in legislation which would clarify the scope of the exemption and assist the ICC in its enforcement of the motor carrier provisions of the Act. Our views may be summarized as follows:

First, we believe it would be appropriate for a cooperative to be required to notify the Interstate Commerce Commission if it intends to transport for hire in motor vehicles which it controls or operates, any property other than its own or that of its members, farm products and farm supplies for non-member farmers, and commodities exempt under section 203(b)(6) of the Interstate Commerce Act. The ICC would thus have a record of those cooperatives which intend to transport the type of property which has been the subject of controversy.

Second, to further assist the ICC and to meet one of the problems with respect to which Commission representatives have expressed concern, we believe the Commission or its agents should be given express authority to have access to the books, records, and accounts pertaining to the motor vehicle transportation of those cooperatives which transport property in accordance with their notice to the Commission.

Third, we believe the quantity of this non-cooperative traffic described above which a cooperative could transport in any year should be limited to a quantity which is incidental to the primary transportation operation of the cooperative and necessary to its effective performance. Such a limitation, we believe, flows from application of the decision in the *Northwest* case referred to previously. The amount of such property which cooperatives should be authorized to transport in order to achieve efficiency of operation will vary depending upon the nature of the business of the cooperative, the geographic area where it operates, and the availability of other backhaul traffic.

Fourth, to clarify a question which has arisen in the past and which appears to be one of concern to the regulated motor carrier industry, we believe that *transportation* operations which a cooperative carries out for non-members should not exceed the *transportation* operations which it carries out for members. Under the Agricultural Marketing Act of 1929, a cooperative may not deal in "farm products, farm supplies, and farm business services with or for non-members in an amount greater in value than the total amount of such business transacted by it with or for members." This provision applies to the total business activities of a cooperative. Apparently, there is concern that in a case where the only non-member business of a cooperative is transportation, the cooperative would be free to engage in transportation for non-members in an amount equal in value to the total business of all kinds conducted by the cooperative for members. A provision which would equate non-member *transportation* business with member *transportation* business would alleviate this concern.

There has also been concern expressed that under the language of the Agricultural Marketing Act cooperatives could transport property for the U.S. Government or any of its agencies without limit. We question, however, whether any such result was intended. Any doubt could be removed by a specific provision that transportation of property for the U.S. Government or any of its agencies is to be considered non-member business.

We believe that legislation which embodies the views set out above would constitute an appropriate prescription of the intended scope of the cooperative exemption, and would provide a mechanism which would materially assist ICC

in its enforcement of motor carrier operations. It would give appropriate recognition to the interests of the agricultural community, the common carrier industry, and the public.

The Bureau of the Budget advises that there is no objection to the presentation of this report from the standpoint of the Administration's program.

Sincerely yours,

ORVILLE L. FREEMAN, *Secretary.*

OFFICE OF THE SECRETARY,
DEPARTMENT OF TRANSPORTATION,
Washington, D.C., August 2, 1967.

HON. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: Your Committee has requested the views of this Department on H.R. 6530, a bill

"To amend section 203(b)(5) of the Interstate Commerce Act to clarify this exemption with respect to transportation performed by agricultural cooperative associations for non-members."

Section 203(b)(5) of the Interstate Commerce Act provides that, except for safety considerations and qualifications and maximum hours of service of employees, there shall be no Interstate Commerce Act regulation of motor vehicles controlled and operated by a cooperative association as defined in the Agricultural Marketing Act of 1929, as amended, or by a federation of such cooperative associations, if such federation possesses no greater powers or purposes than cooperative associations so defined. "Cooperative association" as defined in the Marketing Act means any association in which farmers act together in processing, preparing for market, handling, and/or marketing the farm products of persons so engaged, and also means any association in which farmers act together in purchasing, testing, grading, processing, distribution, and/or furnishing farm supplies and/or farm business services, provided, however, that such associations are operated for the mutual benefit of the members thereof as such producers or purchasers and conform to one or both of the following requirements:

First: That no member of the association is allowed more than one vote because of the amount of stock or membership capital he may own therein; and

Second: That the association does not pay dividends on stock or membership capital in excess of 8 percent per annum.

And in any case to the following:

Third: That the association shall not deal in farm products, farm supplies, and farm business services with or for nonmembers in an amount greater in value than the total amount of such business transacted by it with or for members. All business transacted by any cooperative association for or on behalf of the United States or any agency or instrumentality thereof shall be disregarded in determining the volume of member and nonmember business transacted by such association.

The present proposal would amend section 203(b)(5) by adding language which would indicate that, in transportation for nonmembers for compensation, the exemption from regulation would apply only when those vehicles are being used in the transportation of farm products, farm supplies, or other farm-related traffic.

Basically, H.R. 6530 is designed to eliminate certain kinds of traffic from the benefits of the exemption. More specifically, the bill is designed to overcome the decision of the Ninth Circuit Court of Appeals in *Northwest Agricultural Cooperative Association* v. *ICC*, 350 F. 2d 252, which held that an agricultural cooperative (as defined in the Marketing Act) whose primary activity was transporting farm products and farm supplies did not lose its status as a cooperative association so as to subject its transportation activities to economic regulation by the ICC where its transportation of non-farm products and supplies was incidental and necessary to the cooperative's farm-related transportation, both in character and amount.

The court defined *incidental* as "limited to otherwise empty trucks returning from hauling member farm products to market, and producing a small return in proportion to the . . . [the cooperative's] income from trucking farm products and farm supplies."

Necessary was defined as when "it is not economically feasible to operate the trucks empty on return trips, and . . . [where] the additional income obtained is no more than that required to render performance of the cooperative's primary farm transportation service financially practicable."

The court further stated that "a cooperative would not be of this character [an association as defined] if its non-farm related business exceeded that which was necessary and incidental to its farm-related business, and it is difficult to imagine circumstances under which non-farm related business could approach fifty percent of the total and still remain incidental and necessary to farm-related business."

In reaching its conclusions, the court relied on the legislative history, the precedents in *ICC* v. *Jamestown Farmers Union*, 47 F. Supp. 749 (D. Minn. 1944), aff'd. 151 F. 2d 403, 8th Cir. 1945, and repeated rejections by Congress of past efforts to narrow the reach of the Agricultural Marketing Act to serve the policies underlying the Interstate Commerce Act at the expense of those upon which the Agricultural Marketing Act is based. The court also rejected the ICC's effort to impose a definition which would have required that transportation of traffic other than for cooperative members must be "functionally related" to the business of the cooperative. The Supreme Court denied a petition for certiorari at 382 U.S. 1011.

The Department is opposed to the proposed legislation. The present exemption has permitted the agricultural cooperatives to conduct efficient and economic operations by allowing a limited amount of for-hire truck transportation. As the Circuit Court pointed out, the legislative history and prior court decisions supported the position of the cooperatives. Moreover, in the 1966 hearings on S. 1729, a similar bill, it was demonstrated that the cooperatives themselves had exercised initiative in 1959 in attempting to resolve the matter by getting the Interstate Commerce Commission to adopt formally its own Administrative Ruling as to their activities; the ICC had rejected their overtures. It was further demonstrated that the amount of non-agricutlural supplies hauled for nonmembers was less than 0.9 of 1 percent of all of the backhaul trips (which included member traffic and agricultural products exempt elsewhere under section 203(b)(6)). Based upon Department of Agriculture studies, it was estimated that the volume of trucking at issue was .00027 of 1 percent of total trucking operations in the Nation. In addition, the cooperatives were able to demonstrate that the seven motor carriers who appeared at the hearings on S. 1729 asserting injury had substantial overall growth rates and an increase in earnings. Moreover, when investigatory proceedings have been undertaken by the ICC, the cooperative involved has made its books available to the Commission.

In sum, the Department is of the opinion that the present exemption is consistent with Congressional intent and that it has not been abused in any sense to the significant detriment of regulated carriers. Our position in this regard reflects both civilian and military considerations. Transportation by agricultural cooperatives for the Department of Defense, while it has permitted efficient service and needed economics in the face of rising freight rates, has been extremely modest when compared to the total amount of traffic moved for that Department by all land carriers.

Section 203(b)(5) is a carefully drawn statute which properly recognizes that the needs of agriculture and those of the regulated for-hire industry must be carefully balanced if the public interest is to prevail. The Commission itself has been able to carry out this intent since the Northwest decision by developing a body of case law within the framework of the court's decision in such recent cases as *Edgerton Cooperative Oil Association—Investigation of Operations*, 105 M.C.C. 100, *Cache Valley Dairy Association Investigation of Operation*, 103 M.C.C. 798, and *Agricultural Transportation Association of Texas Investigation*, 102 M.C.C. 527. It is therefore apparent that the Commission is in a position to cope with any issues presented by the activities of cooperatives, and is not, in our opinion in need of further authority restrictive of a small but legitimate activity. It could also, for example, propose by rulemaking appropriate guidelines to clarify any uncertainties as might appear.

One possible amendment, as we view matters, is that necessitated by the failure of the Agriculture Marketing Act to classify the transportation of property for the U.S. Government or any of its agencies as non-member business. We would have no objection to such a clarifying amendment. As to H.R. 6530, however, we would oppose its enactment.

The Bureau of the Budget advises that from the standpoint of the Administration's program there is no objection to the submission of this report for the consideration of the Committee.

Sincerely yours,

JOHN L. SWEENEY,
Assistant Secretary for Public Affairs.

DEPARTMENT OF THE ARMY,
Washington, D.C., July 2, 1968.

Hon. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: Reference is made to your request for the views of the Department of Defense with respect to H.R. 6530, 90th Congress, a bill "To amend section 203(b)(5) of the Interstate Commerce Act to clarify this exemption with respect to transportation performed by agricultural cooperative associations for non-members." The Secretary of Defense has assigned to the Department of the Army the responsibility for expressing the views of the Department of Defense on this bill.

Section 203(b)(5) of the Interstate Commerce Act, 49 U.S.C. 303(b)(5), exempts agricultural cooperative associations, as defined in the Agricultural Marketing Act of 1929, from economic regulation by the Interstate Commerce Commission. On August 10, 1965, the United States Court of Appeals for the Ninth Circuit in the case of *Northwest Agricultural Cooperative Association, Inc.* v. *Interstate Commerce Commission*, 350 F. 2nd 252, cert, den. 382 U.S. 1011 (1966), judicially established the right of agricultural cooperative association truck lines to backhaul non-farm commodities for non-members. The court limited the legitimate extent of such traffic to that which is incidental and necessary to the farm-related transportation of the cooperative. Since that decision, the Department of Defense has utilized the transportation services of agricultural cooperative associations where their use was in the best interest of the Government.

H.R. 6530 would amend section 203(b)(5) of the Interstate Commerce Act to eliminate the present exemption from economic regulation except in those situations where the back-haul traffic is farm-related.

The Department of Defense is required under Chapter 137 of Title 10, United States Code, the former Armed Services Procurement Act, to procure the supplies and services it needs by competition to the maximum practicable extent. To deprive the Department of the use of the transportation facilities of bona fide farm cooperatives would deprive it of one of the alternatives management presently possesses to foster competition for military traffic.

Our experience to date demonstrates that farm cooperatives are capable of providing efficient service to the Department of Defense at reasonable cost without adverse impact on regulated carriers. The transportation capability of the farm cooperatives constitutes an important segment of the total United States transportation system. If farm cooperatives are to make their maximum contribution to the economy of the nation, their transportation facilities must be available to shippers in those situations where prudent management dictates their use. Otherwise it will not be possible to achieve the objectives outlined in the 1962 Presidential Transportation Message to the Congress wherein it was stated:

"The basic objective of our nation's transportation system must be to assure the availability of the fast, safe and economical transportation services needed in a growing and changing economy to move people and goods, without waste or discrimination, in response to private and public demands at the lowest cost consistent with health, convenience, national security and other broad public objectives. . . . This basic objective can and must be achieved primarily by continued reliance on unsubsidized privately-owned facilities, operating under the incentives of private profit and checks of competition to the maximum extent practicable."

For the foregoing reasons, the Department of Defense recommends against the enactment of H.R. 6530.

The enactment of the bill would remove an effective element of price and service competition and thus deprive the Department of Defense of a source of efficient and low cost transportation for freight shipments. As a result, budgetary requirements of the Department of Defense would be increased.

This report has been coordinated within the Department of Defense in accordance with procedures prescribed by the Secretary of Defense.

The Bureau of the Budget advises that, from the standpoint of the Administration's program, there is no objection to the presentation of this report for the considertaion of the Committee.

Sincerely yours,

STANLEY R. RESOR,
Secretary of the Army.

EXECUTIVE OFFICE OF THE PRESIDENT,
BUREAU OF THE BUDGET,
Washington, D.C., July 1, 1968.

HON. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This is in reply to your request for the views of the Bureau of the Budget on S. 752, an act "To amend sections 203(b)(5) and 220 of the Interstate Commerce Act, as amended, and for other purposes".

This Act is similar to H.R. 6530 in that it would restrict the statutory exemption from economic regulation given to transportation by agricultural cooperatives.

Unregulated transportation by cooperatives is extremely minor and limited in comparison to total for-hire truck and rail transportation and does not appear to have been abused or to have had any adverse effect on the regulated carriers. Such transportation provides revenues that are essential to the efficient operation of the cooperatives while also providing significant benefits and economies for the users.

Although we would have no objection to an amendment clarifying that transportation for the U.S. Government is "non-member business", we continue to believe, as expressed in our comments on H.R. 6530, that the present exemption properly recognizes and carefully balances the needs of agriculture, the regulated for-hire carriers and the public interest. We would therefore be opposed to enactment of S. 752.

Sincerely yours,

WILFRED H. ROMMEL,
Assistant Director for Legislative Reference.

DEPARTMENT OF AGRICULTURE,
Washington, D.C., June 28, 1968.

HON. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This will reply to your request of June 7, 1968, for a report on S. 752, a bill "To amend sections 203(b)(5) and 220 of the Interstate Commerce Act, as amended, and for other purposes."

This bill would amend section 203(b)(5), known as the agricultural cooperative transportation exemption, in order to limit and clarify the scope of the exemption and to assist the Interstate Commerce Commission in its enforcement operations. Specifically, there would be added to section 203(b)(5):

> Provisions under which the interstate transportation that could be performed by a cooperative association or federation of cooperative associations, for nonmembers who are neither farmers, cooperative associations nor federations thereof for compensation (except motor transportation otherwise exempt) would be limited to that which is incidental to its primary transportation operation and necessary for its effective performance, but in no event more than 15 percent of its total interstate transportation services in any fiscal year, measured in terms of tonnage.
>
> A provision that transportation performed by a cooperative association or federation for or on behalf of the United States or any agency or instrumentality thereof shall be deemed to be transportation performed for a nonmember.
>
> A provision that a cooperaative association or federation which performs interstate transportation for nonmembers who are neither farmers, cooperative associations nor federations thereof (except motor transportation other-

wise exempt) shall notify the Interstate Commerce Commission of its intent to do so prior to the commencement thereof.

A provision that in no event shall a cooperative association or federation which is required to give notice to the Commission transport interstate for compensation in any fiscal year of such association or federation a quantity of property for nonmembers which, measured in terms of tonnage, exceeds the quantity transported interstate for itself and its members in such fiscal year.

The bill would also amend section 220 of the Interstate Commerce Act by adding a new subsection which would authorize the Commission or its agents to have access to and authority, under its order, to inspect, examine and copy (but not prescribe the form of) accounts, books, records, memorandums, correspondence, and other documents pertaining to motor vehicle transportation of a cooperative association or federation of cooperative associations required to give notice to the Commission pursuant to the third provision described above.

The Department supports enactment of S. 752 in its present form.

In its original form, S. 752 was identical to H.R. 6530, introduced in the House of Representatives on March 2, 1967. These bills, if enacted, would have severely limited the scope of the exemption and would have impaired the efficiency and economy under which transportation is conducted by cooperatives in accordance with existing provisions of law.

In its report to your Committee under date of July 24, 1967, the Department expressed opposition to H.R. 6530. At the same time, however, the Department pointed out that there would appear to be merit in legislation which would clarify the scope of the exemption and assist the Interstate Commerce Commission in its enforcement of the motor carrier provisions of the Act.

To accomplish these objectives, the Department report suggested a number of clarifying provisions for inclusion in amendatory legislation. All of these suggestions are now embodied in S. 752, as passed by the United States Senate, and as presently before your Committee for consideration.

One additional provision is incorporated in the bill before you. That provision is a specific limitation on the amount of interstate transportation (except motor transportation otherwise exempt) which a cooperative association or federation of such associations may perform for nonmembers who are neither farmers, cooperative associations, nor federations thereof. Such interstate transportation, which the Department recommended be limited to an amount which is incidental to the primary transportation operation of the cooperative or federation and necessary to its effective performance, is also made subject to a specific limitation of 15 percent of the total interstate transportation services of the cooperative or federation.

The inclusion of a specific percentage limitation on the indicated traffic apparently stemmed from a concern on the part of regulated motor carriers that the limitation imposed by the terms "incidental" and "necessary" might permit a cooperative association or federation to transport a significant volume of such traffic, perhaps up to 50 percent of its total interstate volume. The 15 percent limitation should allay any such concern. The Department does not object to this limitation.

The Bureau of the Budget advises that there is no objection to the presentation of this report from the standpoint of the Administration's program.

Sincerely yours,

ORVILLE L. FREEMAN, *Secretary.*

DEPARTMENT OF THE ARMY,
Washington, D.C., July 2, 1968.

Hon. HARLEY O. STAGGERS,
Chairman, Committee on Interstate and Foreign Commerce, House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: Reference is made to your request for the views of the Department of Defense with respect to S. 752, 90th Congress, an Act "To amend sections 203(b)(5) and 220 of the Interstate Commerce Act, as amended, and for other purposes". The Secretary of Defense has assigned to the Department of the Army the responsibility for expressing the views of the Department of Defense on this Act.

Section 203(b)(5) of the Interstate Commerce Act, 49 U.S.C. 303(b)(5), exempts agricultural cooperative associations, as defined in the Agricultural Marketing Act of 1929, from economic regulation by the Interstate Commerce Commission. On August 10, 1965, the United States Court of Appeals for the Ninth Circuit in the case of *Northwest Agricultural Cooperative Association, Inc.* v. *Interstate Commerce Commission*, 350 F. 2d 252, cert. den. 382 U.S. 1011 (1966) judicially established the right of agricultural cooperative association truck lines to back-haul non-farm commodities for non-members. The court limited the legitimate extent of such traffic to that which is incidental and necessary to the farm-related transportation of the cooperative. Since that decision the Department of Defense has utilized the transportation services of agricultural cooperative associations where their use is deemed to be in the best interest of the Government.

S. 752, as introduced on 31 January 1967, would amend section 203(b)(5) of the Interstate Commerce Act to expressly state that in providing for-hire transportation to non-members, the agricultural cooperatives exemption applies only when the commodities transported consist of farm products, farm supplies, or other farm related traffic. The effect of such an amendment would be to eliminate the present exemption except in those situations where the back-haul traffic is farm-related. The amendment of section 203(b)(5) of the Act proposed in S. 752, as passed by the Senate on 4 June 1968, on the other hand, would place no such restriction as to the type of commodities that may be handled for non-members, but would limit presently authorized non-member traffic including transportation performed for the United States Government to an amount not to exceed 15% of the total interstate tonnage handled by such cooperatives during any fiscal year. Additionally, in order to assist the Interstate Commerce Commission in the enforcement of the cooperatives exemption, S. 752 as passed by the Senate requires that cooperatives shall give the Commission prior notice of its intent to perform transportation for non-members and for such purpose, make available all accounts, books, and records for Commission examination.

In letter to the Senate Committee on Commerce dated 24 July 1967 this Department opposed enactment of S. 752, as introduced, on the basis that the proposed amendment would totally deprive the Department of Defense of the use of transportation facilities of bona fide farm cooperatives and thus remove an effective element of price and service competition. For this reason the Department of Defense continues to oppose S. 752, as passed by the Senate.

While the amendments proposed in S. 752, as passed by the Senate, appear to have merit in that they should clarify the scope of the exemption and materially assist the Interstate Commerce Commission in its enforcement, this Department is particularly concerned with the provisions which would place a 15% limitation on non-member traffic. It is not known at this time whether this specific limitation considered together with the provision subjecting United States Government traffic thereto would materially reduce the ability of farm cooperatives to furnish transportation services to the Department of Defense. However, to the extent that this or any other percentage limitation would produce such a result, this Department strongly objects.

This report has been coordinated within the Department of Defense in accordance with procedures prescribed by the Secretary of Defense.

The Bureau of the Budget advises that, from the standpoint of the Administration's program, there is no objection to the presentation of this report for the consideration of the Committee.

Sincerely yours,

STANLEY R. RESOR, *Secretary of the Army.*

Mr. FRIEDEL. I am certain that all of the witnesses here today are aware of the time limitations under which the Congress is now operating in an effort to clear up its schedule of desirable legislation before the advent of the conventions in August, and the fact that we therefore have only a short time this morning in which we can compile a record on this problem.

I trust accordingly that the presentation of statements will be kept within reasonable bounds, although the entire statements, of course, will be included in the record.

Our first witness this morning is the Honorable Virginia Mae Brown, Vice Chairman of the Interstate Commerce Commission.

STATEMENT OF HON. VIRGINIA MAE BROWN, VICE CHAIRMAN, INTERSTATE COMMERCE COMMISSION; ACCOMPANIED BY GEORGE M. STAFFORD, COMMISSIONER; DALE W. HARDIN, COMMISSIONER; BERTRAM E. STILLWELL, DIRECTOR, OFFICE OF PROCEEDINGS; BERNARD E. GOULD, DIRECTOR, BUREAU OF ENFORCEMENT; ROBERT W. GINNANE, GENERAL COUNSEL; ROBERT L. CALHOUN, LEGISLATIVE COUNSEL; AND JAMES GLENN, CONGRESSIONAL LIAISON OFFICER

Mrs. BROWN. Good morning, Mr. Chairman and members of the subcommittee.

I want to first introduce the people I have with me from the Interstate Commerce Commission this morning.

Commissioner Stafford, Commissioner Hardin, Director Stillwell of the Office of Proceedings, Director Gould of the Bureau of Enforcement, and General Counsel Robert Ginnane. We have also Mr. Calhoun, our legislative counsel, and Mr. Glenn, our congressional liaison officer.

My name is Virginia Mae Brown. I am Vice Chairman of the Interstate Commerce Commission.

On behalf of the Commission, I wish to thank the subcommittee for this opportunity to testify on H.R. 6530, introduced by Chairman Staggers.

This bill is designed to clarify the scope of section 203(b)(5) of the Interstate Commerce Act which presently exempts from the Commission's economic regulation the transportation performed by Agricultural Cooperative Associations for nonmembers.

In addition to this bill, I will also be commenting on S. 752, as amended, and passed by the Senate on June 4, 1968, which deals with the same general subject although in a much different fashion.

H.R. 6530 implements one of the Commission's legislative recommendations transmitted to Congress last year by amending section 203(b)(5) so as to limit the transportation by agricultural cooperatives for nonmembers to farm products, farm supplies, or other farm related traffic.

This bill is identical to S. 752, as originally introduced and upon which the Commission testified before the Senate Subcommittee on Surface Transportation on July 24, 1967. (Hearings on agricultural cooperative transportation exemption before the Subcommittee on Surface Transportation of the Senate Committee on Commerce, 90th Cong., first sess., 1967.)

In the interest of saving the committee's time, I will not restate in detail our reasons for recommending this legislation. For the information of the subcommittee, a copy of former Chairman Tucker's testimony before the Senate subcommittee is attached at the conclusion of my prepared remarks.

Mr. FRIEDEL. That will be included in the record. Thank you.

Mrs. BROWN. As the attached statement points out in detail, the Commission for the last several years has been concerned over the effect which the transportation activities of exempt agricultural cooperatives for persons other than members of the cooperation on the Nation's regulated common carriers, in particular the extent to which

these exempt carriers were beginning to transport, on a substantial basis, commodities which bore no real relationship to the primary farm or farm related activities of these associations.

This situation was aggravated by the existence of certain agricultural cooperative associations that are only superficially qualified under the definition of such cooperatives set forth in the Agricultural Marketing Act of 1929, which is incorporated by reference in section 203(b)(5) of the Interstate Commerce Act, and by the decision in *Northwest Agricultural Cooperative Association* v. *Interstate Commerce Commission* (350 F. 2d 252 (9th Circuit 1965) cert. denied 382 U.S. 1011 (1966)) which relaxed to a considerable extent the limitations on the transportation activities of bona fide cooperative associations in a carrying non-farm-related products for nonmembers. It was against this background that we recommended enactment of S. 752 and H.R. 6530.

In the course of the Senate committee's deliberations on S. 752 in its original form, several alternatives to our initial proposal were offered by representatives of motor carrier and railroad industries and a representative of the National Council of Farmer Cooperatives.

As amended by the Senate committee and passed by the Senate, S. 752 represents a composite of the many views expressed in the course of the Senate hearings. Although the Department of Agriculture, along with the Departments of Defense and Transportation initially opposed any legislation in this area, the Secretary of Agriculture subsequently indicated a willingness to accept an amended version of S. 752 provided certain additional changes were made. These changes are included in the Senate-passed bill.

The additions made to section 203(b)(5) by S. 752 are set forth and discussed on pages 10 to 16 of the Senate committee's report (Agricultural Cooperative Transportation Exemption, Report No. 1152, 90th Cong., 2d sess.).

In essence, these amendments limit the interstate transportation for compensation by a cooperative for nonmembers who are neither farmers nor other cooperatives to that which is "incidental to its primary transportation operations and necessary to its effective performance" unless such transportation is otherwise exempt under part II of the act and places an upper ceiling on nonmember transportation by providing that in no event shall it exceed 15 percent of its total interstate transportation services, measured in terms of tonnage in any fiscal year.

S. 752 also requires a cooperative to give notice to the Commission of its intent to engage in transportation for nonmembers who are neither farmers nor another cooperative.

It also limits the total interstate transportation for compensation for all nonmembers (including that performed for farmers and others not subject to the 15-percent limitation) to a qauntity of property which is equal in tonnage to that which it performs for itself and its members in any fiscal year. Finally, S. 752 amends section 220 of the act so as to clarify our authority to inspect the books and records of a cooperative association.

As originally introduced, both S. 752 and H.R. 6530 would have limited transportation by exempt agricultural cooperative associations for nonmembers to "farm products, farm supplies, or other farm-related traffic."

We believed that these bills would have provided a fair and workable solution to the problems confronting both the Commission and common carriers subject to our jurisdiction which have resulted from the expansion of the transportation operations for nonmembers under present section 203(b)(5).

We continue to prefer the approach taken in these bills as originally introduced. However, subject to evaluation of such experience as may be gained thereunder, S. 752 as passed by the Senate would appear to be a step in the right direction.

We should note that some of the provisions of the subcommittee print, as revised, in particular the 15 percent limitation on nonmember traffic, will raise a number of novel questions with respect to administering and enforcing this exemption. It may be possible to minimize these potential difficulties through the establishment of appropriate rules and regulations defining the scope and application of this exemption as suggested by the Senate committee in its report. We have followed this procedure in the case of the exemption for the motor carrier transportation of agricultural commodities under section 203(b)(6), using the general rulemaking authority conferred by section 204(a)(6) of the act.

If S. 752 is enacted, it is our intent to initiate an appropriate rulemaking proceeding to implement the substantive portions of this act along the interpretative guidelines set forth in the Senate committee's report and to take such steps as may be required to give effect to the notice provision.

We believe that enactment of this bill will serve to prevent undesirable diversion of traffic from the Nation's essential common carriers while, at the same time, it will not unduly restrict the legitimate activities of exempt agricultural cooperatives. Accordingly, with the qualifications I have noted, we support enactment of S. 752.

This concludes my prepared remarks, Mr. Chairman.

(The statement of Chairman Tucker referred to follows:)

STATEMENT OF HON. WILLIAM H. TUCKER, CHAIRMAN, INTERSTATE COMMERCE COMMISSION, BEFORE THE SUBCOMMITTEE ON SURFACE TRANSPORTATION, SENATE COMMITTEE ON COMMERCE, JULY 24, 1967

Mr. Chairman, members of the subcommittee, my name is William H. Tucker. I am Chairman of the Interstate Commerce Commission and have served in that capacity since January 1, 1967.

On behalf of the Commission, I wish to thank the subcommittee for this opportunity to testify on S. 752, introduced by Senator Magnuson and Senator Lausche, which is designed to clarify the scope of the present exemption in section 203(b)(5) of the Interstate Commerce Act from the Commission's economic regulation of transportation performed by Agricultural Cooperative Associations for non-members. This bill implements one of the Commission's legislative recommendations transmitted to Congress on January 23, 1967, by amending section 203(b)(5) so as to limit the transportation by agricultural cooperatives for non-members to farm products, farm supplies, or other farm related traffic.

This bill is substantially identical to a specific proposal suggested by the Commission before this subcommittee in the 89th Congress as an amendment to S. 1729[1] and is designed to clarify the scope of the exemption contained in section 203(b)(5) in light of the so-called *Northwest Agricultural Cooperative* litigation which I will discuss subsequently.

Section 203(b)(5) of the Act, which this bill would amend, is one of a number of specific statutory exemptions from the comprehensive scheme of regulation of

[1] *Agricultural Cooperative Transportation,* Hearings before the Surface Transportation Subcommittee of the Committee on Commerce, United States Senate, 89th Congress, 2nd Sess., on S. 1729 (1966).

motor carriers set forth in part II of the Act. Under this section, motor vehicles controlled and operated by agricultural cooperatives, or by a federation of such cooperatives are exempt from the Commission's economic regulation provided the cooperatives meet certain qualifying criteria as defined in the Agricultural Marketing Act of 1929 (12 U.S.C. § 1141).

The Agricultural Marketing Act, as pertinent here, provides that an agricultural cooperative association ". . . [S]hall not deal in farm products, farm supplies, and farm business services with or for non-members in an amount greater in value than the total amount of such business transacted by it with or for members. All business transacted by any cooperative association for or on behalf of the United States or any agency or instrumentality thereof shall be disregarded in determining the volume of member and non-member business transacted by such association."

The original exemption from regulation for agricultural cooperatives was included in the Motor Carrier Act of 1935. In 1940, this exemption was expanded to include a federation of such cooperative associations, if such federation possesses no greater powers or purposes than cooperative associations so defined.

Although, in general, the only difficulty arising from this exemption for many years was whether, in a given fact situation, a particular operation qualified as an agricultural cooperative association within the definition of such an association under the Agricultural Marketing Act, in the early 1960's the Commission began receiving complaints from carriers and shippers in many sections of the country concerning the expanding operations of allegedly *bona fide* agricultural co-ops.

It was a very tedious process to investigate and bring to a conclusion all of these complaints. Necessarily, we attempted to deal with the problem by laying down broad guidelines. In 1961, the Commission held in the *Machinery Haulers Assn.* v. *Agricultural Commodity Serv.*, 86 M.C.C. 5, that for a co-op to enjoy the benefits of section 203(b)(5) of the Interstate Commerce Act it must meet the following tests:

(1) It must be operated and controlled by and for the benefit of its farmer members through its duly elected officers and directors.

(2) It must either own or control, under long-term lease, the vehicles which it uses to perform transportation.

(3) Its membership must be limited to those who were in fact producers of agricultural commodities.

(4) It may not perform transportation services functionally unrelated to its members' farming activities.

The guidelines established in this proceeding were largely left undisturbed by the courts until a decision was handed down by the United States Court of Appeals for the Ninth Circuit, in *Northwest Agricultural Cooperative Association* v. *Interstate Commerce Commission* 350 F. 2d. 252 (1965), *cert. denied* 382 U.S. 1011 (1966). Since this case is indicative of the problems which the provisions of S. 752 are designed to alleviate, it may be useful at this point to briefly outline the undisputed facts, stipulated by all of the parties involved, which prompted this litigation.

Northwest was and is a non-profit corporation organized under the Idaho Marketing Act for the purpose of enabling its members to collectively and economically transport their agricultural products to markets. It is solely engaged in transportation activities and operates a fleet of long-haul trucks for this purpose. On return trips from market places, Northwest transported farm supplies back to its members. However, the volume of these supplies did not equal the amount of farm products shipped outbound and, consequently, Northwest had empty space in its trucks. To make use of this space Northwest made a practice of backhauling non-farm-related commodities for non-members of the association. For example, it transported for non-members such things as furnaces, air conditioners, and water heaters from California to Idaho; machinery from Minnesota to Idaho; hardware from New Jersey to Oregon; wire springs from Illinois to Oregon; yarn from Oregon to Idaho; door hanger parts from New York to Oregon; and roofing materials from California to Idaho. From November 13, 1963, to March 19, 1964, Northwest received approximately $230,375 for transportation services. Approximately $41,000, or about 16 percent of that sum, was derived from the transportation of non-farm commodities for non-members. It was this latter type of transportation which the Commission sought to have stopped.

In support of its complaint, the Commission contended that transportation activities of agricultural cooperatives are not completely exempt under section 203(b)(5) from its economic regulation. We pointed out in this respect that an

agricultural cooperative is defined in the Agricultural Marketing Act as one dealing in "farm products, . . . farm supplies and/or farm business services." We admitted that transportation services performed for non-members of the association directly or functionally related to their agricultural activities, were exempt from economic regulation. But, we argued that for-hire transportation on non-exempt commodities for non-members of an association is not exempt, and thus Northwest's transportation of such commodities without a certificate of public convenience and necessity violated the Act.

Northwest's defense to the suit was that the transportation was exempt under section 203(b)(5). It pointed out that its for-hire transportation of non-exempt commodities for non-members produced much less revenue than it received from transporting member products, and that the income from such activities inured to the benefit of members of the association by economizing their marketing expenses. Northwest's president stated that if Northwest were denied access to this income from non-members, its cost of transporting the cooperative's farm products to market would exceed the cost of available common carriage and thus would force the cooperative to discontinue its operations.

Although a Federal District Court enjoined Northwest from transporting for compensation non-exempt commodities in interstate commerce by motor vehicle unless the transportation was directly beneficial or functionally related to the farming activities of Northwest's members or was authorized by appropriate authority, the Ninth Circuit Court of Appeals reversed this decision holding: (1) that a cooperative does not lose its status by engaging in activities other than its primary statutory activity, so long as they are incidental to its primary activity and necessary to its effective performance, and (2) that "* * * [O]n the uncontradicted facts Northwest's transportation of non-farm products and supplies was incidental and necessary to its farm-related transportation both in character and in amount—incidental because limited to otherwise empty trucks returning from hauling member farm products and farm supplies; necessary because it is not economically feasible to operate the trucks empty on return trips and because the additional income obtained is no more than that required to render performance of the cooperative's primary farm transportation service financially practicable."

Specifically rejecting the Commission's contention that a cooperative association may not deal at all in non-farm products, supplies, or business service, the Court concluded (1) that a cooperative will retain its exemption so long as it remains in essential character a "cooperative association" as described in the statutory definition, and (2) that the "* * * [R]eturn hauls * * * [A]re 'connected with farm operations,' for they are incidental and necessary to the effective performance of Northwest's * * *" "* * * trucking operation [which], viewed as a whole, is a farm service performed jointly by Northwest's members "for themselves', "and "* * * therefore did not deprive Northwest of its essential character as a 'cooperative association' under the Agricultural Marketing Act." At the same time, the Court stated, by way of caveat, that a "* * * cooperative would not be of the character contemplated by the statute if its non-farm related busines exceeded that which was necessary and incidental to its farm-related business, and in no conceivable circumstances could non-farm related business approach 50 percent of the total and remain incidental and necessary to that which was farm-related."

As I have previously noted, the Supreme Court, by its denial of the petition for a writ of certiorari, declined to review the Court of Appeals' decision. Although the Supreme Court has held that its denial of certiorari does not indicate approval of a lower court decision and that courts in other circuits are free to reach a result opposite from that taken by the Ninth Circuit, we are not optimistic over the prospect that the impact of the *Northwest* decision will be latered by judicial decision and, therefore, we are seeking enactment of this legislation. Pending enactment of this bill, we feel that the *Northwest* decision gives us no alternative but to sanction the transportation activities of these associations in non-farm related commodities for non-members where the record indicates that the association in question is a *bona fide* agricultural cooperative and its business handled for non-members is "incidental and necessary" to its primary function. This standard has most recently been applied in two proceedings, *Agricultural Transportation Assn. of Texas, Investigation of Operations*, 102 M.C.C. 527 (1966) and *Cache Valley Dairy Assn., Investigation of Operations*, 103 M.C.C. 798 (1967). In the first proceeding, which is now in the courts, we issued a cease and desist order against ATA of Texas, upon

finding that it was not a *bona fide* cooperative as defined by the Agricultural Margeting Act. In *Cache Valley,* however, we discontinued the proceeding upon finding that the Cache Valley Dairy Cooperative was a *bona fide* cooperative and engaged in non-member transportation only to the extent being "incidental and necessary" to its primary function. In this case, it appeared that the blackhaul reveues derived from non-member traffic in such commodities as beer, steel, lumber and rubber products averaged about one-half of the cost of the association's outbound hauling.

Although the *Northwest* decision failed to indicate at what point, short of the 50 percent limitation, a cooperative's transportation operation would cease to be "incidental and necessary" to its primary business function as a farm cooperative, it is expected that the transportation activities of these cooperatives will include an increasing amount of non-farm traffic for non-members and still be exempt from Commission regulation so long as such transportation does not approach 50 percent of the association's total transportation activities. Moreover, since under the Agricultural Marketing Act, all business transacted between a cooperative and a Federal Agency is disregarded in computing the volume of member and non-member business handled by a cooperative association, any percentage of business limitation is, however, essentially meaningless under the present law.

Since the Commission has no regulatory authority over the transportation activities of these associations, we lack the power to require reports from them which would indicate the amount and type of non-farm related traffic now being handled by exempt cooperatives for non-members. Although some limited data compiled by the Department of Agriculture in 1963 and 1964 before the *Northwest* decision indicated that only a small amount of traffic fell into this category, it is reasonable to assume that the Court of Appeals decision has stimulated expansion in this area, since whatever doubt may have existed over the legality of these activities has been removed. A clear indication of this is the decision of the Department of Defense to make use of exempt cooperative trucking for the handling of military shipments whenever it appears to be in the best interest of the government to do so.

Even though the exact amount of traffic handled by these associations cannot be precisely documented, it is clear that trucking operations performed by them for nonmembers possess certain economic characteristics which, when compared with the economic characteristics of the Nation's common carriers, rail and motor, make the traffic of the latter carrier's extremely susceptible to diversion. Since by law and in fact, cooperative associations are not primarily in the transportation business, it is not vital that these activities generate sufficient revenues from non-members to cover the full cost of operations plus a sufficient return on investment to hold and attract new capital. Indeed, it is conceded that the only need for engaging in these activities for non-members is to provide "backhaul" revenue in order to make the cooperatives' principal transportation activities—that of carrying their own members' traffic—economically viable at all. In addition, since these exempt activities do not constitute common carriage, these associations are free to pick and choose what traffic they wish to handle and on what terms they wish to handle it without regard to published tariff rates, adequacy of service, or any of the others economic regulatory duties imposed by law on common carriers. So constituted, it is readily apparent that the exemption afforded these associations by section 203(b)(5), as judicially interpreted, provides a potent economic weapon against the Nation's common carriers which form the backbone of our transportation system.

It is argued that, since the amount of non-farm traffic carried for non-members by these associations is so small, this or similar amendments to section 203(b)(5) designed to confine this exemption to reasonable limits are unnecessary. We do not agree with this argument. In our judgement, the *Northwest* decision has served to stimulate the transportation of non-farm traffic for non-members by these associations. In this regard, it has recently been brought to our attention that in at least one instance, an allegedly exempt cooperative is actively soliciting non-farm related traffic from commercial shippers who would ordinarily be making use of regulated common carriers. For some time, we have been concerned about the adequacy of common carrier service, particularly on small shipments. At the same time, we recognize that the carriers cannot be expected to fully carry out their common carrier responsibilities if much of their profitable revenue freight is being subjected to diversion by exempt motor carrier operations. It should not be necessary for common carriers to suffer traffic di-

version to these associations in large amounts before remedial action is required.

It is also stated that the effect of any legislation such as S. 752 is to place a higher value on the preservation of the business of regulated common carriers than on the prosperity of the Nation's agricultural producers, since any limitation on the exemption will allegedly render the transportation activities of these associations unprofitable and thus force their discontinuance with resulting higher transportation costs on the producers of agricultural products.

In our opinion, favorable consideration of this legislation does not require choosing between the unquestioned national policy of preserving and enhancing the agricultural sector of our economy on the one hand, and preserving and enhancing our system of common carriage, as contemplated by the National Transportation Policy, on the other.

It should be pointed out that the language used in this bill corresponds to that defining the primary functions of an exempt agricultural cooperative in the Agricultural Marketing Act and would re-establish what we believe to be the intent of Congress in enacting section 203(b)(5) as indicated by the portions of the Congressional debate on the exemption in 1935 which are attached as an appendix to my prepared statement. In administering this exemption prior to the *Northwest* decision, the Commission is not aware of any instance in which its decisions created serious economic harm to the transportation activities of these associations.

In addition, the effect of the *Northwest* decision must be viewed in light of the basic statutory scheme of regulation in part II of the Act as it pertains to the motor carrier activities of those engaged in agricultural activities. For example, section 203(b)(4a) exempts from regulation the transportation by a farmer of his own products or supplies. The problem raised by the *Northwest* decision, however, is that it permits farmers to band together to perform transportation that *each* farmer could not *lawfully* perform, i.e., a group of farmers (cooperative) may legally backhaul any traffic that will reduce their over-all cost of transportation, but under the statute a single farmer may not avail himself of such non-farm related back hauls solely to make his outbound transportation more economical and efficient.

Similarly, section 203(b)(6) exempts all agricultural commodities by any motor carrier from regulation but does not permit the backhauling of non-agricultural commodities in the interest of efficient or economical transportation except by regulated carriers holding duly issued certificates and permits.

Lastly, in order to make the activities of an agricultural cooperative more economical and efficient, the vehicles used in such operations have been given specific exemption in section 204(f) of the Act from this Commission's rules against trip leasing. The total statutory scheme of regulation, then, plainly reveals that there is no need for the broad and generous construction made by the Court of Appeals in the *Northwest* case. Considered in this light, we believe that the rather moderate amendment to section 203(b)(5) proposed by S. 752 will not result in the serious economic consequences alleged by past opponents of this measure. Nothing in this bill restricts the freedom of these associations to transport any commodities for their members while the limitation we are proposing for non-member traffic will, in our opinion, confine the exemption to reasonable bounds without at the same time inhibiting the economical use of a cooperative's transportation facility.

For these reasons, we urge favorable consideration of this bill. This concludes my testimony, Mr. Chairman.

Appendix

Excerpts From Legislative History of Section 203(b)(5)

When Congressman Jones offered the amendment to exempt agricultural co-ops from economic regulation, he stated:

"I want to assure the members of the committee as well as the Members of the House that there is no desire on the part of those who are interested in this amendment to open the floodgates. . . ." (79 Cong. Rec. 12220 (1935))

Congressman Terry, member of the House Interstate and Foreign Commerce Committee, made these statements during the consideration of the amendment:

"The Committee feels that to the extent the cooperatives are carrying and trucking their own property that they should be exempt, and they are exempt under the terms of the exception on page 9; that is, the casual, occasional, or

reciprocal transportation of property in interstate commerce by any person not engaged in transportation by motor vehicle as a regular occupation or business. All farmers are exempt under this provision and also under subsection 8.

* * * * * * *

"The farmer's operations are included in the exemptions that are in the bill. Every bit of trucking they do in transporting their own property is exempt; and the committee, after full consideration, felt that where the cooperatives go into the regular trucking business as such, that they should come within the provisions of the bill as to reasonable regulations." (79 Cong. Rec. 12221)

Congressman Whittington then stated:

"If the bill covers the matters that are intended to be covered by the proposed amendment, then the acceptance of the amendment would be merely a clarification of the bill, because many Commissions are rather hesitant as to the meaning of the word 'casual.'" (79 Cong. Rec. 12221)

Mrs. BROWN. In the report accompanying S. 752, as amended, it stated on page 15, and I quote:

The need for Commission rule-making power to administer the provisions of the Committee amendment is obvious.

The report goes on to give examples of the provisions of the bill which should be interpreted in rulemaking proceedings. Among those specified would be the establishment of guidelines covering the definition of the term "necessary for" and "incidental to" in accordance with the intent of this legislation.

Of course, there are areas of investigation in such a proceeding other than those mention in this report and no doubt found upon careful analysis of the bill and would be included therein.

In a similar situation, the Commission institute rulemaking proceedings into and concerning the matter of the terms "agricultural commodities not including manufactured products thereof." This was used in section 203(b)(6) of the Interstate Commerce Act. This case was the determination of exempted agricultural commodities and is reported in 52 MCC 511.

There we construed what at that time we considered the meaning of this exemption and with respect to what commodities were included therein.

So, I have no doubt that the rulemaking proceeding as suggested in the Senate report will be very helpful as an effective way to administer the proposed legislation.

Mr. FRIEDEL. I want to compliment you for your very fine opening statement.

Mr. Pickle.

Mr. PICKLE. Thank you, Mr. Chairman.

Mrs. Brown, is there agreement between the Interstate Commerce Commission and the Department of Agriculture with respect to S. 752?

Mrs. BROWN. It is my understanding that the Department of Agriculture and the Commission agree in regard to the position taken in S. 752.

Mr. PICKLE. Do we have a representative of the Department of Agriculture who will testify later this morning?

Mr. FRIEDEL. Yes.

rM. PICKLE. Now, is the Department of Defense satisfied about S. 752 at this date?

Mrs. BROWN. To my knowledge, the Department of Defense and the Department of Transportation have not changed their position. However, I don't understand that they are going to testify.

Mr. PICKLE. Do we have a representative of the Defense Department here this morning?

Do we know, Mr. Chairman, what their position is on this particular measure?

Mr. FRIEDEL. Mrs. Brown says they have not changed. They were opposed to S. 752.

You state they have not changed their views, Mrs. Brown.

Mrs. BROWN. That is my understanding.

Mr. PICKLE. As you understand it, what is the view of the Defense Department?

Mr. Chairman, inasmuch as I am asking for a statement of position with respect to another Department, I would ask that the record reflect what is the Defense Department's position on this measure if it is agreeable.

Mr. FRIEDEL. As I understand it, they are opposed to the bill.

Mr. PICKLE. I would like for it to be a part of the record if that is agreeable.

Mr. FRIEDEL. Without objection.

(See Department of Defense report, p. 9.)

Mrs. BROWN. That would be fine because I am not positive, Mr. Chairman, but I think possibly their statement of position was put in prior to amendment, as far as the record goes.

Mr. PICKLE. One other question.

Does this measure have anything to do with the rate to be charged for the hauling of any of these commodities? The rate structure is not involved in any way with respect to this measure; is that correct?

Mrs. BROWN. That is correct.

Mr. PICKLE. Mr. Chairman, I would like to reserve time for other questions I may have later.

Mr. FRIEDEL. All right.

Mr. Devine.

Mr. DEVINE. I have no questions, Mr. Chairman.

I want to welcome Mrs. Brown and commend you for a thorough and brief statement on behalf of the Commission.

Mrs. BROWN. Thank you very much, Mr. Devine.

Mr. FRIEDEL. Mr. Adams.

Mr. ADAMS. Mrs. Brown, it is nice to have you here this morning.

On page 3 and page 4 of your statement, the various limitations are confusing. I would like to go through them and perhaps you can tell me whether I have this right; starting with the paragraph at the bottom of page 3 and over to page 4, I would like to go through it.

As I understand the exemption, this is on back hauls for others; first their hauling must be incidental to farming; that is, the first one, except they may give 15 percent for nonmembers. Is that right?

Mrs. BROWN. That is right.

Mr. ADAMS. Then you allow, even though it may be a farm commodity and it may be for a farmer, you have a limitation on it that if they are nonmembers the total amount that is hauled in 1 year, even if it is a farm commodity, if it is for nonmembers must be less than 50 percent of the total amount that is hauled by the farmer.

You have about three balls in the air at the same time. I am trying to take them apart. Mrs. Brown, this is basically for the nonmember farmer.

Mrs. BROWN. You are correct.

Mr. ADAMS. So that the bill as it is now written says if you are a farm cooperative you must haul more than 50 percent for your members, for yourself. That is the first thing.

Mrs. BROWN. The only qualification to that is what they haul intrastate.

Mr. ADAMS. I won't get into intrastate.

Then the second thing is that this cooperative can go outside of its membership and outside of farm commodities for 15 percent but that 15 percent stays within the 50 percent.

Mrs. BROWN. Right.

Mr. ADAMS. In other words, you can haul yarn or hangers and so on up to 15 percent for nonmembers and then you can haul agricultural commodities up to less than 50 percent. Is that correct?

Mrs. BROWN. That is correct.

Mr. ADAMS. Those are the only exemptions unless there is some other category under part 2 that I don't happen to know about or have in front of me that would be exempted in any event. Is that your bill now?

Mrs. BROWN. That is right.

Mr. ADAMS. Thank you, Mr. Chairman.

Mr. FRIEDEL. Mr. Watson.

Mr. WATSON. Thank you very much, Mr. Chairman.

I apologize, Mrs. Brown, for not being here during your testimony in its entirety.

Pursuing Mr. Pickle's line of questioning a little bit, as I understand it, the Defense Department was against this. We do not know their position now since these amendments have been included in the bill. Is that your understanding?

Mrs. BROWN. Yes. I always hesitate to state another person's position but originally they were opposed.

Mr. WATSON. I think you are right in not trying to speak for someone else. It is confusing for us to get our own positions together here. Later on we can get some definitive position from the Department.

I appreciate your testimony.

Mrs. BROWN. Thank you.

Mr. FRIEDEL. As I understand it, the Defense Department enters into a contract with these agricultural cooperatives.

Mrs. BROWN. Yes.

Mr. FRIEDEL. Under the present law, they can bring back any commodity.

Mrs. BROWN. Yes. The court decision in the *Northwest* case, a lot of it stems from that, which is a relatively new interpretation.

Mr. FRIEDEL. The House bill and senate bill would correct that, in your opinion?

Mrs. BROWN. From here on after passage of this type bill, it would be subject to the 15-percent limitation.

Mr. FRIEDEL. Thank you, Mrs. Brown.

Mrs. BROWN. Thank you, Mr. Chairman.

Mr. FRIEDEL. Our next witness is Mr. George Dice, Director of Transportation and Warehouse Division, Consumer and Marketing Service, U.S. Department of Agriculture.

Mr. Dice.

STATEMENT OF GEORGE DICE, DIRECTOR, TRANSPORTATION AND WAREHOUSE DIVISION, CONSUMER AND MARKETING SERVICE, DEPARTMENT OF AGRICULTURE; ACCOMPANIED BY DONALD GRAHAM, ASSISTANT TO THE DIRECTOR, TRANSPORTATION AND WAREHOUSE DIVISION; AND MORRISON NEELY, OFFICE OF THE GENERAL COUNSEL

Mr. DICE. Good morning, Mr. Chairman and members of the committee.

May I introduce my associates?

On my right, Mr. Donald Graham, Assistant to the Director of Transportation and Warehouse Division.

On my left is Mr. Morrison Neely, attorney in the Office of the General Counsel of the Department.

I appreciate the opportunity to present this committee with the views of the U.S. Department of Agriculture on S. 752.

This bill would amend sections 203(b)(5) and 220 of the Interstate Commerce Act, as amended, for the purpose of clarifying the scope of the so-called agricultural cooperative exemption and of assisting the Interstate Commerce Commission in its enforcement operations. The Department supports enactment of this legislation.

The Department has filed a written report on S. 752 with this committee.

I will make one comment with respect to that report, sir. It points out that the Department did report adversely to the committee on H.R. 6530 on the basis that we felt that that bill would unduly restrict the operations of farmer cooperatives in transportation.

We did, however, point out also in that report that certain suggestions which the Department had made to this committee were also incorporated in S. 752 as passed by the Senate. I would like to comment briefly on this bill as passed by the Senate and now before you and on the issue which it concerns.

Over the years there has been considerable litigation before the Interstate Commerce Commission and in the courts with respect to the nature and amount of transportation which could be performed by cooperative associations, or federations of such associations, pursuant to the exemption contained in section 203(b)(5) of the Interstate Commerce Act. It is not necessary to describe this litigation in detail.

Generally, cooperatives and the Department of Agriculture supported an interpretation of section 203(b)(5) which would permit cooperatives to transport, in addition to their own and members' property, incidental quantities of property belonging to others, and to transport on backhauls nonmember property of a character which would otherwise be subject to regulation, provided the transportation of such property remained incidential to the transportation of property of the cooperative and its members. The Interstate Commerce Commission, the regulated motor carriers, and the railroads supported a more restrictive interpretation.

Ultimately some of those interested in the issue advanced legislative proposals with the intent to more definitively spell out the extent of the transportation operation which could be performed under the exemption, and particularly the nature and extent of the transporta-

96-778—68——4

tion which could be performed by a cooperative or federation for nonmembers.

In the interest of conservation of the committee's time, we will not go into detail with respect to these legislative proposals. A number of them are described in the report (No. 1152) issued by the Senate Committee on Commerce, in reporting on S. 752.

This bill resulted from consideration by the Senate committee of a subcommittee print also described in the report. In its report to the committee on that subcommittee print, the Department of Agriculture suggested a number of revisions. As pointed out in the committee's report, all of these revisions were adopted in S. 752 as reported by the committee. The committee also pointed out (on p. 18 of the report) that it had been advised that this version of S. 752 "would be acceptable to the Interstate Commerce Commission, three major farm groups which presented testimony or statements at the hearings—the National Council of Farmer Cooperatives, American Farm Bureau Federation, National Grange—as well as by the carriers—the American Trucking Associations and Association of American Railroads."

We are quite sure that those named above, as well as others who have testified or commented on legislative proposals in the past, were in general agreement with the objective of assisting the Interstate Commerce Commission in proceeding more effectively against illegal operators masquerading as bona fide agricultural cooperatives.

Similarly, most parties were agreed on the objective of clarifying the scope of the exemption. It is probably fair also to state that in accomplishing these objectives, all of those named above, as well as the Department, would have preferred some modification or variation from the specific proposal now before this committee.

The willingness of these interests to accept this approach to the accomplishments of the objectives would appear to us to be a rather strong endorsement of the bill. The Department recommends its enactment.

Mr. Chairman, I would like to comment briefly on this question of the limitation contained in S. 752. In doing so, I would like to clarify, first, transportation operations performed by cooperatives which generally are not subject to any controversy. They do transport property belonging to the cooperatives or the federation or property of the members of the cooperative federation. They also transport, and this has not been subject to controversy, incidental amounts for other nonmember farmers.

They also on occasion enter into reciprocal transportation; in other words, haul on a backhaul from an outbound movement, a load of traffic for another cooperative back in the same direction.

Now, other than this traffic there is the traffic which I would refer to as controversial traffic. This is traffic which would normally be handled by regulated motor carriers or by other common carriers. It is this traffic which has been subject to controversy.

Under this bill, if a cooperative or federation does not transport any of this so-called controversial traffic it is not subject to a limitation under this bill. In other words, it may haul exempt traffic under section 203(b)(6) of the act just as any private carrier may transport this traffic without limit, but if the cooperative elects to engage in transportation of this so-called controversial traffic then it is subject to certain limitations.

One of these limitations is that this traffic shall not be in excess of an amount which is incidental to the primary purpose of the cooperative or federation and necessary to its efficient or effective performance.

A second limitation is that it may not in any event exceed 15 percent of the total interstate transportation of the cooperative or federation.

Then, finally, if a cooperative or federation elects to engage in this controversial traffic, then the total amount of all nonmember traffic which it transports may not exceed the amount of member traffic which it transports in its fiscal year.

I shall be glad to answer any other questions that the committee has.

Mr. FRIEDEL. Thank you, Mr. Dice, for a statement which was very brief and to the point.

One thing that disturbs me about this legislation is that it is another effort to work out transportation policy on a piecemeal basis. We have a lot of problems in transportation.

To my way of thinking, the only way to work these problems out is in a comprehensive piece of legislation so that the interests of all modes of transportation, users, and the public can be weighed and properly balanced.

Mr. Dice, I want to thank you for your statement.

Mr. Pickle.

Mr. PICKLE. Mr. Dice, it would seem to me that if all of these groups, the Interstate Commerce Commission, USDA, the carriers, other agencies, are for this bill, who is against it? I am interested, though, in your comments with respect to the items that you call controversial items that would be shipped. I assume this would be items not directly or incidentally related to their own cooperatives.

Give me an example of what you mean by controversial items, items that get us into the category which requires these limitations of quantity.

Mr. DICE. On a backhaul, after transporting a load of its own commodities, a cooperative, if it does not have available farm supplies it is taking back or if there is not available an exempt commodity under section 203(b)(6), may transport a load of general groceries or roofing materials.

Mr. PICKLE. Give me an example of a cooperative starting off from its base and it ships a load of something to another part of the country and turns around. I would like to have a better idea of a specific commodity or commodities and what they would bring back.

Mr. DICE. Examples of what have been brought back would include general groceries, canned goods, that type of thing, roofing material, structural material, structural steel; I believe in some instances they have transported beer. Generally, commodities that are subject to regulations.

Mr. PICKLE. Would you classify as being related to their incidental operations lumber, steel, beer?

Mr. DICE. To an agricultural cooperative, I would not call that farm related or related to its operation.

Mr. PICKLE. In other words, on their backhaul, then they could bring back to this cooperative almost anything that would normally be sent by common carrier.

Mr. DICE. That is correct; within the limitations if this bill should be enacted. This would have to remain incidental to the primary transportation objectives of the cooperative and necessary to its effective performance.

You see, in transporting its own goods, if the cooperative returns empty in all instances obviously its transportation operation will not be efficient. The right to haul incidental and necessary traffic, the right to haul this otherwise regulated traffic to an incidental and necessary degree we have felt was the intent of the Congress in its original enactment.

Without regard to the question of congressional intent, now that we are talking about possible new legislation, we believe that it is desirable that this be permitted to the incidental and necessary degree and we have agreed, we have not raised objections to the 15 percent limitation.

Mr. PICKLE. Certainly as you have said if the cooperative shipped to and from a different point commodities which were directly related to their own operation then they could ship 100 percent of the goods and no limitation would be necessary.

Now, I think there would be some question of what would be the congressional intent, if they went outside of that, how much would they be allowed. I assume in your case, the U.S. Department of Agriculture, you would like to have for them a very large percent for the limitation and I assume that the Interstate Commerce Commission and the carriers would want it to be more limited in what that amount would be.

Mr. DICE. In its decision in the so-called Northwest Agricultural Cooperative case, the Ninth Circuit Court of Appeals made reference to the necessity that a cooperative maintain its status as an agricultural cooperative. While I can't quote it exactly from memory they said in effect that it is difficult to believe that this nonfarm-related traffic could approach 50 percent and still remain incidental and necessary to the cooperatives' primary purpose.

Mr. PICKLE. That is all, Mr. Chairman.

Mr. FRIEDEL. Mr. Devine.

Mr. DEVINE. No questions, Mr. Chairman.

Mr. WATSON. Thank you, Mr. Chairman.

Mr. Dice, I am in the same position as our chairman. We have had a number of bills before this subcommittee that have been unusual this year involving a lot of controversy. So, I haven't had an opportunity to read the Senate reports. So, if we could get a little background on this, I understand that the cooperatives were, of course, granted this exemption for a worthwhile purpose but then in order to make it more productive or lucrative they started the backhauls of virtually everything—steel, wire, refrigerators; everything else. So, then the Commission had to come in and try to take some corrective steps to control this.

Is that not the way the problem arose?

Mr. DICE. This is right.

Now, you referred to returning with almost anything. There is quite a considerable variety of this so-called nonfarm-related traffic or traffic that would be subject to regulations. But this doesn't mean that the cooperatives which transport this on backhaul do so in large

volume. Of course, if this bill is enacted, it would place a very definite limitation. But under the interpretation of provision 203(b)(5) by the Ninth Circuit Court of Appeals, the transportation of this nonfarm-related goods would have to remain incidental to the primary purpose of the cooperative and necessary to its efficient performance or efficient operation.

In several instances that has become well known, the *Northwest Agricultural Cooperative* case and the *Cache Valley* case which was the subject of litigation also, the amount of this backhaul traffic of nonfarm-related goods generally was in the range of 15 to 18 percent of the total interstate transportation.

Mr. WATSON. So even if we pass this bill here the cooperatives will be able to continue to perform virtually as they have been?

Do I construe that from your statement?

Mr. DICE. The Senate committee makes it clear, at least it makes clear its intent that the incidental and necessary language still prevails.

Now, the amount of transportation that a cooperative could undertake which would be incidental and necessary to its primary operation would depend in some measure on the area of the country in which it operates, the availability of other backhaul traffic, and the general nature of its operations. It could very well be that if a federation of cooperatives, for example, has members in several sections of the country, that the outbound movement from one of its members will make possible a backhaul movement from another. In such an instance, it might be that it could be determined that the amount of traffic which would be necessary to the effective operation of that cooperative might be less than 15 percent.

Now, if the 15-percent limitation were not there, there might very well be an instance where a cooperative with virtually no opportunity for backhaul traffic might haul something more than 15 percent of the nonfarm related goods and this might be quite appropriate in terms of making its operations efficient.

Mr. WATSON. Of course, in some instances, that is the very problem; they have been hauling substantially more than that, primarily on the backhaul.

Mr. DICE. I don't personally have any knowledge of instances of bona fide cooperatives that are hauling substantially more than that. Now, there may be such instances. If they are, I am not aware of them.

Mr. WATSON. Under the terms of the Senate bill, the cooperatives would be restricted to no more than 50 percent for nonmember traffic first.

Mr. DICE. If they engage in the transportation of any of this otherwise regulated traffic.

Mr. WATSON. That is right. But they would be limited to 50 percent nonmembers. What is the limitation presently if they do not choose or even if this bill passes, if they do not choose to come under the provisions of it, what is the limitation for cooperatives so far as nonmember traffic?

Mr. DICE. Under the Agricultural Marketing Act of 1929 and this proposed legislation would not change that, under the Agricultural Act, the cooperative could not remain a cooperative and do a total amount of nonmember business in excess of its member business. This is one of the criteria.

Mr. WATSON. In other words, they are limited to 50 percent nonmember business.

Mr. DICE. And this relates to all kinds of business.

Mr. WATSON. So we still retain the 50-percent limitation so far as nonmember business?

Mr. DICE. That is right.

Mr. WATSON. Second, if they choose to take advantage of this and they are limited to 15 percent of their total volume so far as incidental shipments.

Mr. DICE. Total interstate transportation; yes, sir. 50 percent of the total, both member and nonmember. That is right.

Mr. WATSON. I looked at the Senate bill, S. 752. On the first page, line 10, it says, "shall be limited to that which is incidental to its primary transportation operation."

Aren't we inviting just a constant lawsuit here as to construing incidental? What is incidental to its primary transportation operation?

Mr. DICE. Generally, that would be backhaul transportation after movement of a load for the cooperative or its members.

Mr. WATSON. What would the backhaul consist of? That is the problem. I know they have to have a backhaul business in order to make it somewhat economical.

Mr. DICE. The backhaul could consist of farm supplies. It could consist of reciprocal traffic, from another cooperative. It could consist of unmanufactured products of agriculture that are exempt under 203(b)(6) of the act. To the extent that it stays, assuming enactment of this legislation, within 15 percent of the total, then it could also transport the other commodities.

Mr. FRIEDEL. Will the gentleman yield for a brief question?

Mr. WATSON. Yes.

Mr. FRIEDEL. Would it include lumber if the farmer said he wanted to build a new barn, or roofing for a roof?

Mr. DICE. If it is for farm supply purposes, we think this would be included.

Mr. FRIEDEL. Would it include lumber, roofing, things of that sort, or would it be just agricultural products?

Mr. DICE. I would say this would come within the scope of farm supplies. I am not saying that lumber for any purpose. I am saying lumber for the purpose of construction and use on the farms of members.

Mr. WATSON. I was just going to pursue this a little bit and find out some specific things in your judgment which may be included or excluded.

Mr. PICKLE. I hope the gentleman will ask who makes this determination.

Mr. WATSON. I was going to ask that. I will ask it now.

Who will make the determination as to what is incidental and what is necessary?

Mr. DICE. The Interstate Commerce Commission.

Mr. WATSON. If their decision is not in line with the general common carriers, then we have an invitation for a lawsuit, do we not?

Mr. DICE. I suppose that whenever there is diagreement with the decision of the Commission there is potential for a lawsuit.

Mr. WATSON. When I was practicing law, we always said bless those who sue our clients, so I am not trying to knock the law business at all.

Would air conditioners be incidental to it?

Mr. DICE. Yes.

Mr. WATSON. You think that would be incidental?

Mr. DICE. The nature of the commodity does not, as I understand the legislation, have anything to do with the determination as to whether incidental and necessary. It is the amount of all of this traffic which would otherwise be subject to regulation.

Mr. WATSON. Mr. Dice, do you mean to tell me under the terms of this bill these cooperatives would be able to haul anything, just you looking at the volume rather than the actual item?

Mr. DICE. They could haul any commodity which would be subject to regulations within the limitation that it be incidental and necessary, within the limitation of 15 percent, and within the limitation that if they transport this type of goods, this traffic plus the other nonmember goods would have to not exceed 50 percent.

Mr. WATSON. In other words, they could haul anything just so long as it does not exceed 15 percent?

Mr. DICE. That is right.

Mr. WATSON. So it does not make any difference whether it is incidental to a farm operation, necessary to the farm operation at all? Is that your interpretation?

Mr. DICE. Subject to the limitation I indicated that if the Commission should find in a given instance that an amount less than 15 percent is all that is necessary to the efficient operation of the cooperative it could determine that not more than that could be transported.

Mr. WATSON. I can see we are in a very complex area here so far as interpretation. It says incidental to its primary transportation operation.

Of course, you are knowledgeable in this field, far more than I, but I can see where any two people differ on the interpretation as to what is incidental to its primary transportation operation. I thought its primary transportation operation was the transport of agricultural commodities. Isn't that the basis for the establishment of these cooperatives, to get the products to the market quickly?

Because they could not allegedly provide the transportation on schedule as necessary by the farmers in order to meet the farmers' needs, they set up the cooperatives and they could do it in a hurry. Isn't that the basic need for them?

Mr. DICE. That is right. On the basis that a cooperative or a group of farmers acting together can do so more efficiently than each individual.

Mr. WATSON. I agree in this field but oftentimes things start with the finest of purposes and then they branch out. Apparently that is what has happened now.

Mr. FRIEDEL. The time of the gentleman has expired.

Thank you very much.

Mr. DICE. Thank you, Mr. Chairman.

Mr. FRIEDEL. We have quite a few witnesses. I hope their statements will be brief.

The next witness is James F. Pinkney, chief counsel, Public Affairs, American Trucking Associations, Inc.

STATEMENT OF JAMES F. PINKNEY, CHIEF COUNSEL, PUBLIC AFFAIRS, AMERICAN TRUCKING ASSOCIATIONS

Mr. PINKNEY. Mr. Chairman and members of the subcommittee. My name is James F. Pinkney, and I represent the American Trucking Associations, Inc., 1616 P Street NW., Washington, D.C. 20036, an organization of the trucking industry representing all forms of motor carriers of property, and having affiliated State associations in 50 States and the District of Columbia.

We appear here today in behalf of the regulated common carrier system of motor transportation, which is being seriously jeopardized by the expanding for-hire transportation of general commodities by farmer cooperatives. We support S. 752 at this time, in preference to H.R. 6530.

S. 752, passed by the Senate June 6, 1968, would go a long way toward correcting a very troublesome and unhealthy situation in the transportation industry.

I refer to the situation caused by the decision in the so-called *Northwest* case (*Northwest Agricultural Cooperative Association, Inc.* v *ICC*, 350 F. 2d 252, certiorari denied by U.S. Supreme Court), in which the court held that an agricultural cooperative may transport nonfarm related commodities for nonmembers of the cooperative and still be exempt from economic regulation by the Interstate Commerce Commission, provided such transportation does not approach too closely to 50 percent of the cooperative's total transportation business. Stated bluntly, it held that agricultural cooperatives are free, subject to the percentage of business limitation, to engage in general trucking.

Seeking to capitalize on this decision, a number of transportation cooperatives, professing to be farmer cooperatives under the Agricultural Marketing Act of 1929, have entered into the business of transporting general commodities including, in the case of one large one, the transportation of very large quantities of munitions for the U.S. Government.

They transported those munitions both ways; it was not a backhaul situation. Its movements and those of many other such cooperatives have not been confined to incidental movements and have cut deeply into the business of many regulated for-hire motor carriers who are subject to all of the obligations and duties imposed by law on certificated carriers.

These farmer transportation cooperatives have not and do not assume any of the obligations and duties of common carriers and, in all instances known to us, have negotiated to transport freight at below normal tariff rates.

Of course, they don't have to take the bad with the good. They take only truckload quantities as the general practice and have no obligation to serve the public generally.

The bill before you, S. 752, would, as indicated above, bring the operations of these cooperatives more nearly into line with what we believe was definitely the intention of Congress when it enacted section 203(b)(5) of the Interstate Commerce Act—the section which, read in conjunction with the Agricultural Marketing Act, was designed to permit a farmer cooperative to transport farm-related property for nonmember farmers.

The bill does not roll back the exemption to the interpretation given it by the Interstate Commerce Commission, and which was in effect for many years prior to the *Northwest* decision, but would permit such transportation cooperatives to haul some general freight for the public generally but not to exceed an amount in tonnage that would exceed 15 percent of its total interstate tonnage.

The bill also provides machinery whereby the Interstate Commerce Commission would be able to police the activities of the cooperatives—which it now finds extremely difficult to do.

The instant bill has a long history culminating in a general expression of acceptability by all of the principal interests involved. I refer to the Department of Agriculture, the Interstate Commerce Commission, the Association of American Railroads, the American Trucking Associations, Inc., the National Council of Farmer Cooperatives, the American Farm Bureau Federation, the National Grange, and the Transportation Association of America.

We anticipate that several of the alleged agricultural transportation cooperatives will oppose. We also anticipate that these will be those cooperatives, including a great deal of munitions, that are engaged in the large-scale transportation for the general public between large areas in all parts of the United States and that these are the cooperatives presently under attack by the Interstate Commerce Commission or others for performing operations far beyond the scope of the Northwest decision under which they claim exemption.

I have attached typical newspaper advertisements or announcements by so-called farmer transportation cooperatives which indicate the aggressive nature of these people in seeking to transport traffic normally handled by certificated carriers.

We respectfully request this subcommittee promptly to report this salutary bill and to urge its early passage by the House of Representatives in its present form.

That concludes my statement, Mr. Chairman.

Mr. FRIEDEL. Thank you, Mr. Pinkney.

Do you want the attachments you have to your statement included in the record?

Mr. PINKNEY. I would, indeed, sir.

Mr. FRIEDEL. Without objection, it is so ordered.

(The documents referred to follow:)

UNITED AGRICULTURAL TRANSPORTATION ASSOCIATION OF AMERICA MARKETING CO-OP,
Lynwood, Calif.

Attention: Traffic Manager.

AT LAST A BREAKTHROUGH ON HIGH FREIGHT RATES

DEAR SIR: "Supreme Court sanctions co-op backhauls". The Ninth Court of Appeals in the Northwest Co-op v. ICC case. The decision of that court was that co-ops could back-haul regulated goods if it was necessary to their operation. This means that if a co-op has a rig in Chicago and it can't get an exempt load right away, it can pick up anything and return home rather than return empty. And, the co-op can do it without ICC authority of any kind. The only limitation is that more than half of the co-op's business must be in farm-related goods.

The above is now the law of the United States! Co-ops can do exactly as we have stated. The Supreme Court turned thumbs down on the ICC and the Justice Department who had wanted the Court to rule in their favor. And, the Supreme Court made its one sentence decision in a record three days!

We are allowed to haul 49% of our total freight for non-members which we need to get our trucks back from the east, as we haul from the West Coast to the East Coast for our members. Our members are all farmers and ranchers.

We have ample insurance for your protection. All of our equipment are late model trucks and our Vans are 40' in volume. As per the "Bill" quoted above, we can haul any type of freight coming back from the East Coast, and set our tariffs.

We are most anxious to be of service to you. I have personally been in and also associated with, the freight business for the past 20 years, both in produce and dry freight. Please feel free to call our office or drop us a line for any kind of additional information on rates etc.

Cordially yours,

HOWARD MECOM,
General Manager.

FARM CO-OPS OF AMERICA,
RETURN LOADS SERVICE,
Elizabeth, N.J.

Gentlemen: The U. S. Supreme Court ruled on January 25, 1966 (Case No. 809) that Farm Co-operatives now have the right to *backhaul* any commodity for any company whether or not the product is related to farming and whether or not the shipper is a member of a Farmers Co-operative.

See reverse side of this letter for reprint of news article from Transport Topics.

What this means if you are a shipper is that these farm co-op trucks can give you direct service from any city to any city at lower freight rates.

These exempt hauling tractor-trailers of all descriptions are now available to your company (with a couple of days notice) through this office which acts as a coordinator for the Farm Co-operatives delivering their goods in the greater New York area.

We guarantee the following:

a. Shipments direct—from your plant to your customer. No delay enroute—no transferring of freight—the driver who makes your pickup is the same driver who will make delivery. We are interested in 5000 lbs.—up to truckloads—same truck will make several pickups and several delieveries to various states—offering a unique service at truckload rates.

b. Because we are not regulated by I.C.C., our vehicles can travel as they wish over irregular routes to any city in the U.S.—Our rates are not regulated and we guarantee to reduce your present freight costs considerably.

c. Ship with full insurance protection—new equipment—clean, courteous drivers.

If you are interested in learning more about Farm Co-op Backhauling, please write or call.

Sincerely yours,

ED RHODES,
Eastern Co-ordinator, Farm Co-ops of America.

[Advertisement from May 1967 issue of the Wall Street Journal]

TRANSPORTATION DIRECTORS

We are an Agricultural Co-op fully qualified under the recent Northwest decision to haul your product as back-hauls incident to our business of hauling perishable commodities into the north. If you have loads from the north into the southeast, we may be able to work together advantageously. For further information call, or write:

National Growers' Marketing Association, Route No. 5, Farmers Market, Greenville, South Carolina; telephone 239–7609; George Dumit, General Manager; Kenneth Moody, Dispatcher.

Mr. FRIEDEL. I want to thank you for your very brief statement.

Mr. Pickle.

Mr. PICKLE. Mr. Chairman, I don't believe I have any questions. I understand the position of the association.

Mr. FRIEDEL. Mr. Devine.

Mr. DEVINE. Thank you, Mr. Chairman.

I don't think any questions are necessary.

Mr. FRIEDEL. Mr. Watson.

Mr. WATSON. Thank you, Mr. Chairman.

I think it is quite remarkable all these people have finally gotten together on this one particular bill. I have hastily glanced at some of these articles that you have put into the appendix of your statement. I agree with you that they are making a big pitch trying to get general business and do not restrict it to its primary purpose.

Referring to Mr. Staggers' bill, H.R. 6530, did I not understand someone earlier said Mr. Staggers' bill was too restrictive? It seems to me that it would give you, the common carrier, more protection than the Senate bill, S. 752.

Mr. PINKNEY. It would have, and we supported that approach to this problem initially, as did the railroads and other carrier interests. It became perfectly obvious that we had run into solid opposition from the farm community and the Department of Agriculture. So we tried to work out something that could at least give us some relief in the current situation. We believe this will be, as Mrs. Brown said, a step in the right direction—a long step in the right direction.

Mr. WATSON. Compromise, and let everybody live.

Mr. PINKNEY. Yes, sir. It also has the effect of permitting the Interstate Commerce Commission for the first time to obtain knowledge as to who is performing this nonmember transportation, because this bill does not apply until such time as one of these farm co-ops has notified the Commission that it intends to haul general freight. And then routinely the Commission may examine its books. That is also provided in the bill.

Mr. WATSON. Thank you.

Mr. FRIEDEL. Thank you very much, Mr. Pinkney.

Mr. PINKNEY. Thank you, gentlemen.

Mr. FRIEDEL. Our next witness is Mr. Harry Breithaupt, general solicitor for the Association of American Railroads.

STATEMENT OF HARRY BREITHAUPT, GENERAL SOLICITOR, ASSOCIATION OF AMERICAN RAILROADS

Mr. BREITHAUPT. Mr. Chairman and members of the subcommittee, mindful of the chairman's admonition as to brevity, I will present my statement for the record.

I will say for the purpose of the oral record that the railroads join with the Interstate Commerce Commission and the Department of Agriculture and the regulated motor carriers in endorsing and supporting S. 752 in the form in which it was passed by the Senate, and urge your favorable consideration of that measure.

(Mr. Breithaupt's prepared statement follows:)

STATEMENT OF HARRY J. BREITHAUPT, JR., GENERAL SOLICITOR, ASSOCIATION OF AMERICAN RAILROADS

My name is Harry J. Breithaupt, Jr. I am General Solicitor of the Association of American Railroads, with headquarters at the offices of the Association in Washington. I appear in behalf of the member lines of the Association of American Railroads, by authority of its Board of Directors, in support of S. 752 as passed by the Senate on June 4, 1968.

Section 203(b)(5) of the Act (which this bill would amend) exempts from economic regulation by the Interstate Commerce Commission—motor vehicles controlled and operated by a cooperative association as defined in the Agri-

cultural Marketing Act, approved June 15, 1929, as amended, or by a federation of such cooperative associations, if such federation possesses no greater power or purposes than cooperative associations so defined.

Such motor vehicles are thus exempt by that section from all of the provisions of part II of the Interstate Commerce Act (the so-called Motor Carrier Act) except those provisions relative to qualifications and maximum hours of service of employees and safety of operation or standards of equipment.

For a number of years the Interstate Commerce Commission has expressed concern about abuses and other evils growing out of this escape provision of the Act. Others, too, have been concerned. The Commission's principal concern in this regard in past years and the principal concern of others as well up until late 1965 and early 1966 was abuse—sometimes flagrant—of the statutory exemption occurring through subterfuge and deceit practiced by persons who in order to escape economic regulation of general for-hire transportation services performed by them operated unlawfully under the guise of agricultural cooperative associations.

During the course of hearings conducted by a Subcommittee of the Senate Commerce Committee in July of 1966, several witnesses showed by actual examples and case histories just how bogus or phony or fake agricultural cooperative associations have been used as cover for illict transportation activities. The record of those hearings, which were directed to S. 1729 (89th Congress), contains a great deal of well-documented material on that subject. There is no need to repeat it here.

In any event, the principal problem in connection with the agricultural cooperatives exemption is no longer that the eremption is being abused by means of spurious cooperatives. I do not mean to say that the exemption is no longer used as a guise for the performance of unlawful transportation. That troublesome problem has not gone away. Comparatively recent developments, however, have produced a problem that is more serious than that to which the earlier bill was directed.

I refer to the decision of the United States Court of Appeals for the Ninth Circuit in *Northwest Argicultural Cooperative Association, Inc.* v. *Interstate Commerce Commission*, 350 F. 2d 252 (1965), and to the Supreme Court's denial of *certiorari* in that case on January 24, 1966.

The *Northwest* case involved a non-profit corporation formed under the Idaho Cooperative Marketing Association Act for the purpose of enabling its members collectively and economically to transport their agricultural products to markets. Northwest was, and presumably still is, engaged solely in transportation activities with a fleet of long haul trucks. On return trips from market areas, Northwest transported farm supplies back to members of the cooperative. The volume of these farm supplies did not equal the volume of farm products shipped on the outbound trips, however, and consequently Northwest had available empty backhaul space in its trucks. In order to utilize this space Northwest backhauled non-farm-related commodities for non-members of the association for compensation.

For example, Northwest transported for non-members furnaces, air conditioners, and water heaters from California to Idaho; machinery from Minnesota to Idaho; hardware from New Jersey to Oregon; wire springs from Illinois to Oregon; yarn from Oregon to Idaho; door hanger parts from New York to Oregon, and roofing materials from California to Idaho. During a four-month period in 1963–1964 Northwest received approximately $230,375 for transportation services, of which some $41,000, or about 16 percent, was derived from the transportation for non-members of non-farm commodities.

The Interstate Commerce Commission brought suit in 1964 in the United States District Court for the District of Oregon to enjoin Northwest from this hauling of general commodities for-hire throughout the country, for non-member merchants and manufacturers, without a certificate of public convenience and necessity.

The Commission contended that transportation activities of agricultural cooperative associations are not completely exempt from economic regulation under section 203(b)(5) of the Interstate Commerce Act. It pointed out that an agricultural cooperative is defined in the Agricultural Marketing Act as one dealing in "farm products . . . farm supplies and/or farm business services." It conceded that transportation services performed for members of a cooperative that are "directly or functionally related" to their agricultural activities are exempt from economic regulation. It argued, however, that for-hire transportation of non-

exempt commodities for non-members of an association is not exempt, and thus that Northwest's transportation of such commodities without a certificate of public convenience and necessity violated the Act.

Northwest defended on the ground that all of its transportation activity was exempt from regulation under section 203(b)(5). It pointed out that its for-hire transportation of non-exempt commodities for nonmembers produced much less revenue than it received from transporting products for its members, and that the income from these outside activities inured to the benefit of Northwest's members by economizing their marketing expenses.

The district court permanently enjoined Northwest from "transporting, by motor vehicle in interstate commerce on public highways for compensation, property other than that which is exempt from economic regulation under the Interstate Commerce Act, unless either (1) such transportation is directly beneficial or functionally related to the farming activities of defendant's members, or (2) there is in force and in effect, with respect to * * * [Northwest] a certificate or permit or other authorization issued by the Interstate Commerce Commission authorizing it to engage in such operations." The court found (234 F. Supp. 496, 498):

> * * * The difficulty with defendant's position is that it sanctions for-hire transportation in open competition with regulated common carriers without subjecting the Association's [Northwest's] fleet to regulation. Though Congress intended to exempt agricultural cooperatives from regulation under the Act in the transportation of their goods to market and their necessary supplies and services on return, I do not read the statute as granting these associations an exemption to enter the general transportation business. Undoubtedly, the Association's practice affords economies to its members, but these are economies not intended to be conferred by the Act.

This seems to us to have been a sound decision, but on appeal by Northwest to the United States Court of Appeals for the Ninth Circuit the district court's decision was reversed. The court of appeals first held that, since the agricultural cooperative exemption in the Interstate Commerce Act applies broadly to "motor vehicles controlled and operated by a cooperative association as defined in the Agricultural Marketing Act," the limitation upon Northwest's transportation activities urged by the Commission "must be found in the definition of a cooperative association in the Agricultural Marketing Act."

The court then held that "a cooperative does not lose its status by engaging in activities other than its primary statutory activity so long as they are incidental and necessary to its effective performance," and that "Northwest's transportation of non-farm products and supplies was incidental and necessary" to the effective performance of Northwest's farm service within that test.

The Solicitor General, on behalf of the Interstate Commerce Commission, filed a petition for a writ of certiorari; but the Supreme Court denied review.

Thus, it is clear that the problem is no longer merely one of transportation performed by fictitious or spurious agricultural cooperative associations, but is now one of much broader scope and impact. Under the court of appeals' decision a *bona fide* agricultural cooperative association may perform transportation services of non-farm-related commodities for non-members of the association, and do so for-hire and yet wholly exempt from economic regulation by the Interstate Commerce Commission. The only limitation appears to be that a cooperative's non-farm related business must not too closely approach fifty percent of the cooperative's total business. The court said (350 F. 2d 252, 256):

> *A cooperative will retain its exemption only so long as it remains in essential character a "cooperative association" described in the statutory definition.* Thus the activities in which it engages must be such that the cooperative can be fairly described as a farmer organization primarily engaged in marketing farm products for farmers, or purchasing, testing, or furnishing farm supplies or farm services for farmers; and operating for the benefit of the members of the cooperative in their capacity as producers of farm products or purchasers of farm supplies or farm business services. *A cooperative would not be of the character contemplated by the statute if its non-farm related business exceeded that which was necessary and incidental to its farm-related business, and in no conceivable circumstances could non-farm related business approach fifty per cent of the total and remain incidental and necessary to that which was farm-related.* [Italics supplied.]

This decision, with the situation it has created, poses a very serious problem for the regulated carriers. It is fraught with much more difficulty and potential harm for them than the older problem of spurious co-ops. Wholesale diversion of traffic from the regulated common carriers (both truck and rail) is likely, indeed certain, to occur. The potential is there, and the raiding has already started. It is not easy to point to specific examples of diversion. The nature of exempt transportation and the circumstances under which exempt transportation is performed are such that there is an air of secrecy about it. Agricultural cooperatives, like other exempt haulers, are free of those provisions of the Interstate Commerce Act requiring the publication of rates, the filing of reports, etc.

About the only information available to us as to the nature of the nonmember transportation these cooperatives are performing, or undertaking to perform, comes to us from rate quotations they are making in connection with Department of Defense traffic. There we can see the bids they submit, and we can learn the extent to which they are undercutting rail and regulated motor carrier rates. Even in the case of this military traffic transported by cooperatives, however, the information available to us is fragmentary and incomplete; and the military traffic is a very small part of the overall picture.

The broad-scale exemption from economic regulation now available to agricultural cooperative associations in the transportation of non-farm-related commodities for non-members gives them a tremendous advantage in competition with the closely regulated rail and motor carriers for such traffic. The cooperatives' transportation charges are not subject to control by the Interstate Commerce Commission, and they are free to go as low as they please in their efforts to attract traffic for what would otherwise be empty backhauls. Indeed there is nothing in the Court's decision that limits the exemption to backhauls.

As the Solicitor General of the United States said in his petition to the Supreme Court for a writ of certiorari (*Interstate Commerce Commission* v. *Northwest Agricultural Cooperative Association, Inc.*, No. 807, October Term 1965):

> The decision below now holds out the clear prospect that cooperatives will, in the future, be able to obtain substantial backhaul tonnage by diverting traffic in non-farm related commodities from regulated motor and rail carriers. Such cooperatives may charge unregulated rates for the purpose of deriving some contribution to the cost of round trip movements. Such rates will be as low as necessary to divert traffic from the regulated carriers which rely exclusively upon transportation revenues for their livelihood. The record in this case illustrates the range of commodities which is subject to such diversion.
>
> Finally, while the present case on its facts involves only the backhauling of non-farm-related commodities, the principle announced by the court of appeals might also be applied to other transportation of such commodities deemed "necessary and incidental" to the cooperatives' farm-related activities. As one example, a cooperative association which has trucks wholly idle at certain seasons of the year might, on the basis of this decision, employ them during those periods in for-hire transportation of the products of a nearby manufacturing plant.

Nor should it be overlooked that the sweeping exemption now available to *bona fide* agricultural cooperative associations is almost certain to encourage and spur the formation and use of spurious agricultural cooperaives as a means of evading ICC regulation. Illicit transportation of this kind will surely increase. There is now a much greater incentive, or temptation, than heretofore for artifice, sham and deception.

As the law now stands, then, agricultural cooperatives may transport anything for anybody, anywhere, at any rate—entirely free of any economic regulation whatsoever—subject only to the nebulous condition that its transportation activities with respect to non-farm products and supplies be "incidental and necessary" to its primary statutory activity.

The railroads, on the other hand, are required to establish rates that meet statutory standards of justness and reasonableness; to file and publish them for all the world (including the gricultural cooperatives) to see; to adhere strictly to those rates; to forgo any changes in them (absent special circumstances) except upon thirty days' notice; to observe the prohibition and requirements of the long- and short-haul clause, and the aggregate of intermediates clause, in section 4 of the Interstate Commerce Act; and to avoid unjust or undue discrimination, preference or prejudice.

The regulated motor carriers are, speaking generally, subject to these same or similar regulatory restraints.

Agricultural cooperatives are subject to none of these restraints and are privileged to make whatever rates they choose to make, at any time, without notice to anyone and without publication, on whatever basis they regard as necessary to obtain the traffic.

Furthermore, agricultural cooperatives are wholly free of the legal obligation that common carriers have to serve the general public over authorized routes, between named origin and destination points, without selectivity. The railroads, for example, must (within recognized limitations) transport anything for anybody, anywhere.

The farm cooperatives are under no obligation at all to serve the general public. They are free to "pick and choose" traffic as they please, soliciting the most desirable and most lucrative traffic and rejecting that which they do not care to transport.

You can see the intolerable competitve situation in which the railroads and the regulated motor carriers find themselves. You can see that exemption results in no measurable benefit to the general public; that it does nothing to improve or strengthen our national transportation system.

For all thes reasons, we are willing at this time to endorse and support S. 752 in the form in which it was passed by the Senate. It is not as strong a bill as we had hoped the Congress would enact but it is, on the whole, constructive legislalation; and, on balance and everything considered, appears to reflect a reasonable compromise of conflicting interests.

Mr. FRIEDEL. Thank you.

Mr. Pickle.

Mr. PICKLE. No questions.

Mr. FRIEDEL. Mr. Devine.

Mr. DEVINE. No questions.

Mr. FRIEDEL. Mr. Watson.

Mr. WATSON. Mr. Chairman, I might comment we have had such a happy marriage going along I move that we report this bill out before somebody starts rocking the boat here.

I appreciate the gentleman's statement.

Mr. FRIEDEL. Mr. Springer.

Mr. SPRINGER. No questions.

Mr. FRIEDEL. Thank you, Mr. Breithaupt.

Mr. BREITHAUPT. Thank you, sir.

Mr. WATSON. Our next witness is Mr. Harold Hammond.

STATEMENT OF HAROLD HAMMOND, PRESIDENT, TRANSPORTATION ASSOCIATION OF AMERICA; ACCOMPANIED BY FRANK A. SMITH, VICE PRESIDENT OF RESEARCH

Mr. HAMMOND. Mr. Chairman, my name is Harold Hammond, I am president of the Transportation Association of America. I have with me Frank A. Smith, our vice president of research.

In summary, the Transportation Association of America strongly supports passage of S. 752 as passed by the Senate.

I think the primary group in TAA that you would be interested in that was back of this legislation was one composed of the users of transportation. We have a special group of over 100 representatives of all types of users that buy transportation from the regulated carriers. This group was much in favor of S. 752 as passed by the Senate. They supported it.

You will find in my statement before you, on pages 4 to 6, some examples of what we do not like to see happen and as Mr. Pinkney

pointed out, some of the things that the undesirable co-ops are doing today in looking for business and taking it away from the regulated carriers. We have been working on this for over 20 months.

We are happy to see a compromise worked out here which is now agreed to by all the regulated carriers and by the regulatory agency and by some of the departments and the Government.

In summary, I think that the proposed legislation would be most helpful to the regulated carriers. Certainly, it would be helpful to the Interstate Commerce Commission and it will be good for the bona fide co-ops.

For these reasons, the Transportation Association of America urges consideration of S. 752 at the earliest possible date.

(Mr. Hammond's prepared statement follows:)

STATEMENT OF HAROLD F. HAMMOND, PRESIDENT, TRANSPORTATION ASSOCIATION OF AMERICA

My name is Harold F. Hammond. I am President of the Transportation Association of America, with headquarters in Washington, D.C. I am appearing before your Subcommittee today on behalf of the Board of Directors of TAA, of which I am a member, in support of S. 752, as passed by the Senate. This bill in brief, would clarify the nature and scope of traffic that can be hauled by agricultural cooperatives exempt from economic regulation by the Interstate Commerce Commission.

For the record, TAA is a national transportation policy organization composed of transport users of all kinds, investors and carriers of all modes who work together to help develop sound national policies that will assure the strongest possible transport system under private enterprise principles. Policy positions are adopted by a 115-member TAA Board, but only after receiving recommendations from its eight permanent advisory Panels, on which serve about 350 top executives from the following respective transport interests: Users, Investors, and Air, Freight Forwarder, Highway, Pipe Line, Railroad, and Water Carriers.

TAA INTEREST IN CO-OP EXEMPTION

TAA's interest in this legislation is directly related to its long-known interest in the so-called illegal for-hire trucking problem. The Association has long been on record as opposing the entry of unlawful carriers into the general for-hire transport field. As your Subcommittee will recall, TAA was a strong supporter of legislation considered over a period of years designed to strengthen both federal and state enforcement powers in this problem area. Congress passed such legislation in 1965, now known as Public Law 89–170.

Along these same lines, TAA's objective in this current legislative effort is to prevent illegal for-hire motor carriers from engaging in general for-hire transportation under the guise of being an exempt farmer cooperative. Since at present there is no requirement that an organization claiming to be an agricultural cooperative must prove that it is bona fide prior to operating under Section 203(b)(5) of the Interstate Commerce Act, the door is wide open for illegal motor carriers to use this as a guise to engage in for-hire transportation beyond the regulatory control of the ICC.

The ICC claims that the illegal use of this exemption has resulted in the diversion of substantial amounts of important traffic from regulated motor and rail carriers by various groups and organizations posing as farmer cooperatives. It says that it is "unable to cope with this situation effectively because of the necessity of overcoming in each case a presumption of eligibility."

ENFORCEMENT IS DIFFICULT

To prove ineligibility under present statutes is not an easy task, since it takes considerable time to gather evidence against such operators. Even then, the issuance of a cease and desist order by the Commission carries with it no financial penalties, which would be applied only if such an order is not complied with and the Commission takes formal court action to enforce it. This is obviously a time-consuming procedure, which is complicated further by the practice of some pseudo farmer cooperatives of changing their names, location, or form of organiza-

tion sufficiently to force an entirely new investigation and issuance of a cease and desist order.

The question can be raised whether passage of P.L. 89–170 has made it easier to take enforcement action against illegal farmer cooperatives. While it is true that such cooperatives are subject to the provisions of this recently passed public law, the fact remains that the burden of proving their ineligibility to use the co-op exemption still rests with the ICC or any plaintiff in a court suit. Since farmer cooperatives can now lawfully engage, within certain broad limits, in the for-hire transport of general commodities for nonmembers, the problem of identifying the illegal ones is very difficult. As a result, the effectiveness of P.L. 89–170 in this area of enforcement is definitely restricted at this time.

EFFECT OF NORTHWEST CO-OP CASE

A much more serious complication has arisen as a result of the Supreme Court's action last year which, in effect, upheld an appellate court's ruling in the Northwest Agricultural Cooperative Association Case [350 F. 2d 252 (9th Circuit, 1965) certiorari denied (1966)] that the farmer cooperative exemption should be interpreted broadly to permit the backhaul of general commodities for nonmembers so long as revenues therefrom do not exceed its cooperative function revenues and are incidental and necessary to the cooperative's primary legal activity.

The effect of this court decision is to permit farmer cooperatives lawfully to engage in extensive for-hire transportation for nonmembers. Since there are approximately 8,600 farmer cooperatives in the United States, the potential competition to regulated carriers is sizeable. Furthermore, since many of these cooperatives are multi-million-dollar organizations, their potential for engaging in general for-hire transportation beyond ICC economic regulation is equivalent to the scope of operations of many of the larger regulated motor carriers.

The combined adverse effect of these two factors—the difficulty of determining a co-op's eligibility and the liberal interpretation of the exemption by the courts—clearly shows the need for remedial legislative action as soon as possible.

SPECIFIC EXAMPLES OF CO-OP TRAFFIC SOLICITATION

We believe immediate legislative action is needed to prevent a rapid rise in traffic solicitation activity on the part of farmer cooperatives, or organizations posing as such, in the general freight field. As an illustration of this, we can cite a number of specific examples furnished us by various shipper members of TAA. Excerpts from letters sent to us by traffic executives of some of the nation's leading corporations include the following:

1—"A few months ago, a representative of an Illinois farm co-op phoned me. The purpose of the telephone call was to offer the transportation of his co-op in hauling our shipments (*hardware manufacturer*) from Louisville to to any point in the state of Illinois. He indicated that the rates could be negotiated." (Underline words added.)

2—"There is enclosed a copy of letter received from one of the farmer cooperatives." (Copied in part from letter from the Milk Producers Marketing Co., Kansas City, Kansas, to a major *glass manufacturer*.)

> 'I want to thank you for the time you gave me during our phone conversation of two weeks ago, regarding transportation. This is a confirmation of the following rates I quoted you, based on a 40,000 minimum, to California points. Pittsburgh Area, 3.50 cwt.; Akron, Ohio, 3.00 cwt.; St. Louis, 2.50 cwt.; and Chicago, 2.75 cwt. It is our sincere desire to further acquaint you with our ability to be of service to you, and if given the chance I am sure we can cement a very pleasant relationship. Won't you at your earliest convenience let us hear from you?'

3—"Recently, we received an order which called for the material to be shipped via the XYZ Dairy Co., which included notation 'Customer Pickup.' The order indicated that the material was sold to one of our major customers in XYZ. In checking into this transaction, it developed that XYZ Dairy was to pick up the shipment in their truck and make delivery to two customers in XYZ. Once we developed this fact, we immediately ran a check on the XYZ Dairy Co. to determine if it was a bona fide co-op. We found that this company was not a farmer co-op and, therefore, we made other arrangements to make shipment." (Names indicated by XYZ at request of shipper, whose company is in the *chemical business*.)

4—"Our field people report that occasionally our distributors or jobbers (an oil company) in the farm belt area of Iowa, Kansas, Nebraska, etc. insist on our using a co-op trucker, even though we pay the freight, and charges are assessed at the common carrier level—with no expense saving whatsoever to us. At first we attempted to resist using these truckers, but for reasons with which we do not entirely agree, our Marketing people prevailed upon us to comply when such requests are made." (Underlined wording added.)

From these examples you can see that farm cooperatives are not hesitant about soliciting traffic that obviously is in no way related to farm business. The above examples, to illustrate this point, cover hardware, glass, chemicals, and petroleum products. Some farmer cooperatives use the Northwest Case as the basis for open solicitation of traffic managers to haul freight of any kind on a negotiated rate basis beyond any regulatory jurisdiction of the ICC. Two specific examples of this type of solicitation are cited below and on the following page.

The first example of an open solicitation for general freight by a farmer cooperative is the following ad that appeared in the "Wall Street Journel" a short time ago. The other example is the solicitation form letter shown on the next page.

TRANSPORTATION DIRECTORS

We are an Agricultural Co-op fully qualified under the recent Northwest decision to haul your product as back-hauls incident to our business of hauling perishable commodities into the north. If you have loads from the north into the southwest, we may be able to work together advantageously. For further information call, or write: National Growers' Marketing Association, Route #5, Farmers Market, Greenville, South Carolina, Telephone 239–7609, George Dumit, General Manager, Kenneth Moody, Dispatcher.

One disturbing feature about both the form letter and ad cited above is the reference therein to the Northwest Case decision. In both instances, this decision is used as the legal basis for the solicitation of freight of any kind. While brief reference is made to the incidental and necessary test and back-haul limitation set forth by the court, it is inconceivable to us that the shipper will be able to know whether or not his traffic complies with these standards. While the shipper may be able to determine whether his traffic is part of a farmer cooperative's back-haul, he would know little else without checking the cooperative's records. The shipper likewise will find it very difficult, if not impossible, to check whether the farmer cooperative itself is bona fide and to determine if his traffic falls within the broad 50/50, member/nonmember test governing such a cooperative's overall business.

The danger is that as more shippers decide to use farmer cooperatives to benefit from low, negotiated rates, their competitors will soon be forced to do likewise.

UNITED AGRICULTURAL TRANSPORTATION ASSOCIATION OF AMERICA,
MARKETING CO-OP,
Lynwood, Calif.

Attention: Traffic Manager.

AT LAST A BREAKTHROUGH ON HIGH FREIGHT RATES! ! !

DEAR SIR: "Supreme Court sanctions co-op backhauls". The Ninth Circuit Court of Appeals in the Northwest Co-op v. ICC case. The decision of that court was that co-ops could back-haul regulated goods if it was necessary to their operation. This means that if a co-op has a rig in Chicago and it can't get an exempt load right away, it can pick up anything and return home rather than return empty. . . . And, the co-op can do it without ICC authority of any kind. The only limitation is that more than half of the co-ops' business must be in farm-related goods.

The above is now the law of the United States! Co-ops can do exactly as we have stated. The Supreme Court turned thumbs down on the ICC and the Justice Department who had wanted the Court to rule in their favor. AND, the SUPREME COURT made its one sentence decision in a record three days!

We are allowed to haul 49% of our total freight for non-members which we need to get our trucks back from the east, as we haul from the West Coast to the East Coast for our members. Our members are all farmers and ranchers.

We have ample insurance for your protection. All of our equipment are late model trucks and our Vans are 40′ in volume. As per the "Bill" quoted above

we can haul any type of freight coming back from the East Coast, and set our tariffs.

We are most anxious to be of service to you. I have personally been in and also associated with, the freight business for the past 20 years, both in produce and dry freight. Please feel free to call our office or drop us a line for any kind of additional information on rates, etc.

Cordially yours,

HOWARD MECOM,
General Manager.

The door will thus get wider and wider for entry into the general for-hire transport field.

Another good example of general freight solicitation on the part of farmer cooperatives is the successful effort by several of them to obtain military traffic on the basis of undercutting the rates of regulated carriers. Despite strong objections by TAA and railroad, trucking, and freight forwarder groups, the Department of Defense issued a directive, effective December 1, 1966, authorizing the use of exempt farmer cooperatives when they could perform services at rates lower than those of regulated carriers. Thus, another step was taken to encourage farmer cooperatives to actively seek nonfarm-related traffic from nonmembers.

TAA EFFORTS TO RESOLVE ISSUE

During hearings before Congress in July, 1966, on related legislation, it was quite apparent that the directly affected interests were in very sharp disagreement over what statutory changes are necessary to resolve the agricultural co-op problem. Since that time, considerable effort has been exerted within the TAA policy formulating structure to develop policy positions on this issue that all groups could either support or not oppose. These discussions included representatives of farmer cooperative interests.

These efforts helped narrow the differences considerably and resulted in agreement on a number of proposed statutory changes that, in substance, are incorporated in S. 752, as passed by the Senate. As pointed out in the Report of the Senate Commerce Committee, all major groups directly affected by this legislation—including regulatory agencies, carrier trade associations, and farm organizations—have expressed their acceptance of this compromise bill.

We cite this brief background information to stress the point that the provisions in this bill before your Subcommittee have been given very careful study and consideration by all direct interest.

TAA VIEWS ON S. 752

Following is a brief summary of our interpretation of the key changes that S. 752 would make and why we believe they are desirable:

Impose, as the primary limitation on a co-op's hauling of nonfarm traffic, a test that it be incidental and necessary to the co-op's motor transport of farm traffic for its members.

This is the basic test that has been generally applied by the courts to motor transportation performed by agricultural cooperatives. The incorporation of this test into Section 203 (b) (5) of the Interstate Commerce Act through specific legislative language should, we believe, help stress to the courts that Congress intends that any nonfarm traffic hauled by a co-op should have a direct relationship to the co-op's motor transport of farm traffic for its members. If such a relationship does not exist, the transportation would be unlawful regardless of its scope.

This limitation is important because it should prevent outright the for-hire transport by questionable co-ops of commodities normally moved via regulated carriage. It should prevent such practices as back-to-back hauls of nonfarm traffic and of for-hire hauls of commodities to points well beyond the normal operations of a co-op.

Apply a maximum limitation on a co-op's hauling of nonfarm traffic of 15 percent of its total interstate motor transportation service in any fiscal year on a tonnage basis.

This limitation would supplement the basic "incidental and necessary" test. In other words, it represents the maximum amount of nonfarm traffic that a co-op may handle, regardless of its relationship to the co-op's motor transport of farm traffic for its members.

We believe this limitation is a reasonable one and in line with current practices of the Internal Revenue Service in determining the scope of nonmember business a co-op can conduct without losing its tax-exempt status. It should give bona fide co-ops ample flexibility to augment their primary motor transport service for members, yet should prevent them from engaging in any excessive amount of for-hire transport of nonfarm traffic to the detriment of regulated carriers.

Require co-ops hauling nonfarm traffic to notify the ICC of their intent to do so, and to open their books to ICC inspections.

This is a very important provision, since it would permit, for the first time, the ICC to get the true facts about the scope and nature of nonfarm traffic hauled by farmer co-ops. It should also discourage questionable operators from using the co-op exemption as to subterfuge to enter the general for-hire transport field, since they should find it difficult to prove their eligibility..

Classify U.S. traffic hauled by a co-op as nonmember traffic

This change would replace the present blanket exclusion of U.S. traffic from any member vs. nonmember limitations on a co-op's business. In other words, a co-op at present can haul traffic for the Government without any statutory limitation—and do it free of regulation even though in direct competition with regulated carriers. While court action is pending to prevent abuse of this type of exempt co-op transport, passage of this provision of S. 752 should help resolve this particular issue.

We believe the U.S. Government should be treated like any other shipper when it comes to purchasing transportation services. It should not be able to use the co-op exemption as a means of cutting rates of publicly regulated carriers. While passage of this provision may not stop the use of co-ops by Government agencies for hauling military traffic, it should prevent abuse of this privilege and possibly stop the present practice of the DOD in openly soliciting their services.

CONCLUSION

We have attempted to show the general concern throughout the transportation community about the loopholes in the present agricultural cooperative exemption that are encouraging ineligible cooperatives to use the exemption as a guise through which they can engage in general for-hire transportation. We have also pointed out that the ruling by an appellate court in the Northwest Case, allowed to remain in effect by the U.S. Supreme Court, has opened the door even wider by encouraging bona fide cooperatives to engage in general for-hire transport.

While the actual scope of such for-hire transport operations is unknown at this time, the trend is clearly upward. The longer the trend continues in this direction, the greater the harm to regulated public carriers. Therefore, remedial legislative action is needed as soon as possible.

Passage of S. 752 should help resolve this national transportation policy problem area before it becomes too serious. It should clarify Congressional intent concerning the use of the agricultural cooperative exemption and thus make it possible for the ICC to take more effective enforcement action against persons who misuse it. Carriers should benefit, since specific limitations would be placed on the scope and nature of traffic hauled by co-ops, thus preventing entry into the general for-hire transport field. Bona fide co-ops should benefit, since this legislation should help eliminate operators that use the co-op exemption as a subterfuge to avoid regulation, as well as eliminate the need for continued legal action because of differences over the use of the exemption as now worded.

For these reasons, TAA strongly favors passage of S. 752 in its present form and urges favorable action on it by your Subcommittee at the earliest possible date.

Mr. FRIEDEL. I want to thank you for your cooperation, Mr. Hammond.

Are there any questions, Mr. Pickle?

Mr. PICKLE. Mr. Hammond, when the Northwest case was decided, did you find that some of your members were doing business with these cooperatives?

Mr. HAMMOND. Yes, some of them were. Of course, after the decision, there were many more that were approached to do business with the co-ops. Several of those examples are set forth in my statement here

where you will find there was open advertising and solicitation for business from users.

Mr. PICKLE. If these cooperatives are not subject to the Interstate Commerce Commission regulations, they would not be subject to the establishment of a public rate, then the ability of the shipper to transport his goods at a cheaper cost would be greatly enhanced. How much would they save on their rate?

Mr. HAMMOND. Well, it can be negotiated. This would be no set amount because they don't have to adhere to the regulation by the Interstate Commerce Commission. In that case, it would be entirely up to the shipper and to the co-op to set a rate that would be suitable.

What that does in time, of course, it breaks down your whole regulated transportation system.

Mr. PICKLE. Then your position is that it would be a temptation for some of your members to deal with these kinds of agricultural cooperatives?

Mr. HAMMOND. Surely.

Mr. PICKLE. In the best interest of the overall well-regulated transportation industry, it is best to place limitation on the hauling of these commodities?

Mr. HAMMOND. That is correct.

Mr. PICKLE. Thank you.

Mr. FRIEDEL. Mr. Devine.

Mr. DEVINE. No questions.

Mr. FRIEDEL. Mr. Watson.

Mr. WATSON. No questions.

Mr. FRIEDEL. Thank you very much.

Mr. HAMMOND. Thank you.

Mr. FRIEDEL. Our next witness is Mr. James Harmanson, general counsel of the National Council of Farm Cooperatives.

STATEMENT OF L. JAMES HARMANSON, GENERAL COUNSEL, NATIONAL COUNCIL OF FARM COOPERATIVES

Mr. HARMANSON. Mr. Chairman and members of the subcommittee: My name is L. James Harmanson, Jr., general counsel of the National Council of Farmer Cooperatives, on whose behalf this statement is presented.

I want to say that I think I can contribute to the "happy marriage" that Congressman Watson just referred to but not quite as briefly as the two or three preceding witnesses. I will try to be very brief.

I do feel that your subcommittee is as interested in what this bill contains and will do as you are in who is for it and do not want to base your decision entirely on who is for it and who is against it, and that is the reason that I shall try to come directly to the point in which I feel your subcommittee is interested.

The council is a nationwide organization of farmers' cooperative business associations engaged in the primary business operations of marketing farm products, furnishing farm supplies and providing farm business services for their farmer members and other farmer patrons.

The basis for qualification for membership in the council is the same as the basis for qualification under the exemption in section

203(b)(5)—see appendix I—of the Interstate Commerce Act; namely, "cooperative associations" as defined in the Agricultural Marketing Act of 1929, as amended—see appendix II—or "Federations of such cooperative associations."

Hence, the past and present interest of the council in preserving the long-recognized scope of this exemption and definition against the efforts to so restrict it by interpretation or legislation as to render it of no practical value to cooperating farmers is direct and clear.

Four hundred and eighty pages of printed record cover the public hearings for 5 days in 1966 and 1967 on S. 752, the companion measure to H.R. 6530, and its predecessor in the last session of Congress, S. 1729, before the Senate Surface Transportation Subcommittee of the Senate Commerce Committee.

I shall try to be helpful to your subcommittee this morning by dealing directly with basic points on which we believe information will be helpful to you in reaching prompt decision.

We shall state briefly the council's position, summarize the pertinent background to this legislation and outline why we believe prompt action now by your subcommittee is justified and will truly serve the public and no special interests.

Council position

The council opposed in the Senate and is still opposed to S. 752, the companion bill to H.R. 6530, as originally introduced on the recommendation of the Interstate Commerce Commission. The council had a major part in cooperation with other farm organizations and the Department of Agriculture in suggesting most of the changes in S. 752 which were approved by the Senate Commerce Committee and adopted by the Senate.

The council, therefore, supports S. 752 as passed by the Senate on June 4, 1968, and recommends favorable action on that version by your subcommittee and the House Interstate and Foreign Commerce Committee on the end that such bill might be enacted into law before adjournment of this session of the Congress.

Mr. WATSON. May I interrupt the gentleman at this point?

You are in favor of S. 752?

Mr. HARMANSON. As passed by the Senate on June 4, 1968.

Mr. WATSON. Your first statement there says "The Council opposed in the Senate and is still opposed to S. 752."

Mr. HARMANSON. You read on "as"—maybe the comma is in the wrong place, but "as originally introduced on the recommendation of the Interstate Commerce Commission."

Mr. WATSON. But you are in favor of it as passed by the Senate?

Mr. HARMANSON. Yes. The council opposed in the Senate and is still opposed to S. 752 as originally introduced. But we are in favor of it as it passed the Senate.

Mr. WATSON. I understand now.

Mr. HARMANSON. To continue with my statement.

Background

When the Motor Carrier Act was passed in 1935 and became Part II of the Interstate Commerce Act, there were two exemptions of particular importance to farmer cooperatives and agriculture generally which were written into that act.

One, referred to as the "agricultural commodities exemption," now section 203(b)(6) of the act, exempts from economic regulation by the Commission "motor vehicles used in carrying property consisting of ordinary livestock, fish—including shellfish—or agricultural—including horticultural—commodities—not including manufactured products thereof."

The other exemption, referred to as the "cooperative association motor vehicle" exemption, now section 203(b)(5) of the act and the subject of the bills before your subcommittee today, exempts from economic regulation "motor vehicles controlled and operated by a cooperative association as defined in the Agricultural Marketing Act, approved June 15, 1929, as amended, or by a federation of such cooperative associations."

Just two requirements, the motor vehicles have to be owned and controlled by the cooperative association and the cooperative association must meet the requirements of the Agricultural Marketing Act, which is the same definition to qualify for loans from the banks for cooperatives under the farm credit system.

The Interstate Commerce Commission in 1935 unsuccessfully opposed the inclusion of these exemptions in the Motor Carrier act and through the years has sought to give a very narrow and strict interpretation to their scope.

It should be made clear that the railroad industry and the regulated motor carriers all through the years have been very vigorous supporters of that position, restrictive interpretations of these exemptions by the Intestate Commerce Commission.

In the 1940's and 1950's, there was much costly litigation in the courts and in administrative proceedings before the Commission as to when an agricultural commodity loses its character as such and becomes a manufactured product.

Three glaring examples. The Commission took the position that nuts in the shell were an agricultural commodity but after you shell them, they become a manufactured product and no longer are an agricultural commodity. We had the same situation with respect to redried tobacco. It was held by the Commission that the redrying of tobacco changed it from being an agricultural commodity.

There was a big controversy over poultry. If you cut the head and legs off poultry and defeather it, it is no longer a product of agriculture; it becomes a manufactured product. So held the Commission. There was a lot of costly litigation and proceedings before the Commission all through the 1940's and 1950's to try to get that straightened out.

Finally, Congress took action in the Transportation Act of 1958 and clarified this exemption to prescribe with particularity named commodities which would be considered exempt and those which would be regarded as nonexempt under section 203(b)(6). Since that time, there has been little difficulty in administering and complying with this exemption.

In the late 1950's and early 1960's, the Commission turned its attention to the cooperative association motor vehicle exemption and sought to limit the transportation by qualified cooperatives to "farm products, farm supplies, or other farm related traffic." The Commission, however, has been deterred in that effort by the decision of the Ninth Circuit Court of Appeals in 1965 in the Northwest case (*Northwest Agricul-*

tural Cooperative Association, Inc. v. *Interstate Commerce Commission*, 350 F. 2d (Ninth Circuit 1965), certiorari denied, 382 U.S. 1011, Jan. 25, 1966), in which the Council participated as amicus curiae.

In that case, the court held in effect that a cooperative qualified under the Agricultural Marketing Act could lawfully engage without operating authority in the transportation of nonfarm related property for nonmembers to the extent that such transportation is incidental to its primary transportation operations and necessary for its effective performance.

One question of other witnesses that seems to concern some members of the subcommittee is how are you going to determine what is incidental and what is necessary. Would that not open up a field for a lot lawsuits? I think it is true that there is hardly any law passed by Congress that is not subject to lawsuits. But the Ninth Circuit Court of Appeals in this Northwest decision did lay down a guideline as to what is meant by incidental and necessary. I am reading from the decision of the court, the Ninth Circuit Court of Appeals.

The court said that:

> Such transportation is incidental to the cooperative's agricultural activity when limited to use of otherwise empty trucks returning from hauling member farm products to market and producing a small return in proportion to the cooperatives' income in trucking farm products and farm supplies.

We recognize, Mr. Watson, that does not have the particularity that we would like for administration by an administrative agency. I would hope that the Interstate Commerce Commission would not be too restrictive in these interim guidelines that Mrs. Brown referred to this morning, but I would say that there is some guideline contrary to what some of these so-called trucking cooperatives have advertised in the papers—that they can haul anything anywhere. That has hurt the bona fide cooperatives of the country.

If you will look at the law as laid down by the interpretation of the Ninth Circuit Court of Appeals you will see that the court has given some guidelines as to what is incidental and necessary.

Mr. PICKLE. You have read, apparently, the language from the Ninth Circuit Court of Appeals relating to guidelines. Is what you read contained in your testimony?

Mr. HARMANSON. I departed from the testimony because I felt this would be a pertinent place to bring that out for the subcommittee.

In like manner, the court stated that transportation of non-farm-related products is "necessary":

> When it is not economically feasible to operate the trucks empty on return trips, and where the additional income obtained is no more than that required to render performance of the cooperatives' primary farm transportation service financially practicable.

Now, returning to the statement. This interpretation of "incidental and necessary," as has been indicated, is not a new interpretation, but we feel, and the crux of our testimony before the Senate subcommittee was, that this was the interpretation intended by the Congress from the time that this amendment was introduced by Congressman Jones, then chairman of the House Agriculture Committee, when the Motor Carrier Act was passed in 1935 and it is consistent with the interpretation that has been given by the Farm Credit Administration in their regulations in administering this definition for qualification for loans to cooperatives through the banks for cooperatives.

It is also significant that this interpretation also is consistent with the Administrative Ruling No. 91 issued by the Commission's own Bureau of Motor Carriers in 1940 which stated in part that the business of a cooperative for purposes of this exemption under the Marketing Act must be primarily, and I emphasize "primarily", that of farmers acting together and marketing farm products and/or furnishing farm supplies and farm business services.

The Commission's own Bureau recognized as early as 1940 that the operation of the cooperative did not have to be exclusively that of marketing farm products and furnishing farm supplies and farm business services.

During the past 5 years while the controversy over the interpretation of this exemption has been going on in proceedings before the Commission and in the courts, recommendations for legislative action to narrow this exemption have been submitted by the Commission to the Congress. Exhaustive hearings were held in the Senate in 1966 and 1967 and many avenues for action have been explored and considered. The final product to date is S. 752 as passed by the Senate on June 4. Its major provisions, substantially incorporating non-self-serving recommendations originally made by the council in cooperation with other national farm organizations and the U.S. Department of Agriculture, may be summarized thus:

1. A qualified cooperative or federation would be limited in its interstate transportation for compensation for nonmembers, who are neither farmers, cooperative associations nor federations, except transportation otherwise exempt—and that means that which is exempt under 203(b)(6); railroad trucks, common carrier trucks, private trucks—anybody can haul those named commodities—so that which is incidental to its primary transportation operations and necessary to its effective performance and before engaging in such transportation for nonmembers the cooperative would be required to give notice to the Commission of its intent to engage in such transportation.

2. Transportation for or on behalf of the United States or any agency or instrumentality thereof would be considered as nonmember business.

None of the testimony this morning that I have heard has explained to you the reason for that. It is simply this: The Agricultural Marketing Act of 1929, as amended, which is the basis for this exemption in section 203(b)(5), contains a provision that business done with the United States or any instrumentality thereof shall not be considered in determining whether the total business done by the cooperative with its nonmembers exceeds that done with its members.

The reason that was written into the act was that in the 1930's, I think, perhaps 1935, when most of the marketing cooperatives of the country were handling products under the support programs, with which you are familiar, and many marketing cooperatives handling products such as cotton and grain, most of their business was not marketing the products for members but it was storing them for the U.S. Government under the loan program.

Therefore, it meant that if you had this storage business done for the United States, counted as nonmember business, many of the marketing cooperatives would not have been able to qualify for loans from the banks for cooperatives. This was put in by the Congress for a specific

reason and not related to this transportation problem which has developed.

We think it is only fair and we have attempted to support a clear statutory declaration that this business done for the U.S. Government in the hauling field should be counted as nonmember business.

3. The nonmember interstate transportation in any fiscal year measured in terms of tonnage of a cooperative or federation of cooperatives required to give notice to the Commission could not exceed the total quantity of property transported interstate for itself and its members.

4. The Commission would be given specific authority to examine the pertinent motor transportation records of any cooperative or federation required to give notice to the Commission under the bill for purposes of determining whether the cooperative or federation is in compliance with the requirements of this exemption.

A further provision of the Senate passed version of S. 752 would impose a 15-percent maximum limit on the necessary and incidental interstate hauling of other than "exempt commodities" for nonmembers who are neither farmers, cooperative associations, nor federations of cooperative associations.

The council did not originally propose nor support this or any other maximum limitation. The council felt that an arbitrary maximum limitation was not necessary with the other new requirements and that it would unduly hamper the economical and efficient marketing of their members' products by many cooperatives which did not have common carrier service available at reasonable rates if available at all.

But after the Senate Surface Transportation Subcommittee proposed a 10-percent maximum limitation on all interstate hauling for compensation for nonmembers, excepting exempt commodities, the council joined with the U.S. Department of Agriculture and the general farm organizations in proposing as a substitute a maximum 15-percent limitation on interstate hauling for nonmembers who are neither farmers, cooperative associations, nor federations of cooperatives. This counterproposal was adopted by the Senate Commerce Committee and is in the bill as now referred to you from the Senate.

We know there is some opposition to this proposed limitation on the part of some cooperatives and perhaps by some operators who are seeking to utilize this exemption to make money for themselves rather than for farmers.

But with very few exceptions, the council's members have advised us that they can live under this maximum limitation and will do so in order to get this controversy settled by Congress so that they can proceed with more certainty in providing for the transportation needs of their farmer members.

WHY ACT NOW

If this session adjourns without final action by the Congress, the result will be more costly and unproductive litigation, further frustration and uncertainty in the administration of this exemption by the Commission, and encouragement to those unqualified operators who might seek to operate under this exemption to the detriment of the genuine farmer-owned and farmer-controlled cooperatives in the country.

We are convinced that no legislation can be devised which will satisfy all in the regulated transportation industry or in agriculture.

But we are firmly convinced through years of close association with this controversy that the almost unprecedented support or acceptance of the Senate-passed version by the three general farm organizations, the U.S. Department of Agriculture and leading organizations in the railroad and regulated motor carrier industries commends it to you for prompt and favorable action.

We thank you for the opportunity to present the position and recommendations of the Council for action on this important matter.

(The appendices referred to follow:)

APPENDIX I

INTERSTATE COMERCE ACT, PART II SECTION 203(b)(5)

Section 203(b): "Nothing in this part, except the provisions of section 203 relative to qualifications and maximum hours of service of employees and safety of operation or standards of equipment shall be construed to include . . . (5) motor vehicles controlled and operated by a cooperative association as defined in the Agricultural Marketing Act, approved June 15, 1929, as amended, or by a federation of such cooperative associations, if such federation possesses no greater powers or purposes than cooperative associations so defined;"

APPENDIX II

SECTION 15(a) OF THE AGRICULTURAL MARKETING ACT—APPROVED JUNE 15, 1929, AS AMENDED (49 STAT. 317, 12 U.S.C.A. 1141j(a))

As used in this act, the term "cooperative association" means any association in which farmers act together in processing, preparing for market, handling, and/or marketing the farm products of persons so engaged, and also means any association in which farmers act together in purchasing, testing, grading, processing, distributing, and/or furnishing farm supplies and/or farm business services: *Provided, however,* That such associations are operated for the mutual benefit of the members thereof as such producers or purchasers and conform to one or both of the following requirements:

First. That no member of the association is allowed more than one vote because of the amount of stock or membership capital he may own therein; and

Second. That the association does not pay dividends on stock or membership capital in excess of 8 per centum per annum.

And in any case to the following:

Third. That the association shall not deal in farm products, farm supplies, and farm business services with or for nonmembers in an amount greater in value than the total amount of such business transacted by it with or for members. All business transacted by any cooperative association for or on behalf of the United States or any agency or instrumentality thereof shall be disregarded in determining the volume of member and nonmember business transacted by such association.

Mr. HARMANSON. Mr. Chairman, if I might add just a word, Mr. Newsom, Master of the National Grange, was unable to be here in person today. He has asked me to present at this time a letter for the record in which the Grange gives unconditional support for S. 752 as passed by the Senate.

Mr. FRIEDEL. It may be placed in the record.

(The document referred to follows:)

NATIONAL GRANGE,
Washington, D.C., June 28, 1968.

Re S. 752 and H.R. 6530.

Hon. SAMUEL N. FRIEDEL,
Chairman, Subcommittee on Transportation and Aeronautics, Committee on Interstate and Foreign Commerce, House of Representatives, Washington, D.C.

DEAR CONGRESSMAN FRIEDEL: The National Grange supports S. 752 as passed by the Senate on June 4, 1968 and respectfully recommends its early approval by

your Subcommittee so that action can be completed in this Session of the Congress.

The Grange has participated with the other general farm organizations and the National Council of Farmer Cooperatives during the past several years in trying to develop reasonable and fair clarification and amendment of the cooperative association exemption in the Motor Carrier Act to preserve for bona fide cooperatives the economic and efficient marketing of their members products intended by this exemption.

The Bill, as finally passed by the Senate on June 4, 1968, represents a constructive action to preserve the basic scope of this exemption and at the same time establish specific guidelines which should be very helpful in preventing abuses by those not qualified under the exemption.

The Grange was active in 1935 in supporting the inclusion of this exemption in the Motor Carrier Act to preserve for farmers, working together in their cooperatives, this needed economy and efficiency in marketing their products. With the mounting increases in rail and common motor carrier freight rates, this exemption is increasingly important to agriculture.

Since I cannot be present to personally testify at the Hearings on this legislation, I shall appreciate your including in the record this statement of the Grange's unqualified support of S. 752 as passed by the Senate.

Respectfully yours,

HERSCHEL D. NEWSOM, *Master.*

Mr. FRIEDEL. Are there any questions, Mr. Watson?

Mr. WATSON. Thank you very much.

I think you have made a good contribution. Thank you very much.

Mr. FRIEDEL. Our next witness is Mr. Matt Triggs, American Farm Bureau Federation.

STATEMENT OF MATT TRIGGS, ASSISTANT LEGISLATIVE DIRECTOR, AMERICAN FARM BUREAU FEDERATION

Mr. TRIGGS. Good morning, Mr. Chairman, and Mr. Watson.

The American Farm Bureau Federation respectfully recommends the enactment of S. 752, as approved by the Senate.

S. 752 amends section 203(b) (5) of the Motor Carrier Act by establishing limitations on the transportation services that may be provided by agricultural cooperatives.

A major purpose of the bill is to prevent the development of nonregulated for-hire transportation by non-bona fide cooperative using the cooperative form of organization to legitimize such operations.

S. 752, as approved by the Senate, contains more restrictive limitations on cooperatives than we had favored in our testimony to the Senate Committee on Commerce.

Nevertheless, it is our opinion that the bill, as amended, represents a carefully considered and a reasonable compromise of the views presented to the Senate committee by the contending parties.

Its enactment will be a benefit to all by a statutory settlement of a controversy that has occupied the attention of the parties and the courts for many years, without having necessarily been finally resolved.

We respectfully urge the committee to approve, without amendment, S. 752 in the revised form approved by the Senate.

We appreciate the opportunity to present the views of the American Farm Bureau Federation on this matter.

Mr. FRIEDEL. Thank you very much, Mr. Triggs.

Are there any questions, Mr. Watson?

Mr. WATSON. No, Mr. Chairman; other than to thank him.

As usual, the Farm Bureau comes up with a reasonably well thought out and, I think, very sound position.

Mr. TRIGGS. Thank you.

Mr. FRIEDEL. Our next witness is Mr. Angus McDonald, National Farmers Union.

STATEMENT OF ANGUS McDONALD, DIRECTOR OF RESEARCH, NATIONAL FARMERS UNION

Mr. McDONALD. Mr. Chairman and members of the committee: I am research director of the National Farmers Union.

I would like to have this brief statement incorporated in the record. Although it is very brief, I will be even more brief in my summary.

I would like to indicate first our complete support of S. 752 as passed by the Senate.

I also would like to comment on the fact that Mr. Harmanson referred to a number of groups who, ordinarily are not on the same side of the table, are in support of the bill.

It is not unusual, however, for the Farmers Union and the National Grange and Farm Bureau to support legislation together particularly in regard to transportation. We have over the years supported the agricultural exemption. We feel it is necessary for efficient transportation of farm commodities necessary to the livelihood of members of farm cooperatives.

We feel that this bill, while it was not sponsored particularly by our group but our agreement was reached after lengthy consultation with other individuals representing farm organizations, particularly Mr. James Harmanson, whom you have just heard, we agreed that it would be a step in the right direction, that it would possibly avoid lengthy and costly litigation.

Mr. Chairman, that concludes my statement.

(Mr. McDonald's prepared statement follows:)

STATEMENT OF ANGUS McDONALD, DIRECTOR OF RESEARCH, NATIONAL FARMERS UNION

Mr. Chairman and members of the committee, I appear here in support of S. 752 which would, we hope, resolve some of the controversies which have arisen regarding the administration of the agricultural exemption as set forth in the Interstate Commerce Act.

The National Farmers Union, over a long period of years, has supported this exemption which is vitally necessary to the efficient marketing of farm products. We have also opposed various attempts which have been made both by Government officials and certain organizations to weaken the exemption.

We feel that the problem of the transportation of farm commodities is unique. Congress was wise when it passed the Interstate Commerce Act in exempting farm commodities from regulation. Certain commodities are of a highly perishable nature and rigid rules in regard to both transportation rates and routes would greatly hamper efficient transportation.

The agricultural exemption also provides protection for consumers and enables them to purchase high quality food which has been transported to the market in the shortest possible time. Certain agricultural products are not only very perishable but are of such a seasonable nature that transportation facilities may be strained to the utmost at a particular time. This involves relying on all kinds of transportation—both regulated and non-regulated—to bring food products to the point of distribution without spoilage and waste.

We have been very much aware of certain problems which have arisen in regard to the non-member portion of products which are transported by cooperatives in interstate commerce. It is perhaps unnecessary to tell this committee that there is a wide divergence of opinion pertaining to the administration of the agricultural exemption provisions of the ICC Act, both among Government

officials and farm organizations whose members are primarily interested in the production and transportation of agricultural products. We are particularly gratified that over a long period of years there has been, so far as we know, no substantial difference of opinion among farm groups regarding the agricultural exemption. This unanimity of opinion is also evidenced in the support of the bill now before this Committee.

We urge that S. 752 be approved as expeditiously as possible. It is particularly important that action be taken since the other body has already approved a companion bill. We feel that the compromise which has been developed to a large extent by Mr. Harmonson of the National Council of Farmer Cooperatives, represents a step forward in the administration of the agricultural exemption. Passage of the bill will possibly make unnecessary costly and time consuming litigation.

Mr. FRIEDEL. Thank you.

Are there questions?

Now we will hear from the opposition, and I would like to make an oral statement.

We would like to hear one statement and ask the rest to file their statements in the record. But we are going to finish this meeting today.

The first witness is Mr. Olson.

Mr. OLSON. Sir, I think we have all come a long way. It is very important to our portion of the industry that we each be heard.

Mr. FRIEDEL. Mr. O. A. Olson, manager of the All Star Dairy, Lawrence, Kans.

STATEMENT OF O. A. OLSON, GENERAL MANAGER, MILK PRODUCERS MARKETING CO., LAWRENCE, KANS.

Mr. OLSON. Mr. Chairman and gentlemen of the committee, my name is O. A. Olson. I am general manager of Milk Producers Marketing Co., a cooperative corporation with home offices and plant located at Lawrence, Kans., and I am appearing on behalf of that company in opposition to S. 752.

I have with me today on my right Mr. Jenkins, our division manager. On my left, our attorneys, Mr. Bingham and Mr. Sapp, both of Kansas City.

Milk Producers was organized in 1932 under the Agricultural Marketing Act and has been in continuous operation ever since; in each year of operation it has been certified by the U.S. Department of Agriculture as a qualified cooperative association under section 1141j of title 12 of the United States Code, including 1968.

Our company's opposition to the bill is based upon our entry into the transportation field in 1965, as an economic necessity for our survival. We institute these operations only after careful scrutiny and upon the studied advice of counsel.

A brief background on our company may be somewhat helpful to the committee in understanding why we are forced into the activities, and why we feel it is necessary to oppose this legislation.

Milk Producers was organized to provide the dairy farmer in Kansas and Missouri with a production and marketing outlet for their products. Its only stockholders are member-patrons who are actively engaged in the production of milk, or who have in the past been so engaged.

Retired or other farm members not actively engaged in milk production are permitted to retain their stock and receive dividends, but

are not allowed to vote at stockholders' meetings. Active producers are permitted one vote at such meetings regardless of the number of shares they hold. Thus, we comply with all essential requirements of the Agricultural Marketing Act, and have been in such compliance since the company's inception.

Our membership has, during the past 10 years, dropped from a high of 3,000 producers in 1958, to 174 as of June 24, 1968.

Our company processes these products, packages them, and sells them principally in the Kansas City area in competition with such large national dairy corporations as the National Dairy Corp., Hawthorn Mellody Dairy Farms Dairy Co., Foremost Dairies, Inc., the Borden Co., and Fairmont Foods.

National Dairy, Borden, and Fairmont are ranked 31, 42, and 353, respectively, in Fortune's list of the 500 largest industrial corporations, with combined gross sales of over $4 billion for the year 1967. (Fortune, June 15, 1968 issue, p. 186, et seq.)

These companies are primarily responsive to the stockholders, not the farmer, and their principal goals are profits.

Milk Producers have the same goals, but our stockholders are all farmers; unlike these companies, we cannot undercut the dairy farmer by producing milk substitutes or "filled milk" products (in which butterfat is replaced with vegetable fat).

We have strong fears that, if present research by such companies as those I have mentioned is successful, milk and milk products will be crowded out of the market by synthetic production and vigorous selling of margarine. (See Forbes magazine, May 15, 1968, issue at p. 34.)

In view of the regulation of the dairy industry, we are unable to pay more to our producers than any other competitor, since prices are controlled and dictated by the Federal Milk Market Administrator of the U.S. Department of Agriculture.

The only ways in which the dairy farmer can increase the price he receives for his product is by increasing his own efficiency, which he can only do by mechanization and at great capital expense, and by selling to a dairy co-op, such as Milk Producers, with the hope that the co-op's operation will be sufficiently profiitable to permit dividend payments to him.

Our dairy operations have lost money in each of the last 6 years; this is the pattern across the country and, yes, even around the world, producers in increasing numbers are leaving dairy farming for other, more profitable areas of endeavor.

As a result of this, we have experienced a decline in public dairies in the State of Kansas from 99 in 1958 to the present 44, and from 72 in the Kansas City area in 1950 to 10 at the present time.

Mr. WATSON. Your statement about being marketed out of business by the large companies with the synthetic products and all of that, have you ever tried, and I appreciate your problem, have you ever tried to recapture some of the market by saying the only true milk is the original cow milk, not machine produced, something like that?

Mr. OLSON. We certainly do, Mr. Watson. We have an intensive program for consumer education in the field of dairy products acceptance to the human body, as a matter of fact, in competition with substitutes.

Mr. WATSON. The cows are the only ones that give milk. The machine can at best produce something that is artificial.

Mr. OLSON. That is right.

Talking about the economic thing again, the substitutes are making the inroads generally because of the cost of production of milk as opposed to the cost of production of the substitute products.

Mr. WATSON. Thank you.

Mr. OLSON. Business in the United States has found it increasingly necessary to free itself from reliance on one product or service: diversification has become the only safe way to profits. The reasons for this are evident—if a company's principal product or service is faltering, another more profitable operation can take up the slack, and permit the continuation of the principal enterprise.

Milk Producers has quite simply found it essential to do precisely this in order to avoid economic extenction. At the present time, we are negotiating for the purchase of a frozen food operation in addition to our transportation division. We have been unable to pay any patronage dividends for the past 6 years, because we have had no earnings from milk production; nor, were we able to pay any stock dividends during the past year because of current losses.

Our principal business of milk production generated gross sales of approximately $5.9 million of gross sales in 1967; by contrast, our transportation division had gross sales of only $1,675,000, or about 28.3 percent of total gross revenues.

Thus, we remain substantially below the 49-percent ceiling established by the Agricultural Marketing Act for nonmember business.

Our principal transportation customers are also major buyers of our milk products. This, in effect, is the reason for our being in the transportation business. In this way, we are able to provide to our customers a double-barreled sales program—milk products and transportation services. Such customers are national wholesale grocery chains, and can readily make use of both our products and services. If the transportation services were not available, we would face the possible loss of milk customers.

I wish to emphasis two important facts relative to our transportation activities: (1) we serve anyone desiring our facilities without rebates or discrimination; and (2) our truck rates are about evenly balanced between being higher and lower than those of regulated carriers.

Our transportation business has been built upon our willingness and ability to provide the service our customers require rather than any attempt to undercut the rate structure of regulated carriers.

We feel the committee should also be aware of the fact that, insofar as we are able to determine, not one of the other co-ops the Interstate Commerce Commission has challenged in the courts is a bona fide "cooperative association" as that term is defined by the Agricultural Marketing Act. We are aware of only two other bona fide co-ops in the United States presently engaging in the for-hire transportation business: these are the Cache Valley Dairy Association located in Utah, and the Northwest Agricultural Cooperative Association, operating out of the State of Oregon.

I would also point out to the committee that there has been no authoritative findings reported by any group or agency of which we are

aware to determine the qualifications of the so-called co-ops purporting to operate under the exemption of section 203(b)(5) of the Interstate Commerce Act (49 U.S.C. 303(b)(5)).

In fact, of the cases presently pending against co-ops for illegal transportation activities, the companies involved are apparently uniformally not qualified. They are, in fact, wildcat truckers seeking to avoid the requirements of the Interstate Commerce Act by posing as farmers' groups.

Milk Producers is vigorously opposed to the operations of these pseudo-co-ops. They have given our industry a black eye, and specifically have caused milk producers to be unjustly included in a group which is now being condemned for violations of the Interstate Commerce Act.

If we are correct in our belief that our operations are well within the scope of the qualifications contained in section 203(b)(5) of the Agricultural Marketing Act, and that the renegade groups calling themselves cooperatives are not, this legislation is not necessary: The administrative findings of the Department of Agriculture and the Interstate Commerce Commission would form a sufficient basis upon which to terminate the activities of the illegal operators.

Under such circumstances, the legitimate cooperatives engaged in transportation will be forced to limit themselves to a maximum of 49 percent of their gross revenues for nonmembers. In other words, there is an absolute ceiling upon the size of any true cooperative's nonmember transportation—indeed, any other business—activity.

Should this bill be passed, milk producers will be forced either to close its transportation division, curtail its activities substantially, or seek regulated authority from the Interstate Commerce Commission.

Even if we were to become a regulated carrier tomorrow, we will still be subject to the same ceiling of 49 percent nonmember business, including transportation, as imposed by the Agricultural Marketing Act. And, it is well to note that should our revenues from member business decline, the maximum revenues which we may receive from nonmember sources will also decline.

I believe the committees will readily see that the true cooperative poses no substantial threat to the regulated transportation industry. The means of eliminating the illegal operators carrying on their activities under the guise of a cooperative is for greater coordination between the Department of Agriculture and the Commission's Bureau of Enforcement, and vigorous prosecution of the violators. This would free the legitimate co-op to pursue its transportation activities within the limits already imposed upon it, and remove the stigma created by the actions of the sham co-ops.

Milk Producers, I might point out, has no opposition to regulation by the Commission. However, I would also point out that we have committed our company to transportation as a matter of financial survival, and that passage of this bill would effectively destroy what may well be our company's salvation.

Substantial capital has been committed to our operations in an honest faith in their legality; these expenditures could not be fully recovered, and we would be forced to seek out and develop another source of revenue in order to survive. This would require great amounts of time and money not available to us, not to mention the money lost

in the interim. This is tantamount to taking our property without due process of law.

In view of these facts, we must oppose this legislation in its present form. S. 752 is extremely ambiguous: it is unclear whether the limits on nonmember traffic are to be 15 percent or 50 percent of total tonnages transported; at best, it is confusing.

Moreover, it does violence to the terms and philosophy of the Agricultural Marketing Act by carving out an area of possible co-op endeavor and limiting the co-op's activity in that area to 50-percent nonmember business, as opposed to the act's limitation of 50-percent ceiling on all nonmember business, in the aggregate. And these inroads are to be made at the behest of a strong, well-organized special interest group, the regulated carriers.

I would also point out that it seems inappropriate for the committee to take any decisive action on the matter until it has had a better opportunity to consider the full implications of the measure, the effect passage would have upon the bona fide cooperatives like milk producers, and whether or not passage would really serve to curtail illegal operations and promote the best interests of the regulated transportation industry.

I strongly question the wisdom of recommending passage unless there is greater opportunity for a more extensive study than exists in the present session of Congress.

I would like to conclude with some comments on possible amendments which the committee might wish to consider.

As I stated a moment ago, Milk Producers has no objection to regulation by the Commission; we have always attempted to cooperate with that agency to the greatest extent possible, have made all our books and records available to the Commission's representatives, and I seriously doubt that regulation would pose any great difficulties for us.

But in order to acquire authority to continue our present operations, we would be forced to stop them, at least temporarily, file our applications, and then wait until all the administrative hearings, appeals, and judicial action were completed. In the process, we would lose most of our customers and good will, and be unable to meet our commitments for equipment—in other words, lose all of the business we have managed to build over several years.

In imposing formal regulation or licensing upon any business of this type, Congress has almost uniformly permitted legitimate operators to continue their activities by merely proving their qualifications and operations, rather than the burden of establishing in extensive and often bitterly contested administrative cases the need for a new service.

I would therefore suggest that, if the committee deems passage advisable, it amend the bill to provide that existing cooperatives engaging in transportation activities be granted authority by the Commission encompassing those activities upon proof of the following:

(A) That they are, in fact, a bona fide "cooperative association" under the Agricultural Marketing Act, and recognized as such by the U.S. Department of Agriculture; and

(B) That they have been performing a transportation service at the effective date of the bill.

This is no more than was done for the motor carrier industry upon passage of the Motor Carrier Act in 1935; the requirement of proving the qualifications under paragraph (A) would serve to prevent the pseudo co-ops from obtaining any authority from their illegal operations.

Finally, I would also suggest, in view of the overall decline in revenues for cooperatives as closely connected with farming activities as milk producers (that is, not those which are principally involved in activities which are not farm related), that an amendment to section 1141j of title 12, U.S.C. (the Agricultural Marketing Act) be considered to the effect that all business conducted by a cooperative association under the regulation of the Interstate Commerce Commission (or similar agency) would be disregarded in determining the volume of member and nonmember business transacted by such association.

I wish to thank the committee for this opportunity to appear today and make our position known, and for your courteous attention.

Mr. FRIEDEL. Thank you, Mr. Olson, for a very informative statement.

I have no questions.

Mr. Watson?

Mr. WATSON. Mr. Chairman, I have two or three questions.

May I parenthetically state at this time I have an appointment I should have met at 12. The House is in session.

If these gentlemen want to be heard, certainly I want to give them an opportunity to be heard.

Could we possibly get permission to sit this afternoon and take a little while? I would like to ask him two or three questions. I want to give everybody an opportunity to be heard.

Mr. FRIEDEL. We will try to get permission to sit while the House is in session. If we get permission, we will come back at 2 o'clock.

Mr. WATSON. Would you like to dispose of this witness?

I will ask him two or three questions.

Mr. FRIEDEL. Yes.

Mr. WATSON. Mr. Olson, you at first made a rather strong indictment of all the cooperatives except three, yours and two others. You are not a member of this council that the gentleman represented a moment ago?

Mr. OLSON. No; we are not.

Mr. WATSON. Upon what basis do you make this blanket indictment? Briefly now.

Mr. OLSON. Under the qualifications branch as we are regulated by the U.S. Department of Agriculture, each year they determine by our activity our right to do for our members as the act provides. In other words, in our case of milk, we as a true cooperative under their surveillance are allowed to weigh, test, sample, and determine the rate of pay of the member producers that we represent. This is the qualification by which each year the qualification branch gives us this true status. This is what I base that on.

Mr. WATSON. In other words, you conclude simply because you are further regulated and inspected by the Department of Agriculture that that puts you in a unique position in contrast to those agricultural commodities and cooperatives that are not regulated, inspected, or have

these added burdens; they are not true cooperatives? Is that the basis of your position.

Mr. OLSON. We believe that the problem probably stems from the fact that many groups have banded together and call themselves a cooperative, operating under the cooperative principle very much the same as perhaps grocery stores or any other like businesses.

This is where we feel the distinction is between the two. The word "cooperative," in other words, must mean something. This is where I base this contention.

Of course, the cooperative could extend well beyond milk. It could include other agricultural commodities.

Mr. WATSON. You don't mean to imply that all of these other cooperatives are truckers? Certainly you have genuine bona fide farmer cooperatives.

Mr. OLSON. They are not agricultural. That is the difference.

Mr. FRIEDEL. Will the gentleman yield?

Mr. WATSON. Yes.

Mr. FRIEDEL. What do you haul on your backhaul?

Mr. OLSON. We are hauling general commodities of all types. This is for economic necessity actually. That is the purpose of this.

Mr. FRIEDEL. Isn't that what the other cooperatives do?

Mr. OLSON. Yes. We are trying to draw the distinction here without malice to anyone between the types of cooperatives, cooperatives in principle, cooperatives as regulated and planned by the Department. This is the difference between them.

Mr. WATSON. Since you are restricted to milk, help me to understand what commodities you would be in a position to haul on your backhaul.

Mr. OLSON. Our understanding, again, the qualification of the cooperative does not necessarily mean that it is relegated to strictly the product it is principally engaged in. This could be grain or a number of other—cotton, I suspect, is a large one in this field.

But the Department has the qualification branch for each area in which they incorporate the necessary requirements for being a true cooperative, to render the services back to their members as is defined in the act. Ours, peculiarly, is milk.

Mr. WATSON. Help me to understand how your equipment would be adaptable to any other commodities other than liquids. Certainly, milk would be highly restrictive insofar as placing any other liquid from a special container truck.

Mr. OLSON. We are not professing to be delivering liquid as liquid in tankers. What we are delivering is finished products as you would purchase in the home and store. Our transportation differential is involved in general commodities. This is our mode of operation.

Mr. WATSON. Mr. Olson, when you get into this processing business, then, you are in the same business as these larger dairies?

Mr. OLSON. That is right. We are farmer-owned, farmer-controlled, doing business in the finished product as a continuation of the farmer-produced milk.

Mr. WATSON. You get the milk from around the farms?

Mr. OLSON. Right.

Mr. WATSON. You bring it into your plants. Then you process it into all types of things: cheeses and everything else.

Mr. OLSON. No, sir; strictly fluid products.

Mr. WATSON. Then you have your trucks go out and distribute it in the various marketplaces?

Mr. OLSON. That is right.

Mr. WATSON. Would you not come into the general processing industry such as Borden's, some of the others you speak of?

Mr. OLSON. That is right. There is a tremendous difference in the size of the people involved here. That is why we mentioned that.

Mr. WATSON. Yes; I am sure of that. The difference in size would not, I think, warrant any distinction between your position and that of the other.

Actually, Mr. Olson, your worry is prospective rather than present, isn't it? You say you are well below the 49 percent ceiling established by the Agricultural Marketing Act. So, if you have any problems they would be prospective rather than present?

Mr. OLSON. If this bill is passed, very definitely they would restrict us to the 15 percent.

Mr. WATSON. You could continue operating as you are now, I assume. You would not declare under this act.

Mr. OLSON. In that it would destroy, of course, our division for transportation because of the small amount of volume of product we would have moving interstate. It would not be economically feasible to continue to operate the division.

Mr. WATSON. In other words, your contention is that this act is directed against the wildcat truckers seeking to avoid the requirements of the Interstate Commerce Commission by posing as farmer groups. Actually, it would be a detriment to yours and two other bona fide farm cooperatives.

Mr. OLSON. We are not trying to put a blanket treatment on it. Our feeling here, once again, is that true cooperatives—the section which we have been legally advised is permissible for us to operate under on a for-hire basis, is one that was designed primarily for true cooperatives, being cooperatives that qualify under the Department. This is why we are not knowledgeable as to other true cooperatives that might be so engaged as we are. So, of course, we are having to set ourselves apart.

We feel that the groups of truckers who have amalgamated and called themselves a cooperative could very well be creating the prospect of disaster to what might have been very honestly established in this section to provide diversification for true cooperatives.

Mr. WATSON. Mr. Olson, you actually believe that you are entitled to continue under the "bona fide cooperative exemption" simply because your stockholders are farmers? Isn't that it? You can have the processing activity and so forth which would remove you from the exemption but simply because your stockholders are farmers then you think that exemption should follow on through the manufacturing process and everything else?

Mr. OLSON. We are required, Mr. Watson, as a cooperative to qualify. Again this is rendering services back to the patrons. These are the people who own the organization, the farmers who own and operate it. We must, as I have said before, we must continue to qualify each year on the basis of services to these members.

Certainly, here is where we feel justified in establishing diversified departments that will help to enhance the way of life for the members.

We comply with the Marketing Act at all times. This cannot be true of a group of truckers.

Mr. WATSON. I agree with you that the farmers certainly have a tight squeeze and ultimately the consumer is paying for it. I appreciate that fact. But if we were to follow your premise, then we would say that a textile mill, the farmers could get together and buy a textile mill and they could bring their wool or their cotton into the textile mill and they manufacture it; just so long as the stockholders are farmers, the exemption would follow them on through in transporting their goods.

Mr. OLSON. Yes, sir. That is the whole idea of the act originally.

Mr. WATSON. I think if we would follow that, we would completely destroy the whole transportation process which is in delicate balance now.

You state on page 7 that even if you were to apply to become a regulated carrier, you would still be subject to the same ceiling of 49 percent.

Mr. OLSON. Yes, sir.

Mr. WATSON. You could apply to be a common carrier if you wish and haul anything. I am not saying it would be granted. It would be based on the public convenience and necessity but you would apply to be a common carrier and then you would not have to worry about any of this. You could haul anything you wished.

Mr. OLSON. No; not and be, again, a qualifying cooperative.

Mr. WATSON. You can't have your cake and eat it, too.

If you want to be a common carrier and carry anything and not be subject to all these limitations, you could apply to be a common carrier, could you not?

Mr. OLSON. I don't know how we could do this as a cooperative.

Mr. WATSON. I mean set up an independent carrier system.

Mr. OLSON. I suspect this would probably not set very well with the qualifications people.

Our cooperatives generally do not engage themselves in outside business as more or less stockholders of it. I don't know legally whether this would be against them or not. It would not be the wish of our company, I am sure.

Mr. WATSON. You could not qualify as a common carrier and still retain your exemption as an agricultural cooperative because the two are imcompatible.

Mr. OLSON. In the qualifications, again, I believe, that it would be specifically held that this business done with nonmembers would still apply to the 49 percent regardless of how you would divide it, set it apart or anything else. Their reaction to that would be nonmember business.

Mr. WATSON. Still, we come back to the basic position right now, it would not hurt you but you are more concerned about the prospective difficulties?

Mr. OLSON. That is true.

Mr. WATSON. More than you are about the present difficulties.

Mr. OLSON. That is true.

Mr. WATSON. Thank you.

Mr. FRIEDEL. The committee will stand in recess until 2 o'clock, provided permission is given, as has been requested.

(Whereupon, at 12:30 p.m., the subcommittee recessed, to reconvene at 2 p.m. the same day.)

AFTER RECESS

(The subcommittee reconvened at 2:30 p.m., Hon. Samuel N. Friedel, chairman, presiding.)

Mr. FRIEDEL. The hearing will come to order. For a continuation of hearings on H.R. 6530 and S. 752 amending section 203(b)(5) and 220 of the Interstate Commerce Act to clarify the exemption with respect to the transportation performed by the Agricultural Cooperative Associations for nonmembers.

The first witness this afternoon will be Mr. Winston M. Boggs, the sales manager of the Agricultural Transportation Association of Texas.

Gentlemen, I will say again that it will be a service to the committee if you summarize your statement by letting us know whether you support the legislation or are opposed to it. Your full statement will be in the record.

STATEMENT OF WINSTON BOGGS, SALES MANAGER, AGRICULTURAL TRANSPORTATION ASSOCIATION OF TEXAS; ACCOMPANIED BY JACK R. COBB, GENERAL MANAGER; AND HOWARD McCORMICK, GENERAL MANAGER, AMERICAN FARM LINES, OKLAHOMA CITY, OKLA.

Mr. BOGGS. Mr. Chairman and members of the subcommittee, I am accompanied by Mr. Jack R. Cobb, general manager of the Agricultural Transportation Association of Texas and Mr. Howard McCormick, general manager of the American Farm Lines, Oklahoma City, Okla., one of the largest transcontinental cooperative trucklines.

Mr. Chairman, I have a very short statement; I will read some of it and then I will insert the rest of it to save your time.

My name is Winston Boggs; I am sales manager for Agricultural Transportation Association of Texas whose main offices are located at 107 NW. 29th Street, Fort Worth, Tex. ATA of Texas is a farm cooperative truckline.

Our board of directors are as follows: Taylor Meriman, traffic manager, Tri-Valley Growers, San Francisco, Calif.; George Rees, general manager, Oxnard Frozen Foods, Oxnard, Calif.; Harry Riddling, Jr., sales manager, Cypress Gardens Citrus Products, Inc., Winterhaven, Fla.; Frank Perez, sales manager, Naturipe Berry Growers, San Jose, Calif.; Joe Marshburn, general manager, Florida Citrus Canners Co-op., Lake Wales, Fla.; Robert Stubbs, sales manager, Plymouth Citrus Products, Plymouth, Fla.; Glen Grader, secretary-treasurer, National Processors, Inc., Albany, Oreg.

All of these are cooperatives.

Our transportation cooperative is made up of farm producing cooperatives and federated cooperatives. We operate 100 pieces of equipment and cover 48 States for our members. We appreciate this opportunity to present our views on S. 752 to your committee. We are outlining our specific objections to the provisions of this proposed bill.

We would like to discuss the basic issues which we believe have been presented for decision.

We do not sanction operations which claim, but are not entitled to, the partial exemption provided by section 203(b)(5) of the Interstate Commerce Act. We support the Interstate Commerce Commission in the enforcement of the law which it has the duty to administer, and we appreciate their problem in dealing with illegal operations that claim co-op exemption. We know there are transportation co-ops that are not bona fide under the definition of cooperative associations as set forth in the Agricultural Marketing Act. These illegal operations should be stamped out, and since they also hurt bona fide agricultural cooperatives and federated co-ops, we believe in, and support, the Interstate Commerce Commission in its enforcement. In fact, we have tried to help Interstate Commerce Commission to enforce the law.

Also we know of some that are illegal that the Interstate Commerce Commission has gotten injunctions and they have been put out of business. So they have some authority. They have some so far as stopping the illegal co-op.

Now, the co-ops that are running transcontinental have only about 500 tractor trailers involved in these co-ops. We haul for our members from the west coast to the east coast and we have no members on the east coast or Midwest so we have to haul back for nonmembers back to the west coast because it is not feasible to deadhead that piece of equipment back.

That is the reason why we think this 752 as passed by the Senate would almost put us out of business because we cannot deadhead our equipment from the east coast back to the west coast. If we run a hundred pieces of equipment over there we could load about 15 of them back and deadhead the rest of them back. This would not be feasible under this. So far as the rest of the law is concerned in S. 752 as passed by the Senate, I think it would be good to be in the bill.

All our objection to the bill is the percentage in the bill of 15 percent. I think the percentage should be left as is in the Agricultural Act that is in force now.

(Mr. Boggs' prepared statement follows:)

STATEMENT OF WINSTON BOGGS, SALES MANAGER, AGRICULTURAL TRANSPORTATION ASSOCIATION OF TEXAS

My name is Winston Boggs; I am Sales Manager for Agricultural Transportation Association of Texas whose main offices are located at 107 N.W. 29th Street, Fort Worth, Texas. ATA of Texas is a farm cooperative truck line. Our Board of Directors are as follows:

Taylor Merriman, Traffic Manager, Tri-Valley Growers, San Francisco, California
George Rees, General Manager, Oxnard Frozen Foods, Oxnard, California
Harry Riddling, Jr., Sales Manager, Cypress Gardens Citrus Products, Inc., Winterhaven, Florida
Frank Perez, Sales Manager, Naturipe Berry Growers, San Jose, California
Joe Marshburn, General Manager, Florida Citrus Canners Coop., Lake Wales, Florida
Robert Stubbs, Sales Manager, Plymouth Citrus Products, Plymouth, Florida
Glen Grader, Secretary Treasurer, National Processors, Inc., Albany, Oregon

Our transportation cooperative is made up of farm producing cooperatives and federated cooperatives. We operate 100 pieces of equipment and cover 48

states for our members. We appreciate this opportunity to present our views on S. 752 to your Committee. We are outlining our specific objections to the provisions of this proposed Bill. We would like to discuss the basic issues which we believe have been presented for decision.

We do not sanction operations which claim, but are not entitled to, the partial exemption provided by Section 203(b)(5) of the Interstate Commerce Act. We support the Interstate Commerce Commission in the enforcement of the law which it has the duty to administer, and we appreciate their problem in dealing with illegal operations that claim coop exemption. We know there are transportation coops that are not bona fide under the definition of cooperative associations as set forth in the Agricultural Marketing Act. These illegal operations should be stamped out, and since they also hurt bona fide agricultural cooperatives and federated coops, we believe in, and support, the Interstate Commerce Commission in its enforcement. In fact, we have tried to help Interstate Commerce Commission to enforce the law.

We know ourselves of several so-called agricultural coops that are now operating and these should be stopped. I think it would be stopped if the Bill S. 752 was passed in regards to the law involved in the bill; but I do not think that the percentage should be changed unless it is just to make the government freight non-member. We have some so-called coops that are operating and were set up just to haul government freight, but I do not think just because there are a few bad apples in a barrel that we should throw out the whole barrelful.

It is necessary for non-member backhaul, when it is not economical or feasible to operate the trucks empty on a return trip. We have members on the West Coast that ship to the East Coast and we have to depend on non-member or government freight movements to get the trucks back to the West Coast to our members. Therefore, if the House of Representatives pass the bill that the Senate has passed, limiting the coops, including government, to 15% non-member movement, then out of 100 trucks sent to the East Coast, we would have to run approximately 85 of them back empty. This would not be feasible for anyone except some of the common carriers that are hauling defense department movements that charge from $1.00 to $1.50 per mile for their backhauls, which I think is a ridiculous rate.

The farmers who are participating in the farm transportation coops are trying to promote the effective merchandising of agricultural commodities in interstate and foreign commerce so that the industry of agriculture will be placed on a basis of economical equality to that of other industries; and to that end, to protect, control and stabilize the current of interstate and foreign commerce in the marketing of their agricultural products. The number of trucks operated by farm cooperatives has increased about 12% during the past six years, while total truck registration increased approximately 30% over the same period. Actually, the cooperative trucks represent 3/10ths of 1% of the total truck registrations in 1966, as compared with 3/10ths of 1% in 1960, so the cooperatives are decreasing instead of increasing as alleged by regulated motor carriers and railroads. So, we do not see why the percentage should be changed in the present Agricultural Marketing Act. There are only approximately 500 tractor-trailers that are operating 1,000 miles or more across country for farm cooperatives. I do not see where this would hurt the motor carriers or the railroads since motor carriers and railroads have thousands and thousands of pieces of equipment operating, so we would oppose the change in the Agricultural Marketing Act as far as the percentage is concerned.

Mr. FRIEDEL. What is the percentage in the old bill?

Mr. BOGGS. Not to do more for nonmembers than you do for members. So it would be 49–51. The Government is exempt now. It does not count for you or against you.

Mr. FRIEDEL. Let me get it clear in my mind. Are you opposed to S. 752?

Mr. BOGGS. Yes, sir; in the form it is now.

Mr. FRIEDEL. In your statement in the fourth paragraph you say: "We know ourselves of several so-called agricultural co-ops that are now operating and these should be stopped. I think it would be stopped if the bill S. 752 were passed."

Mr. BOGGS. Right.

Mr. FRIEDEL. Yet you say you are opposed to it?

Mr. BOGGS. "In regards to the law involved," it says in my statement, "in the bill," but I do not think that the percentage should be changed. I am opposed to it as far as the percentage is concerned but as far as the rest of the bill is concerned, I am not.

Mr. FRIEDEL. Are there any questions, Mr. Adams?

Mr. ADAMS. The only question I had was the same thing that the chairman asked on the 15 percent. If you carry back farm commodities you could go up to—are you still limited to 15 percent?

Mr. BOGGS. Not on farm commodities as far as under section 203(b)(6) which is produce.

Mr. ADAMS. The limitation we worked out this morning was 15 percent for nonmembers, 50 percent farmers and nonmembers, if nonagricultural. But if it is agricultural that comes back, the limitation does not apply.

Mr. BOGGS. If it is agricultural and fresh produce, it goes under section 203(b)(6).

Mr. ADAMS. Is that the only type of agricultural products you can carry that are exempt?

Mr. BOGGS. For nonmembers, yes.

Mr. ADAMS. For nonmembers?

Mr. BOGGS. Yes, sir.

Mr. FRIEDEL. Thank you very much.

Mr. MCCORMICK. Mr. Chairman, I am with the American Farm Lines. We are the largest——

Mr. FRIEDEL. What is your name?

Mr. MCCORMICK. Howard McCormick. We are the largest transcontinental member-owned, farmer-financed, farmer-controlled co-op in existence today that runs transcontinental. We are opposed to any legislation that will be detrimental to the farmers in defense of our country.

That is all we have to say about it.

Mr. FRIEDEL. Thank you very much.

Mr. BOGGS. Thank you, Mr. Chairman.

Mr. FRIEDEL. Our next witness is Mr. W. T. Brady, secretary, Tex-Cal Farmers & Ranchers Cooperative, Inc, Compton, Calif

STATEMENT OF W. T. BRADY, EXECUTIVE SECRETARY, TEX-CAL FARMERS & RANCHERS CO-OP, INC., COMPTON, CALIF.

Mr. BRADY. Mr. Chairman, we also support all of the opposition to this bill. I would like to read my statement. It is very short. I have a couple of small quick observations to make and that will be it, I believe.

My name is W. T. Brady, and I am from Los Angeles, Calif. I am the executive secretary of Tex-Cal Farmers & Ranchers Co-op, Inc., a nonprofit farm cooperative, incorporated under the laws of the State of Texas.

Our association is composed of farm members which have banded together to market the various farm commodities and to transport these commodities under section 203(b)(5) of the Federal Agricultural Marketing Act.

We are most concerned with H.R. 6530—at this point I would like to insert the bill S. 752 which we have been talking about all day—and feel that the passage of this bill will, in its present form, be a detriment to our members as well as thousands of farmers and ranchers throughout the United States. We strongly oppose this bill in its entirety as we feel that the present regulations are more than adequate to regulate the transportation of goods in an economical way from farms to the markets.

The purpose of transportation for our farmers is to transport the goods to the markets economically and, in turn, have some sound, feasible, and economical method to return this equipment back to our members so that the overall cost of transportation will not price our members out of the competitive markets.

If the passage of this bill, in its present form, is completed, it will limit our trucks to haul only 15 percent of nonmember freight as a return haul and we must, therefore, deadhead 85 percent of our trucks to the point of origin. As anyone with simple arithmetic background knows, this is economically impossible and will, therefore, cause the prices of farm goods delivered to the market to be appreciably increased.

I would like to point out at this particular time that it costs within an infinitesimal percentage the same cost to deadhead a truck as it does a full load. Your difference in costs is very, very slight. The only savings basically are the fuel savings.

We have recently read that the common carriers, both truck and rail, have been granted substantial increases for the transportation of commodities; however, we are basically using the same rates in our association that have been used for several years.

Our association is also an approved cooperative by the Department of Defense for the cartage and hauling of their goods from, and to, the various bases throughout the United States. As many of us know, Government freight is exempt from economical regulation under section 22 of the Motor Carrier Act, and under section 203(b)(5), we have been saving the Government untold thousands of dollars on the movement of Government freight.

In these days of higher taxes, through the bill that is pending for the 10 percent surcharge, and the reported $6 billion cut in the national spending, by not passing this bill, we will still be in a position to assist the Government in cutting their cost of transportation.

It has been related to me, by the various transportation people in the Department of Defense, that movement by the agricultural marketing association vehicles has afforded the Government a substantial savings, plus they are receiving through truck service that is faster than the service that they had prior to this time.

I would like to point out at this particular time since we have written the statement we made a little survey. There are 13 approved co-ops of the Department of Defense out of the thousands of co-ops throughout the United States.

These 13 co-ops in the last year and a half have hauled approximately $15 million worth of revenue-producing freight. After studying the tenders that have been filed by the common carriers under section 22 and studying the cheapest tender that the co-ops have filed, under our exemptions that we filed with the Department of Defense we find

a 25 or 30 percent savings for the tax year, meaning that in the last year or year and a half these 13 co-ops have saved the taxpayers $5 million.

This must not be overlooked as we see it.

Mr. FRIEDEL. Let me ask you this question. How many co-ops are there? Do you know?

Mr. BRADY. I have no idea. To my knowledge they are not even cataloged. There are thousands of them.

Mr. FRIEDEL. Do you know what percentage the 13 cooperatives bears to the overall trucking requirements of the Department of Defense?

Mr. BRADY. You mean the total freight that the Government uses the co-ops to ship?

Mr. FRIEDEL. Yes.

Mr. BRADY. I read an article that was published in one of the trade journals a few months ago. It seems to me that it was something less than 1 percent of the total dollars that the Department of Defense spent for freight charges. Yet out of this 1 percent we have estimated a savings to the Government of over $5 million of the taxpayers' money.

This is one of the reasons that we are extremely concerned with this bill. The second reason is that the Department of Defense offers us an opportunity to get our trucks back to the point of origin. We are not like a common carrier that has thousands and thousands of solicitors on the street that can solicit business from every manufacturer in the country.

We have been hauling for the Department of Defense, saving them money. We have no solicitors. Therefore, I feel that by limiting this to 15 percent we will knock the taxpayers out of the savings, plus we will also knock our member farmers from an economical way to move their goods into the market.

This, I think, is the high point that has not been mentioned heretofore.

Now, we feel that if in your judgment this bill must be passed at this session of Congress—we had no knowledge ourselves of the Senate bill at the time of the hearing or we would have been there, but we had knowledge of this hearing last week. So this was quite short notice. I think that if there is such a hurry for the Congress to have to pass a bill, then there is no provision of any kind for a grandfather clause in any of the bills and I appeared before this committee 10 years ago in 1958 and there was a grandfather clause, I personally know, at that time.

I read the original act of 1935 and there was a grandfather clause at that time. So, in effect, if this bill is passed the way it is written, I firmly believe that you will put many, many of these co-ops out of business. The freight then will have to go back through the other channels which I will comment on in a moment that apparently have been unsatisfactory and made the cost of the produce at the markets and the farm products higher than they are today because, as we all know, the cost of everything goes up.

Our transportation basic cost is still about the same as it has been for years.

Mr. FRIEDEL. You may proceed with your statement.

Mr. BRADY. If, in your judgment, this bill must be passed, then we strongly advocate and plead that a section be added to this bill to insert a grandfather clause so that those associations that are presently operating under the existing law will not be put out of business as this bill indicates by sound arithmetical calculations we cannot operate our vehicles under this change. This bill will, therefore, have the effect of eliminating many of the cooperatives that are performing transportation services for nonmembers.

I do not feel that Congress should legislate a lawful business out of existence.

In conclusion and in summary, the passage of this bill will work to the detriment of the farmers and the general public by raising the cost of farm products in the markets and will cost the Government these thousands of dollars. And since this was written, we have run this study, now it is in the millions, for the Department of Defense.

I think that these savings and such economy should not and must not be overlooked. I have a comment or two that I have picked up in the last couple of days. This bill, as I see it, was designed to benefit the common carrier exclusively at the expense of the farmers. Now, the provisions of this bill would destroy the only major source of dependable flexible and economically feasible shipments of farm products to the market, the agricultural cooperatives nonprofit transportation machinery.

Trucks owned and operated by the agricultural cooperatives have been exempt from the ICC regulations for more than 30 years and have been a major factor in protecting the farmer from the high freight rates and poor service that would result from the monopolistic dominance by common carriers.

I have only one other statement. In the Senate Report No. 48 of 1966, common carriers neglected or refused to recognize the needs of the farmers. In this Senate report was noted complaints against common carriers regarding small shipments, shipments to and from areas of lesser volume of traffic shipment, having multiple pickups and deliveries and refusal of shipments that the carriers believed to be marginally profitable.

We feel that by the passage of this bill, if we limit ourselves to 15 percent for backhaul, gentlemen, I don't know how we will get our equipment back to the point of origin. Obviously, we can't deadhead them back.

Mr. FRIEDEL. Are there any questions?

Mr. ADAMS. I have just one question.

I take it then what you wont out of this bill is either a grandfather clause for yourself or you want on page 2 the proviso stricken which says:

Provided, That for the purpose hereof, notwithstanding any other provision of law, transportation performed or on behalf of the United States or any agency or instrumentality thereof shall be deemed transportation performed for a nonmember.

Mr. BRADY. The position of putting the Federal Government into the nonmember category is a rather devastating position to the taxpayers as I see it.

Even though your co-ops only haul less than one percent of the defense dollar, still we are still talking about $5 million worth of taxpayers money. I don't believe this can be overlooked.

So, if the bill is passed as it is written, then there should be a grandfather clause to let the people, who have been doing this and saving the Government this money, be able to continue to save the Government this money.

Then, I think that we are in an awful big hurry here, as I understand you, of deadlines to make, you have a situation that the Congress will have to adjourn very shortly. I don't believe that the time for a comprehensive study has been allowed for this thing.

Mr. ADAMS. You have the ability to carry 50 percent of your total tonnage even if it is nonmember, if it is farmer oriented.

Mr. BRADY. I would appreciate if you would point that out to me.

Mr. ADAMS. That is what I asked this morning. Page 1 of the bill says the transportation performed for nonmembers who are neither farmers, cooperative associations, or federations. That is the 15 percent. The proviso on page 2 says you can carry up to the same quantity if it is for a nonmember but I gather in the agricultural field.

Mr. BRADY. It does not say it though. My reading of it, I interpret it in the manner and I may be entirely wrong. If we haul what we would consider to take as agricultural exempt products under 206(b).

Mr. ADAMS. Up to 50 percent.

Mr. BRADY. It does not say that. There is no proviso for that anywhere that I can find. As I read the bill we can haul 85 percent for members, 15 percent for nonmembers. Let us assume that we have our truck back East and it must come back for a member——

Mr. ADAMS. You have a cooperative association or farmer who is a nonmember, he wants you to backhaul. You can backhaul until you use up to 50 percent of your tonnage.

Mr. BRADY. Where is that?

Mr. ADAMS. Line 5 through line 8 on page 1 and lines 13 to 20 on page 2 there is no other interpretation you can make unless the language means nothing.

Mr. BRADY. What were the lines on the second page.

Mr. ADAMS. The proviso, lines 13 through 20.

Mr. BRADY. I see. I had not read that because I was looking for a percentage figure.

This raises another question, though. Does the 15 percent come off the 50 and go down to 35 for nonmembers?

Mr. ADAMS. This morning I asked that and they said it goes 15 and 35 to make a total of 50. In other words, you go 15 percent for nonmembers. Then you can go an additional 35 percent for people who are farmers or cooperatives who are nonmembers just so long as your total of what you do for nonmembers plus the farmers isn't more than half of your total.

As I gather from your background you are probably transporting citrus products or frozen juices and so on to the East. You could backhaul farmers material within that definition for 35 percent and you could backhaul for nonmembers, nonfarmers, 15 percent.

If I am wrong in that, I would appreciate your submitting a statement so that we can be sure we have the right interpretation.

Mr. BRADY. I am sure what you have said is correct. However, there is a practical operational point where we have a problem. There is

little of the farm products that move into the west coast from some of these areas that are farmers sell and market their products.

Our problem, if there are products that belong to a different farm group or an exempt product, we will call it that, is that the coordination of this is sometimes impossible. So, we do have a great amount of difficulty coordinating the products that would come under the 206(b) section of the law and it becomes an operational problem.

Mr. ADAMS. What do you haul back?

Mr. BRADY. Prior to the time of the Department of Defense we hauled just general freight, sir, and an occasional member load and it was very occasional because the cooperatives that we deal with on the west coast and that we belong to, their major move is from the west coast to the east coast. The move from the east coast to the west coast, there is a limited quantity of cooperative freight coming West.

Therefore, we are forced to find some method to fill our trailers. Upon reading this, it brings another question to mind. I don't know and I would like to ask the gentleman whether he can clarify it. Let us assume that our trucks are back East, can we then trip lease a certificated carrier? Does this count against this 15 percent?

Mr. ADAMS. We haven't said that it would.

Mr. BRADY. I am just asking you. I don't know.

Mr. FRIEDEL. You are supposed to give us the information.

Mr. BRADY. This is the problem because the reason we are against the bill, we feel that there is legislation sufficient to stamp out the abuses that we have listened to all morning.

Mr. FRIEDEL. I understand. If this bill passes you would like to continue doing what you are doing today under a grandfather clause?

Mr. BRADY. Yes, sir.

Mr. FRIEDEL. With no limitation whatsoever on any commodity.

Mr. BRADY. We still have the primary objective in mind that we must serve our members. There are times of the year that the members' commodities for the market are not available. There are different growing seasons and so forth.

There are times when you are going to park a piece of expensive equipment. This works to the farmers detriment also. He has an investment in this.

Mr. FRIEDEL. Mr. Brady, I want to thank you.

Now, we have three other witnesses. The bells have rung. We will have to go back to the floor again. This will be the end of the meeting.

Mr. James Cardwell, president of the Midwest Growers Cooperative Corp., Oklahoma City, Okla.

STATEMENT OF JAMES CARDWELL, GENERAL MANAGER, TRANSPORTATION OFFICE, MIDWEST GROWERS COOPERATIVE CORP., OKLAHOMA CITY, OKLA.

Mr. CARDWELL. Mr. Chairman and members of the committee, I will try to make this rather brief. My name is James Cardwell, general manager of the Transportation Office of Midwest Growers Cooperative of Los Angeles.

My statement is on file here. It is a matter of the record.

I would like to make a few comments. I would like you to know that we are against the bill in its present form. Also, I would like to bring out that we do save the Department of Defense a substantial

amount of money. I would like you to know that we are not in any way in the manufactured business. Our members grow the products and we haul to the various markets of the Nation.

Consequently, we back haul whatever goods we can get.

(Mr. Cardwell's prepared statement follows:)

STATEMENT OF JAMES CARDWELL, GENERAL MANAGER, MID-WEST GROWERS COOPERATIVE CORP., OKLAHOMA CITY, OKLA.

Mr. Chairman, my name is James Cardwell, and I am the General Manager of the Transportation Office of Mid-West Growers Co-operative Corp., Los Angeles office, which is non-profit farm co-operative incorporated under the laws of the State of Oklahoma.

Mid-West Growers Co-operative Corp. is composed of various farm members banded together to market their various farm products and transport the products under Section 203(b)(5) and 203(b)(6) of the Interstate Commerce Act. We operate with the purpose of transporting the goods of our members to the markets economically and, in turn, have some sound, feasible and also economical method of returning this equipment back to our members in order to maintain an over all cost which will keep our members competitive in the markets.

We are greatly concerned with Bill H.R. 6530 as we feel that the passage of this bill, as it is presently drafted, will prove detrimental not only to our members, but to the thousands of ranchers and farmers throughout the nation. We very strongly oppose the entire bill because, in our opinion, the present regulations more than adequately regulate the transportation of goods, while maintaining an economical manner of doing so.

This bill, as drafted, will limit our trucks to haul only 15% of non-member freight on the return haul and would, therefore, force us to dead head 85% of our trucks back to the original shipping point. This, in effect, would be mathematically and economically impossible and would force the price of farm commodities to be drastically increased in the markets.

Should you definitely feel that a bill of this nature must be passed, we feel that a practical solution would be the insertion of a "grandfather" clause which would insure the cooperatives that are presently operating under the existing law that they would not be put out of business, which the bill as written would certainly do. These cooperatives operating at the present are completely lawful, and we do not feel that Congress should legislate the lawful business out of existence.

We have been approved by the Department of Defense to haul their freight to various locations and bases in the United States. This is exempt from economical regulation under section 22 of the Motor Carrier Act, and by operating for the Department of Defense under Section 203(b)(5), we have been able to reduce the transportation costs for the Department of Defense. It is our understanding, through conversations with various employees for the Department of Defense, that the Department of Defense is receiving faster service because the vehicles which operate under the Agricultural Marketing Act provide "through" truck service at the substantial savings to the government.

In closing, we wish to stress the fact that the passage of this bill, as presently written, will only cause an overall increase in farm commodity costs and will be detrimental to the farmers and the general public. We feel that the savings of thousands of dollars to the Department of Defense, which is presently being afforded by using the Agricultural Marketing vehicles, cannot, should not and must not be ignored and should certainly be taken into consideration.

Mr. FRIEDEL. Thank you, Mr. Cardwell. Are there any questions?

Mr. ADAMS. No.

Mr. FRIEDEL. Our next witness will be Mr. Howard Mecom, general manager of the United Agricultural Transportation Association of America Marketing Co-op.

STATEMENT OF JOHN CABANISS, COUNSEL, UNITED AGRICULTURAL TRANSPORTATION ASSOCIATION OF AMERICA MARKETING CO-OP, WACO, TEX.

Mr. CABANISS. Mr. Chairman and members of the committee, my name is John Cabaniss, Waco, Tex., attorney for the United Agricultural Transportation Association of America Marketing Co-op, of which Mr. Howard Mecom is the general manager. And if I may, I am appearing in his behalf. I will take about 2 minutes of the committee's time. We are trying to help on this. We are against the bill.

Mr. Brady, Mr. McCormick and a number have summed up some of the objections which we have and selfishly we would like to state this for the record, that the board of directors of our co-op has directed us to let the Interstate Commerce Commission inspect the records at any and all times, which they have done and which they have been doing since September 21, 1966 when we were incorporated.

Now, in aid of this committee's work we would like to present one thing. I knew of this as an attorney about Sunday, when I caught a plane. So I grabbed something out of my briefcase that has been of invaluable aid to me. I would like to mention the author's name because I think it is deserving.

He is a law student in Hastings Law School out in California. He is a young man. His name is Charles B. Wiggins. He wrote an article called "Non-Farm Backhauls for Non-Members of Agricultural Cooperatives: Impact of the Northwest Decision."

If you have ever done a little graduate work, in the paper that the professor called for he wants a good style paper and wants you to give a little background and go into historical interpretation of the particular topic you are on, you know how important it is to have someone who can sit down and lay out cold turkey for you. This young man does it.

Mr. FRIEDEL. Would you like to have it printed in the record?

Mr. CABANISS. I would like to, sir.

We thank you for your time.

(The documents referred to follow:)

STATEMENT OF HOWARD MECOM, GENERAL MANAGER, TRANSPORTATION OFFICE, UNITED AGRICULTURAL TRANSPORTATION ASSOCIATION OF AMERICA, MARKETING CO-OP, WACO, TEX.

Mr. Chairman, my name is Howard Mecom and I am the General Manager of the Transportation Office of United Agricultural Transportation Association of America, Marketing Co-op, Los Angeles office. We are a corporation formed under the laws of the State of Texas and are a non-profit cooperative.

Our co-operative consists of members who have banded together to market and transport farm commodities under Section 203(b)(5) and 203(b)(6) of the Interstate Commerce Act. We have, under present laws, transported members' products economically to the market places of the United States and are able to use non-member freight for return of the vehicle back to the point of origin. This method has proved economically sound and has helped keep the cost of farm commodities from drastically increasing.

I am here to state our opinions and views on Bill HR-6530 about which we are extremely alarmed and concerned. This bill, in its present form, will limit our trucks to haul only 15% non-member freight on the return haul, meaning that 85% of the return haul would have to be dead head. This, I am sure you can see, would be economically impossible to do without causing a tremendous increase in the cost of farm products and commodities.

If it is felt that legislation should be granted and passed, we feel that the cooperatives that are presently operating should be protected by, perhaps, the inclusion of a "Grandfather Right" clause which would allow these co-operatives to continue in business. This bill, as presently drafted, would surely put many of the cooperatives out of business. We do not feel that legislation should be passed whereby a lawful business will be forced out of existence.

In the minutes of our co-operative, the Board of Directors have directed me to let the Interstate Commerce Commission check our books and records, which they have constantly done. We have, at all times, fully cooperated with the Interstate Commerce Commission; however, under the existing law, we are not required to do this. I, therefore, feel that if this bill is passed, we should have "grandfather rights" as we have always cooperated with the Interstate Commerce Commission and complied with their regulations.

We also operate as a cooperative approved by the Department of Defense to haul their freight. This government freight is exempt from economical regulation under Section 22 of the Motor Carrier Act, and by operating under Section 203 (b) (5) for the Department of Defense, we have helped reduce the cost of transportation for this branch of the government. It appears to me that this phase of our operation is very important, especially in view of the current tax increase and in view of the fact that there is a six billion dollar cut in the budget. The savings our vehicles have been giving to the government should certainly be taken into consideration as I am sure you can realize this type of savings is very important to the national budget.

It is our opinion, as well as many members of the Department of Defense, that the service rendered by the cooperatives is faster than service previously received, since we are able to provide "through" transportation. This phase is also very important to the Department of Defense.

It was recently approved that the common carriers, including rail and truck, have substantial rate increases. We wish to point out, however, that we have maintained basically the same rates for several years. This is an important factor to the farming and ranching markets and has been a prime factor in the cost of farm commodities.

To summarize our opinions and views, we feel that the passage of this bill will be detrimental to the general public and the farmers and will create an increase in the cost of farm commodities. It will also endanger the existence of lawful businesses that are presently assisting the government in substantial savings in the cost of transportation. We feel that these facts must be very fully and carefully considered.

Thank you very much.

Nonfarm Backhauls for Nonmembers of Agricultural Cooperatives: Impact of the Northwest Decision

(By Charles B. Wiggins, Hastings Law School, California)

In 1965, the Court of Appeals for the Ninth Circuit, in *Northwest Agricultural Cooperative Association* v. *ICC*,[1] held that agricultural cooperatives which haul nonagricultural products to and for nonmembers maintain their transportation exemption from the Interstate Commerce Act,[2] provided such activity is "necessary and incidental" to the statutory purpose of the association. The decision broadened the scope of activities which had been permitted by the Interstate Commerce Commission under this exemption, and climaxed a continuing dispute between the Commission and the courts as to the nature and limitations of the cooperative exemption, most significantly from the regulation of rates. It is the purpose of this discussion to examine the present status of the cooperative exemption, based on the *Northwest* decision, by analyzing the various positions expounded as to the proper statutory construction, and the ramifications of proposals for change in the regulatory system.

---

[1] 350 F.2d 252.
[2] 49 U.S.C. ch. 8 (1964).

THE NORTHWEST DECISION

The Interstate Commerce Commission [3] sought to enjoin [4] Northwest Agricultural Cooperative Association [5] from engaging in certain transportation activities in alleged violation of the Interstate Commerce Act.[6] It claimed that the nonmember backhauling of nonagricultural products by Northwest could not be performed without requisite Commission authorization.[7] Northwest contended [8] that it was an agricultural cooperative, exempt from the regulations of the Commission by virtue of section 303, which provided:

(b) Nothing in this chapter, except the provisions of section 304 of this title relative to qualifications and maximum hours of service of employees and safety of operation or standards of equipment shall be construed to include . . . (5) motor vehicles controlled and operated by a cooperative association as defined in the Agricultural Marketing Act, approved June 15, 1929, as amended, or by a federation of such cooperative associations, if such federation possesses no greater powers or purposes than cooperative associations so defined . . .[9]

Northwest was organized under the Idaho Cooperative Marketing Act [10] "for the purpose of transporting the agricultural products of its members to market at a lower cost than that which the members would incur if transportation were arranged by each member individually." [11] Outbound, Northwest owned-and-operated vehicles carried the products of its members to market. Returning, so far as was possible, these trucks hauled farm supplies required by its members. However, the demand for such supplies did not meet the volume of members products hauled to market. Therefore, in lieu of returning empty, these vehicles hauled, on a for-hire basis, nonfarm products and supplies from and for nonmembers of the association. These nonfarm backhauls accounted for less than 18 percent of Northwest's total revenue for a 4-month test period.[12] It was these nonfarm backhauls the Commission sought to enjoin.

A "cooperative association" is defined by the Agricultural Marketing Act [13] in these terms:

"[C]ooperative association" means any association in which farmers act together in processing, preparing for market, handling, and/or marketing the farm products of persons so engaged, and also means any association in which farmers act together in purchasing, testing, grading, processing, distributing, and/or furnishing farm supplies and/or farm business services: *Provided, however,* That such associations are operated for the mutual benefit of the members thereof as such producers or purchasers. . . .

* * * * * * *

And in any case [conform] to the following:

. . . [T]he association shall not deal in farm products, farm supplies, and farm business services with or for nonmembers in an amount greater in value than the total amount of such business transacted by it with or for members.[14]

Northwest contended that, as a cooperative association within the statutory definition, it remained exempt so long as its total dollar volume of member business exceeded its nonmember business.[15] Its status should not change because its backhauls were of nonagricultural products for nonmembers. Rather, since these backhauls were incidental to its main purpose as a hauler of member products, and comprised less than half of its total business revenue, the association should still remain within the statutory exemption.

The Commission countered this statutory construction.[16] It contended that the terms of the exemption extend only to activities "directly beneficial or function-

---

[3] Hereinafter referred to as Commission.
[4] 234 F. Supp. 496 (D. Ore. 1964).
[5] Hereinafter referred to as Northwest.
[6] The alleged violations were of 49 U.S.C. §§ 303(c), 306(a), 309(a) (1964).
[7] 234 F. Supp. at 498.
[8] *Id.*
[9] 49 U.S.C. § 303(b)(5) (1964).
[10] 5 IDAHO CODE ANN. §§ 22–2601 to –2628 (1948).
[11] Brief for Appellant at 3, Northwest Agric. Cooperative Ass'n v. ICC, 350 F.2d 252 (9th Cir. 1965).
[12] *Id.*; 350 F.2d at 253.
[13] 12 U.S.C. §§ 1141–41j (1964).
[14] 12 U.S.C. § 1141j(a) (1964).
[15] 350 F.2d at 253–54.
[16] *Id.*

ally related" [17] to the marketing of member products or to the provision of member supplies and/or member business services. Northwest's provision of for-hire transportation was not so related to permissible activities. Therefore, it was not entitled to exemption, but was subject to the Commission's regulations.

HELD: *Judgment for Northwest.* Northwest complied with the statutory requirements, and was a "cooperative association" within the definition expounded by the Agricultural Marketing Act. The statutory provision limits *farm* activities performed for nonmembers, but this cannot be construed as an express prohibition of all *non*farm activities.[18] Such nonfarm activities must only be "incidental and necessary" to the cooperative's main purpose of marketing farm products and furnishing farm supplies and farm business services for members.[19] Northwest's nonmember backhauls were necessary, since without them, it could not have transported member products as cheaply as the cost of common carriage. They were incidental, comprising less than 18 percent of total business revenues. Northwest, therefore, retained its exemption by the application of this test.[20]

DETERMINATION OF LEGISLATIVE INTENT

The Interstate Commerce Act

Northwest was decided on the ultimate question of statutory construction. The court was faced with interpreting the Interstate Commerce Act and the Agricultural Marketing Act, both enacted at different times to settle different legislative problems. Of these, the legislative history of the Interstate Commerce Act is the most elucidating, and has posed the most problems.

The agricultural cooperative exemption to the Interstate Commerce Act [21] became law as part of the Motor Carrier Act of 1935.[22] The purpose of that legislation was expressly stated to be the regulation of motor carrier transportation so that economical and efficient service could be promoted "without . . . undue preferences or advantages, and unfair or destructive competitive practices. . . ." [23] The regulatory power of such a policy was vested in the Interstate Commerce Commission.[24] In enacting the bill, Congress provided its own interpretation of the policy statement:

[Y]our committee has no intent to undertake to suppress or restrict in any way the development of motor-carrier transportation by responsible carriers for the good of the public interest. Nor do we want motor-carrier transportation subservient to or restrained or curtailed by any other transportation medium. The purpose of this bill is to provide for regulation that will foster and develop sound economic conditions in the industry, together with other forms of public transportation, so that highway transportation will always progress.[25]

Congress thus indicated its intent that the Motor Carrier Act was to be a remedial statute, designed to redress inadequacies of motor carrier regulation and to protect the public welfare against future undesirable practices. The Interstate Commerce Commission was empowered to regularize, supervise, and ultimately to regulate motor carrier activities in the public interest.

The cooperative exemption was not part of the Motor Carrier Act as originally proposed, but was added by floor amendment.[26] Discussion of the proposal was not extensive.[27] However, some indication of legislative purpose can be ascertained from the Congressional debate.

It is clear from the discussion in the House of Representatives that the basic issue was one of nonmember business conducted by cooperative associations. As described by its proponent, Representative Marvin Jones,

[t]his exemption is consistent with the purpose of the act to regulate the use of highways by persons and corporations who use them regularly as places of business and as the primary means of gaining a livelihood. Cooperative associations do not act as moneymakers in transportation. The hauling is done as a means of reducing the marketing expenses of their members.

---

[17] Brief for Appellee at 17, Northwest Agric. Cooperative Ass'n v. ICC, 350 F.2d 252 (9th Cir. 1965).
[18] 350 F.2d at 256.
[19] *Id.* at 257. This test is hereinafter referred to as the "necessary and incidental" test.
[20] Northwest Agric. Cooperative Ass'n v. ICC, 350 F.2d 252 (9th Cir. 1965), *rev'g* 234 F. Supp. 496 (D. Ore. 1964), *cert denied,* 382 U.S. 1011 (1966).
[21] 49 U.S.C. § 303(b)(5) (1964).
[22] 49 Stat. 543.
[23] *Id.*
[24] *Id.*
[25] 79 CONG. REC. 12,205 (1935).
[26] *Id.* at 12,220.
[27] *Id.* at 12218–22.

Especially in highly organized communities it is almost essential they do some hauling for nonmembers. Otherwise certain farmers who are only temporarily in the community and in some instances tenants might be left without transportation facilities. In some instances it reduces the expense of handling to combine some hauling for nonmembers. This does not mean going into the general business of transportation. It is merely incidental to the hauling for their own members. It is a practical proposition.[28]

And again:

This will not open the gate for a lot of men to go into the trucking business and thus escape, because the moment they haul more for outside people than they haul for their own members they will be out of the window so far as the exemption is concerned.[29]

While it is clear that Congress anticipated some nonmember hauling would take place under the exemption—in fact indicated that this would be necessary to effect the general purpose of the Motor Carrier Act—the permissible limits of this activity were not defined in the debates. A pertinent comment was made during Congressional consideration of the Act, however, which offers evidence of the Congressional limits anticipated.

While the definition referred to permits the cooperatives to deal in and transport the products of non-members, restrictions in the definition and practical considerations make it impossible for cooperatives to engage in outside trucking to a degree that would injure regular, for-hire motor carriers.[30]

The Agricultural Marketing Act

The cooperative exemption to the Interstate Commerce Act refers for definition to the Agricultural Marketing Act.[31] The latter Act establishes the Farm Credit Administration, a function of which is to make loans to eligible cooperative associations meeting the statutory qualifications.[32] In section 1141j of the Act, the cooperative definition is propounded. The difficulty in interpretation has come with respect to the third requisite for qualification, that a cooperative, "shall not deal in farm products, farm supplies, and farm business services with or for nonmembers in an amount greater in value than the total amount of such business transacted by it with or for members." [33]

It is significant to note that the Interstate Commerce Act provision exempts cooperatives "as defined in the Agricultural Marketing Act" [34] rather than merely referring to the specific cooperative definition expressed in section 1141j of that Act. This indicates that the scope and purpose of the entire Act should be taken into account when applying the bare words of the definition to the facts of a particular case, and provides yet another source of determining the intent of Congress as to those organizations falling within the definition.

The policy of the Agricultural Marketing Act is expressed in section 1141. This section provides:

"(a) It is declared to be the policy of Congress to promote the effective merchandising of agricultural commodities in interstate and foreign commerce so that the industry of agriculture will be placed on a basis of economic equality with other industries, and to that end to protect, control, and stabilize the currents of interstate and foreign commerce in the marketing of agricultural commodities and their food products—

* * * * * * *

"(2) by preventing inefficient and wasteful methods of distribution.

"(3) by encouraging the organization of producers into effective organizations or corporations under their own control for greater unity of effort in marketing and by promoting the establishment and financing of a farm marketing system of producer-owned and producer-controlled cooperative associations and other agencies.[35]

In view of the general reference to this policy in the exemption clause of the Interstate Commerce Act, the purpose of the definition should be considered in light of the avowed congressional policy establishing that definition.

---

[28] *Id.* at 12,218.
[29] *Id.* at 12,219.
[30] Letter from Joseph D. Eastman, Federal Coordinator of Transportation, to Senator Wheeler, July 27, 1935, *quoted in* Machinery Haulers Ass'n v. Agricultural Commodity Serv., 86 M.C.C. 5, 15 (1961).
[31] 12 U.S.C., §§ 1141–41j (1964).
[32] 12 U.S.C. § 1141e (1946).
[33] 12 U.S.C. § 1141j(a) (1964).
[34] 49 U.S.C. § 303(b)(5) (1964).
[35] 12 U.S.C. § 1141(a)(2)–(3) (1964).

The contemporaneous constructions placed upon the provisions of the Interstate Commerce Act by the Commission which possesses special competence in this field, are entitled to great weight and respect and will not be overturned unless they are arbitrary or plainly erroneous.[36]

The traditional concern of the Interstate Commerce Commission in dealing with cases arising from the cooperative exemption has been to prevent an association, under the guise of the exemption, from engaging in transportation as a public carrier for-hire.[37] This concern manifests the problem the Commission has had in attempting to impose any form of regulation on cooperatives.

The Commission must enforce the regulatory provisions within its authority with a view toward promoting the "National Transportation Policy." [38] designed to encourage the establishment and maintenance of reasonable charges for transportation services, without unjust discrimination, undue preferences or advantages, or unfair or destructive competitive practices . . . and enforced with a view to carrying out the above declaration of policy.[39]

But exempt cooperatives which engage too extensively in the area of for-hire carriage of nonmember and nonagricultural goods, will be in derogation of this "Policy" restriction on "unjust discriminations, undue preferences or advantages."

Logically, the Commission's position seems sound. An agricultural cooperative is exempt from all regulatory control, except for safety and hours of service provisions, merely by being such a bona fide cooperative.[40] Since it is exempt, a cooperative need have no contact with the Commission whatsoever. It is not required to file a petition for exemption, or to describe its exempt activities in any way. The practical effect of this is that by declaring itself exempt, a cooperative, whether actually exempt or merely claiming to be exempt, can operate in interstate commerce in any way the cooperative itself may determine to be permissible under the statute.

The Commission has the power to investigate violations of the statutes within its jurisdiction, either upon the receipt of a complaint concerning such practices,[41] or upon its own motion.[42] It may also apply to the appropriate district court to enjoin operations by motor carriers in violation of the statutory regulations.[43] However, the problem of administration of such provisions is clear: before bringing any action against a cooperative, the Commission must first have knowledge, either independently or furnished by complaint, of both the existence of the cooperative and the nature and extent of its unpermitted activities. But where there is no requirement for cooperatives to notify the Commission of their activities, or even of their existence, organized and rational supervision becomes all but impossible.

The Interstate Commerce Commission must attempt to regulate the transportation activities of agricultural cooperatives, consistent with its purpose to prevent "undue preferences or advantages, and unfair or destructive competitive practices." [44] However, it is unable to maintain even supervisory authority over the operations of these cooperatives, since there is no requirement of qualification for exemption by application to the Commission. Faced with this dilemma, the Commission may take two cources of action: it may seek a change in the law to enable it to obtain knowledge at least of the existence of those cooperatives entitled to exemption, or it may work with the present legislation, and attempt to confine the exemption by construing the statutes in accordance with its viewpoint. In fact, both these courses of action have been attempted.

---

[36] ICC v. Weldon, 90 F. Supp. 873, 877 (W.D. Tenn. 1950); *accord,* East Tex. Motor Freight Lines, Inc. v. Frozen Food Express, 351 U.S. 49, 54 (1957).

[37] Northwest Agric. Cooperative Ass'n v. ICC, 350 F.2d 252, 256 (9th Cir. 1965); ICC v. Jamestown Farmers Union Federated Cooperative Transp. Ass'n, 151 F.2d 403, 404 (8th Cir. 1945); Cache Valley Dairy Ass'n Investigation of Operations, 96 M.C.C. 616, 620 (1964); Agricultural Transp. Ass'n of Tex. Investigation of Operations, 96 M.C.C. 293, 299 (1964); Machinery Haulers Ass'n v. Agricultural Commodity Serv., 86 M.C.C. 5, 24 (1961).

[38] Transportation Act of 1940, ch. 722, § 1. 54 Stat. 898, 899.

[39] *Id.*

[40] 49 U.S.C. § 303(b) (1964).

[41] 49 U.S.C. § 13(1) (1964).

[42] 49 U.S.C. § 13(2) (1964).

[43] 49 U.S.C. § 322(b)(1) (1964) (this is the provision utilized by the Commission in *Northwest*).

[44] 49 Stat. 543 (1935).

COMMISSION POSITION

Recommendations for Statutory Change

The Commission has recommended consistently that changes be made in the existing laws to allow it more control over the carriers exempt from its regulation. It is responsible for enforcing the safety and hours of service regulations of the Interstate Commerce Act even as to exempt haulers such as cooperatives,[45] and has urged legislative action that would provide some means for determining the operation of exempt carriers in order to enforce compliance with these applicable regulations.[46] In response to such requests, bills were introduced into Congress in 1957 [47] which would have required the yearly filing of a short statement identifying the carrier and its activities by all carriers exempt from regulation but subject to the safety provisions of the Act.

The recommended amendment would not require the filing of complicated or elaborate reports. It is only necessary that we be kept informed respecting the identity of such carriers, their location, and the number of vehicles owned or operated. This could be accomplished through the simple expedient of mailing a postcard once a year.[48]

Each bill died in committee.[49]

In 1961, the Commission changed its position. Rather than requiring the mere registration of carriers as it had done previously, it sought to gain substantive regulatory control over the exempt haulers. The Commission found that organizations were often claiming exempt status for themselves as cooperatives, even though they were clearly not qualified for exemption. This practice siphoned off a substantial amount of revenue from goods that would otherwise be transported by carriers subject to Commission regulation. Further, even when these unqualified exempt carriers were identified, the Commission was unable to overcome the "presumption of eligibility" which each carrier claiming exemption possessed.[50]

Bills were introduced in two separate Congressional sessions.[51] These bills, if enacted, would have required that in order to obtain an exemption, cooperatives claiming exempt status would be required to apply for and receive a certificate of exemption issued from the Commission, attesting to their inclusion within the Agricultural Marketing Act definition. Again the bills died in committee.[52] In the presentation of one of the bills [53] it was stated that

> [w]hile the number of groups and organizations claiming exemptions as agricultural cooperatives has grown considerably in the last 10–15 years, the Commission is not presently equipped with authority effective enough to weed out those which are not entitled to the exemption or to prevent other such persons from commencing operations. . . .
>
> It is not the purpose of the proposed measure to interfere in any way with the legitimate operations of bonafide agricultural cooperatives under the exemption provided in the Interstate Commerce Act. It is, however, designed to enable the Commission to cope more effectively with groups and organizations using this exemption as a device to engage in unlawful transportation activities.[54]

It is justifiable to infer that, due to its history of inaction concerning the statutes proposed in this field, Congress does not wish to answer the pleas of the Commission with remedial legislation aimed at ameliorating the existing situation. For whatever reasons, Congress is unwilling to change the inherently ambiguous nature of the agricultural cooperative exemption. This refusal forces the Commission to act within its limited scope in attempting to regularize the carriers claiming its benefit.

---

[45] 49 U.S.C. § 303(b) (1964).
[46] 69 ICC ANN. REP. 129 (1955). The same recommendation is made in 70 ICC ANN. REP. 165 (1956) and 71 ICC ANN. REP. 139 (1957).
[47] S. 1490, 85th Cong., 1st Sess. (1957); H.R. 5664, 85th Cong., 1st Sess. (1957).
[48] 71 ICC ANN. REP. 139–40 (1957).
[49] CCH 1957–1958 CONG. INDEX 3555, 5570.
[50] 75 ICC ANN. REP. 184 (1961). The same recommendation is made in 76 ICC ANN. REP. 201 (1962), 77 ICC ANN. REP. 19 (1963), and 78 ICC ANN. REP. 76–77 (1964).
[51] S. 677, 88th Cong., 1st Sess. (1963); H.R. 3770, 88th Cong., 1st Sess. (1963); S. 1729, 89th Cong., 1st Sess. (1965); H.R. 5400, 89th Cong., 1st Sess. (1965).
[52] CCH 1963–1964 CONG. INDEX 3547, 5565; CCH 1965–1966 CONG. INDEX 3552, 5566.
[53] S. 1729, 89th Cong., 1st Sess. (1965).
[54] 111 CONG. REC. 7064–65 (1965) (remarks of Senator Magnuson, Chairman of the Commerce Committee, in which this measure died).

Construction of the Existing Statutes

Nonfarm Business Prohibited

Unable to effectuate its recommendations in congressional action, the Commission has worked within its investigatory framework in attempting to define the limits of exempt operations, either by its own proceedings or by judicial interpretation. It has urged persistently that the exemption provisions of the Motor Carrier Act [55] should be strictly construed so that cooperatives shall not be allowed to engage indiscriminately in for-hire carriage for nonmembers.[56] Its contention is that the Motor Carrier Act is a remedial statute.[57] Exemptions to such statutes must be applied as narrowly as possible to permit application of the regulatory provisions to all carriers within its scope.[58]

With reference to the definition of the cooperative associations found in the Agricultural Marketing Act,[59] the Commission implies an inherent limitation. The third proviso of that definition states that a cooperative "shall not deal in *farm* products, *farm* supplies, and *farm* business services with or for nonmembers" [60] in excess of its member activities. To the Commission, the express mention only of *farm*-related activities indicates that Congress did not anticipate that cooperatives would engage in *non*farm-related dealings at all,[61] or at least that whatever nonfarm-related dealings a cooperative did have would have to be "functionally related" to its principal farm-related function.[62] Thus, to the Commission, non*member* dealings were obviously anticipated,[63] but the incidental hauling of agricultural products for nonmembers is far different from the hauling of nonagricultural products to and for nonmembers, and such incidental hauling should not be covered by the exemption.[64]

In its brief filed for the *Northwest* appeal, the Commission made this position clear by applying the maxim of statutory construction "*Expressio unius est exclusio alterius*" [65] to the facts of that case.[66] The Commission found that

> [a]pplying this maxim to 12 USCA Section 1141j(a), a cooperative association means an association in which *farmers* act together doing the things mentioned therein, all of which have to do with *farm* products, *farm* supplies or farm [*sic*] business services. It excludes all matters not included in these terms. . . . It specifically includes only farm items, and therefore excludes all non-farm activities.[67]

Since this was the case, then all nonagricultural backhauls for nonmembers must be, by the terms of the statutory definition itself, outside the scope of proper activities performed by a cooperative.

Logically, it appears that the maximum is inapplicable in this situation. The Agricultural Marketing Act prohibits the provision of more nonmember than member business. This is not a test of inclusion, as required for application of the maxim, but of exclusion.

Accordingly, if the maxim is applied here, the result is that the section must be deemed to contain *all* the factors that would disqualify the association and all other activities must be construed as not so prohibited.[68]

This is neither the position the Commission would advocate nor the position that should be taken with respect to the statute. The maxim should not be applied when it can, by one interpretation, eliminate the substantive restrictions on the nature of a cooperative's business altogether.

---

[55] 49 Stat. 543 (1935).
[56] Machinery Haulers Ass'n v. Agricultural Commodity Serv., 86 M.C.C. 5, 24 (1961); ICC v. Jamestown Farmers Union Federated Cooperative Transp. Ass'n, 151 F.2d 403, 404 (W.D. Tenn. 1945); Cache Valley Dairy Ass'n Investigation of Operations, 96 M.C.C. 616, 620 (1964); Agricultural Transp. Ass'n of Tex. Investigation of Operations, 96 M.C.C. 293, 297 (1964).
[57] ICC v. Weldon, 90 F. Supp. 873, 876 (W.D. Tenn. 1950).
[58] McDonald v. Thompson, 305 U.S. 263, 266 (1938).
[59] 12 U.S.C. § 1141j(a) (1964).
[60] *Id.* (emphasis added).
[61] *See* ICC v. Jamestown Farmers Union Federated Cooperative Transp. Ass'n, 151 F.2d 403, 404 (8th Cir. 1945).
[62] Machinery Haulers Ass'n v. Agricultural Commodity Serv., 86 M.C.C. 5, 25 (1961).
[63] *Id.* at 24.
[64] Cache Valley Dairy Ass'n Investigation of Operations, 96 M.C.C. 616, 620 (1964).
[65] "Expression of one thing is the exclusion of another." BLACK'S LAW DICTIONARY 692 (4th ed. 1951).
[66] Brief for Appellee at 9, Northwest Agric. Cooperative Ass'n v. ICC, 350 F.2d 252 (9th Cir. 1965).
[67] *Id.* at 10.
[68] Reply Brief for Appellant at 6, *id.*

If the Commission's interpretation is correct, the following result is inevitable:

Statutory language: "the association shall not deal in farm products, farm supplies, and farm business services with or for nonmembers in an amount greater in value than the total amount of such business transacted by it with or for members." 12 U.S.C. § 1141j(a).

Interpolations required . . . : [all of the foregoing, plus] " . . . the association shall not deal in or transport any nonfarm products, nonfarm supplies, or nonfarm business services either for members or nonmembers . . ." [69]

Nowhere is this restriction provided for; and prior discussion indicates that this interpretation is unacceptable in light of indications of legislative intent, both at the time the Motor Carrier Act was enacted and also when additional regulatory legislation has been introduced in Congress without success. Therefore, this proposal by the Commission should be rejected.

Nonmember Business Restricted: The Courts and the Commission

The Commission, both by its proposals for change and its construction of the existing statutes, has sought to keep the number of exempt cooperatives to the minimum permitted by a literal interpretation of the statutory definition. The rulings of the courts, however, have not lent support to this position. Rather, they have tended to broaden the scope of the exemption in keeping with their liberal view as to the proper statutory construction.[70] This dichotomy can best be shown by comparing the Commission's interpretations with the answers of the courts.

There is a basic interpretational difference of opinion between the Commission and the courts that is vitally important to the area under discussion. The Commission adheres to the view that

> transportation rendered by a cooperative association must be assessed in light of the essential relationship between the association and its members in their capacities as producers of farm products and purchasers of farm supplies and/or farm business services; and, in order to come within the so-called agricultural cooperative exemption, *such transportation, whether performed for members or nonmembers, must be designed to benefit directly, or be functionally related to its members' activities as such producers and purchasers.*[71]

The courts, on the other hand, have tended to see that

> [n]ecessarily goods must be handled by them which may not be strictly farm suppliers. Some of their customers may not be members or even farmers. But if the cooperative is predominantly engaged in one or more of the activities specified in the Agricultural Marketing Act, and if its business with nonmembers is in an amount not greater in value than the total amount of the business that it transacts with its own members, such association does not lose its fundamental character as a cooperative. In other words, *if such activities are merely incidental to, and necessary for the effectuation of the cooperative's principal activities as embraced within the Act*, the status of the cooperative remains unimpaired.[72]

This conflict between application of the "functionally related" test and the "incidental and necessary" test has caused much difficulty for cooperatives, the Commission, and the courts.

What the parties mean by these phrases is not altoghter clear, but certainly the Commission would impose a more stringent construction on the nature of the nonmember business. To be "functionally related" within the Commission's test, backhauls would have to be "directly essential to the activities of the members of the cooperative in their capacities as producer [*sic*] of farm products, or as purchasers of farm supplies and farm business services." [73] This would seem to suggest, for example, that the backhauling of fertilizer for nonmembers would be acceptable only if a partial backhaul load was required by members, with the space remaining used to haul fertilizer to be sold to nonmembers, but that backhauling such a product for sale to nonmembers, when there was no member demand for it, would not be permitted. It is unlikely that Congress, in enacting

---

[69] Brief for Secretary of Agriculture as Amicus Curiae at 9, *id.*

[70] *See* Chandler, *Convenience and Necessity: Motor Carrier Licensing by the Interstate Commerce Commission,* 28 OHIO ST. L.J. 379, 384–85 (1967).

[71] Machinery Haulers Ass'n v. Agricultural Commodity Serv., 86 M.C.C. 5, 24 (1961) (emphasis added).

[72] ICC v. Jamestown Farmers Union Federated Cooperative Transp. Ass'n, 57 F. Supp. 749, 753 (D. Minn. 1944), *aff'd* 151 F.2d 403 (8th Cir. 1945) (emphasis added).

[73] Machinery Haulers Ass'n v. Agricultural Commodity Serv., 86 M.C.C. 5, 25 (1961).

the exemption provision, meant it to be so strictly applied, especially when the provision relies on a definition not designed to be used for the Commission's regulatory purposes, but in determining eligibility for government loans to cooperatives.

The "necessary and incidental" test proceeds from an interpretation of the purposes of the Agricultural Marketing Act "to promote the effective merchandising of agricultural commodities . . . . by preventing inefficient and wasteful methods of distribution." [74] It recognizes that cooperatives are beneficial to the public, and that their organization and continued success should be encouraged. Since nonmember backhauling helps to accomplish this task by lowering transportation costs of cooperatives, the practice should be permitted as to cooperatives which otherwise qualify for exemption. Also, this test has built-in controls on the extent and amount of nonmember business.

The backhauls must first be "necessary" to the cooperative's business activities. The test would permit nonmember backhauling *only* when backhauling for members cannot provide a sufficient supply of revenue to keep the return capacity of vehicles profitably utilized. Nonmember backhauling, to be "necessary," must be such that the cooperative cannot provide adequate substitutes from member backhauling demands, and cannot profitably continue its operations without such backhauling activities.

The nonmember backhauls must also be "incidental" to the cooperative's primary purpose of the marketing or providing of farm products, supplies, or business services for its members. This incidental activity must always be less in amount than the cooperative's primary activity. Therefore, the safeguard required by the Agricultural Marketing Act definition [75] is imposed by the very term itself.

The rule of the "necessary and incidental" test may be defined as follows. Agricultural cooperatives may haul nonmember goods of a nonagricultural nature without losing their statutory exemption *only* if (1) these products are hauled by cooperative vehicles returning from the delivery of member products, and it appears that (2) there is not sufficient demand from member backhauls, that (3) the association cannot operate economically if its vehicles must return empty, and that (4) the total revenue from such operations does not exceed the total revenue derived from member operations. Under the existing interpretation, if these criteria are met, the cooperative remains within the scope of the exemption, and is not subject to the regulations of the Commission.

INDEPENDENT INTERPRETATION: THE FARM CREDIT ADMINISTRATION

The provisions of the Agricultural Marketing Act, including the definition which concerns this topic, are administered by the Farm Credit Administration.[76] In order to grant loans to cooperatives, the Administration must find the applicant to be a bona fide cooperative within the definition. Therefore, its interpretation of the statute is relevant to the present problem.[77]

By applicable Code of Federal Regulations provisions, section 70.3 allows the Administration to grant loans to cooperatives for nonmember business

> to enable them to handle goods, other than farm supplies, used on farms and in farm homes only when the making of such a loan is directly connected with and reasonably necessary for the performance by such an association of its primary functions [as defined by statute]. The authority for the banks for cooperatives to make such loans is contingent upon . . . reasonably convincing evidence, that the handling of such goods by a cooperative is *incidental to and necessary for the effectuation of the cooperative's principal activities* . . . .[78]

Further, by section 70.8

> [t]he term 'nonmember' as used in § 70.1 [quoting 12 U.S.C. § 1141j(a)], refers to all persons who are not members whether farmers or not . . . .[79]

If cooperatives do not lose their eligibility for loans by the Administration merely for dealing in other than farm goods within the "necessary and incidental" test of section 70.3, the Interstate Commerce Commission interpretation that nonfarm business is prohibited by the very terms of the provision in the

---

[74] 12 U.S.C. § 1141(a)(2) (1964).
[75] 12 U.S.C. § 1141j(a) (1964).
[76] Farm Credit Administration supervisory control is provided by 12 U.S.C. 1141(c) (1964).
[77] ICC v. Iowa Cooperative Ass'n, 236 F. Supp. 873, 877 (S.D. Iowa 1964).
[78] 6 C.F.R. § 70.3 (1966) (emphasis added).
[79] 6 C.F.R. § 70.8 (1966).

Agricultural Markting Act relating to member and nonmember business,[80] is without support here.

Section 70.8 also indicates that one may be a "nonmember" within this same provision[81] even when not a farmer. If one is not a farmer, he would have no appreciable need for the types of products here deemed "farm products." If a cooperative is permitted to haul products for him, presumably, then, at least some of these products would be *non*-"farm products". And a cooperative is allowed to haul such nonfarm-related products by the terms of section 70.3, within the same "necessary and incidental" test propounded by *Northwest*. Clearly, the Farm Credit Administration interprets this statute far more liberally that the Commission would apply it, and the Administration's interpretations are those of an agency whose very purpose is to identify those cooperatives falling within the statutory definitions.

"NECESSARY AND INCIDENTAL" APPLIED

The effect of the "necessary and incidental" test propounded by *Northwest* has been graphically demonstrated by the Commission. In December 1964, the Commission investigated Cache Valley Dairy Association.[82] The Commission found Cache Valley was a bona fide cooperative association but that it was backhauling nonagricultural products for nonmembers accounting for 2 percent of its total revenues. The Commission found that

> in considering the overall content of the statute, we believe that the limitation of the third part of section 1141j implies an affirmative corollary; namely, that an association's dealings with nonmembers shall be limited to farm products, farm supplies, and farm business services.[83]

It enjoined Cache Valley's nonmember backhauls, concluding

> that the transportation activities of a cooperative association partially excluded by section 203(b)(5) of the act are limited to that transportation which is designed to benefit directly or be functionally related to it's members' activities as producers of farm products and purchasers of farm supplies and/or farm business services.[84]

In 1965, the Ninth Circuit Court of Appeals reversed the district court judgment in *Northwest* and propounded the "necessary and incidental" test.[85]

In 1967, the Commission reconsidered its decision in *Cache Valley* in light of the *Northwest* ruling.[86] At the rehearing, the Commission stated that by the *Northwest* test,

> a cooperative which otherwise meets in all respects the requirements of the Marketing Act definition lawfully may transport non-farm-related traffic on a for-hire basis for nonmembers to the extent and only to the extent that such nonfarm-related transportation is shown to be, as a matter of fact, "incidental and necessary" to the effective performance of its primary farm-related functions specifically authorized by that act.[87]

The Commission found that Cache Valley was engaged in nonfarm backhauls only when it failed to have sufficient member backhaul business to fill its trucks, and nonmember backhauling accounted for only 2 percent of its total revenue. Application of the "necessary and incidental" test to these facts compelled a reversal of its previous ruling, and the exemption of Cache Valley.[88]

This ruling, however, was opposed in a vigorous dissent by Commissioner Bush, who expressed the opinion that the legislative intent of Congress had been greatly exceeded by *Northwest*.[89] In his belief, Congress would have changed the law had it desired that this result be achieved;

> [h]owever, until Congress passes legislation authorizing the transportation for nonmembers of a bona fide agricultural cooperative association—of commodities *other than* those transported by such cooperative for its members—we should continue to express our true understanding that the transporta-

---

[80] 12 U.S.C. § 1141j(a) (1964).
[81] *Id.*
[82] Cache Valley Ass'n Investigation of Operations, 96 M.C.C. 616 (1964).
[83] *Id.* at 621.
[84] *Id.* at 622.
[85] 350 F.2d 252 (9th Cir.), *rev'g* 234 F. Supp. 496 (D. Ore. 1964).
[86] Cache Valley Dairy Ass'n Investigation of Operations, 103 M.C.C. 798.
[87] *Id.* at 799.
[88] *Id.* at 804.
[89] *Id.*

tion for nonmembers, of non-farm related traffic is not exempt from regulation pursuant to the provisions of section 203(b)(5) of the Interstate Commerce Act.[90]

CONCLUSION

Cooperative associations, the Interstate Commerce Commission, and the courts have been obligated to interpret the agricultural cooperative exemption by attempting to ascertain Congressional intent with respect to the adaptation of an inherently ambiguous statute. The Commission has urged that the exemption be construed strictly in order to effectuate regulation of all but those cooperatives clearly falling within the terms of the statutory definition of a cooperative. It has seen nonmember backhauls as permissible only if "functionally related" to the main purpose of service to member farmers.

The courts infer from its conduct that Congress has tended to give cooperative associations a favored status. Courts consistently have endeavored to keep the operational impediments of cooperatives to the minimum allowable by a fair interpretation of the statutory purpose. They have held that nonmember backhauling of nonagricultural products and supplies is acceptable if such an activity is "necessary and incidental" to the main purpose of the association.

When a statute is ambiguous, it is the job of the court to interpret the statute in a manner consistent with its determination of the legislative purpose for enactment.[91] A literal interpretation should not be effectuated if legislative purpose is at variance with such a construction.[92] If the words appear unduly narrow to give the statute a realistic and intended meaning, it is the function of the courts to extend its application to broader limits than the words might literally permit.[93]

At the time the Motor Carrier Act and the Agricultural Marketing Act were enacted,[94] the present extent of transportation operations by cooperatives, and the necessity, in many instances, for them to backhaul nonagricultural products for nonmembers as a prerequisite to economical operations, was undoubtedly not anticipated. But the stipulated policy and the contemporary dialogue indicate that Congress intended to allow cooperatives a measure of latitude in conducting their affairs, all of which should ultimately benefit the public as agricultural consumers. The "necessary and incidental" test allows cooperatives to retain this favored position while remaining within the bounds of the exemption. And while these statutes could be modified to provide more exact exemption criteria, legislative unwillingness to change the provisions has made such discussion moot.

Recently decided investigations by the Interstate Commerce Commission indicate that the "necessary and incidental" test can be successfully implemented, despite the fears of that agency to the contrary. In August 1966, the Commission held that, when its exemption is challenged, an association must first bring itself within the statutory definition of a "cooperative association" and then must prove to the Commission that, as a matter of fact its nonagricultural activities are actually incidental, and actually necessary.[95] In May 1967, the Commission further narrowed the test to require that, to be "necessary and incidental," nonfarm activities could not be "a separate direct movement;" they must be conducted as a related backhaul movement resulting from the delivery of member products to market.[96] Thus, even though more liberal than the Commission

---

[90] *Id.*

[91] Day v. North Am. Rayon Corp., 140 F. Supp. 490, 493–94 (E.D. Tenn. 1956); United States v. American Trucking Ass'ns, 310 U.S. 534, 542–44 (1940); SEC v. C. M. Joiner Leasing Corp., 320 U.S. 344, 350–51 (1943); Cawley v. United States, 272 F.2d 443, 445 (2d Cir. 1959); Cabell v. Markham, 148 F.2d 737, 739 (2d Cir. 1945); Brodie v. Gardner, 258 F. Supp. 753, 758 (N.D. Ind. 1966).

[92] Ozawa v. United States, 260 178, 194 (1922), *cited in* United States v. American Trucking Ass'ns, 310 U.S. 534, 543 (1940) *and* Crosse & Blackwell Co. v. FTC, 262 F.2d 600, 606 (4th Cir. 1959). *Accord,* Wirtz v. Allen Green & Associates, 379 F.2d 198, 200 (6th Cir. 1967); United States v. Maryland *ex rel.* Meyer, 349 F.2d 693, 695 (D.C. Cir. 1965); Richmond F. & P.R.R. v. Brooks, 197 F.2d 404, 407 (D.C. Cir. 1952); Arkansas Oak Flooring Co. v. Louisiana & A. Ry., 166 F.2d 98, 101 (5th Cir. 1948).

[93] Juneau Spruce Corp. v. ILWU, 83 F. Supp. 224, 227 (D. Alas. 1949); Elizabeth Arden, Inc. v. FTC, 156 F.2d 132, 134 (2d Cir. 1946); Delany v. Moraitis, 136 F.2d 129, 131–32 (4th Cir. 1943); Day v. North Am. Rayon Corp., 140 F. Supp. 490, 494 (E.D. Tenn. 1956); Bloch v. Ewing, 105 F. Supp. 25, 28 (S.D. Cal. 1952).

[94] The Motor Carrier Act was enacted in 1935, and the Agricultural Marketing Act in 1929.

[95] Agricultural Transp. Ass'n of Tex. Investigation of Operations, No. MC C–4028, 1966 FED. CARR. REP. ¶ 36,034.

[96] Edgerton Cooperative Oil Ass'n Investigation of Operations, No. MC C–4570, 1967 FED. CARR. REP. ¶ 36,100.

desires, the "necessary and incidental" test seems closest to expressing the intent of Congress toward cooperative activities, while still providing a meaningful limitation to be applied by the Commission in assessing cooperative activities in backhaul operations.

Mr. FRIEDEL. The next witness is Mr. Harold Goolsbee, Jr., Manager of Big Sky Farmers & Ranchers Marketing Co-op.

STATEMENT OF HAROLD GOOLSBEE, JR., MANAGER, BIG SKY FARMERS & RANCHERS MARKETING CO-OP, GREAT FALLS, MONT.

Mr. GOOLSBEE. Mr. Chairman and other committee members, my name is Harold Goolsbee, Jr., and I am from Havre, Mont. I am the manager of Big Sky Farmers & Ranchers Marketing Co-op which is incorporated under the laws of the State of Montana.

You have my statement that I would like to have entered for the record.

Mr. FRIEDEL. We will place it in the record.

(Mr. Goolsbee's prepared statement follows:)

STATEMENT OF HAROLD GOOLSBEE, JR., MANAGER, BIG SKY FARMERS & RANCHERS MARKETING CO-OP., GREAT FALLS, MONT.

Mr. Chairman, my name is Harold Goolsbee, Jr., and I am from Havre, Montana. I am the manager of Big Sky Farmers and Ranchers Marketing Co-op which is incorporated under the laws of the State of Montana.

Our Co-operative is composed of farm members which have banded together to market the various farm commodities and to transport these commodities under Section 203(b)(5) of the Interstate Commerce Act.

I am here today to present our views of HR–6530 which is a companion to Senate Bill S–752. We feel that the passage of this bill in its present form will be detrimental to our members as well as the general public throughout the United States. We strongly oppose this bill in its present form as we feel that existing regulations are adequate to regulate the transportation of goods in an economical way from our members to the markets. The purpose of our co-operative for our members is to transport the goods of our members economically and, in turn, have some sound, feasible yet economical method to return our equipment back to our members so that the overall cost of transportation will not price our members out of competitive markets.

With the passage of this bill, HR–6530 and Senate Bill S–752 in the present form, it would limit our trucks to haul only 15% for non-member freight as a return haul. We would then have to dead head 85% of our trucks back to the point of origin. This is economically infeasible and would, therefore, cause the price of farm goods of our members to have an appreciable increase.

We have recently read that the regulated carriers, both truck and rail, have been granted an increase from 3% to 10% for the transportation of agricultural commodities; however, we are still using the same rates in our co-operative that have been used for the past several years due to the fact that we are able to haul non-member freight in our co-operative.

Our co-operative is also approved by the Department of Defense for the cartage and hauling of their goods from, and to, the various bases throughout the United States. With the new law in effect for a 10% sur-charge for taxes and the reported six billion dollar cut in the national spending, by not passing this bill we will still be in a position to assist the government in cutting the costs of transportation because the co-operative vehicles afford the government a substantial savings plus they are receiving through truck service that is faster than any service they used previously. If this bill is passed in its present form, we would not be able to offer these savings to the government.

In summary, we feel that the passage of this bill would work to a detriment to our members, farmers, and the general public by raising the cost of agricultural products in the markets and would cost the government untold thousands of dollars over the years to come. Such a savings to the government and public should not and cannot be overlooked.

Thank you very much.

Mr. GOOLSBEE. I would like to make a comment, that we are opposed to this bill, H.R. 6530 and companion bill S. 752. Our biggest objection is the 15 percent for nonmember freight.

Mr. FRIEDEL. Would you be satisfied with 25 percent, 20 percent?

Mr. GOOLSBEE. We would be willing to compromise on that percentage.

Mr. ADAMS. I would like to ask one question of these gentlemen who appeared in opposition. Section 22, I notice in several of your statements exempts government agencies. Then we have (b)(6) which exempts agricultural commodities, then we have (b)(5) which is the cooperative that we are operating under now.

I would like to know the opinion from counsel whether or not the exemption for the Defense Department you believe would continue under 22 or would be overridden by this legislation.

Mr. BRADY. Section 22 is written specifically for common carriers. We are not common carriers. I pointed that out in my paper that under section 22 the common carriers have filed, we file under section 203(b)(5).

Mr. ADAMS. It is the position—and I would like one of the others who are in opposition to this, if they have a different interpretation, to so state it, that this bill as an amendment to (b)(5) would prevent the carriage of government goods back as a backhaul except to the extent that they could be hauled under a 15-percent limitation.

Mr. GOOLSBEE. That is right.

Mr. ADAMS. Thank you.

Mr. FRIEDEL. Thank you, gentlemen. The meeting is adjourned.

(The following material was submitted for the record:)

STATEMENT OF E. M. NORTON, SECRETARY, NATIONAL MILK PRODUCERS FEDERATION

THE FEDERATION

The National Milk Producers Federation is a national trade association. It represents dairy farmers and the dairy cooperative associations which they own and operate and through which they act together to process and market, in their own plants on a cost basis, the milk and butterfat produced on their farms.

The Federation was organized in 1916 and has represented dairy farmers and their cooperatives in the Nation's capital for more than 50 years.

Practically every form of dairy product produced in the United States in any substantial volume is produced and marketed through dairy cooperatives represented through the Federation.

These are farmers' cooperatives, exempt under section 203(b)(5) of part II of the Interstate Commerce Act and qualified under the Agricultural Marketing Act (12 U.S.C. Sec. 1141 j).

These cooperatives are owned and controlled by the farmers they serve and they are operated for the mutual benefit of such farmers. The cooperatives themselves can take no profit; and all earnings or savings made in the marketing of milk and dairy products, including any savings made in transportation, inure to the benefit of the farmers.

Dairy cooperatives are primarily marketing associations. However, many of them operate supply divisions through which supplies are purchased on a cooperative basis for their farmers.

WHY AGRICULTURAL EXEMPTIONS?

The theory of the Interstate Commerce Act is quite opposite to that of free competition. Under the Act, rates and routes are regulated, competition is restricted, and the transportation business is channelled to selected operators with the objective of providing dependable service by a limited number of strong carriers.

In the unregulated area, rates and adequacy of service are determined by factors of vigorous competition.

It should be emphasized that the issue involved in this hearing is strictly one of competition. The exempt operators are subject to the safety regulations of the Commission. The Commission and the regulated carriers are seeking to restrict the competition provided by the exempt operators.

When the motor carrier part of the Interstate Commerce Act was passed in 1935, agricultural leaders asked that rates and routes in the agricultural field be left unregulated and subject to open competition. This Congress granted, with language broad enough to permit some incidental back-hauling of general freight on trucks used for hauling agricultural products to market, in the interest of economical use of equipment.

This program has operated effectively for more than 30 years. The great majority of truck operations are regulated to accomplish the objective of the Interstate Commerce Act. At the same time, a very small percentage of total operations have remained uncontrolled and subject to competition in the agricultural field. This has resulted in lower rates and more flexible service to farmers which is the objective Congress intended to accomplish by the exemption.

A study made by the Department of Agriculture in 1958 (Marketing Research Report No. 224), concerning the trucking of poultry, indicates that rates were approximately one-third less during a period when such trucking was unregulated as compared with a period when rates were regulated.

A similar study in 1959 (Marketing Research Report No. 316), concerning the trucking of frozen fruits and vegetables, indicates rates approximately one-fifth lower under free competition as against a regulated period.

In both cases, processors reported that service had improved during the period when the trucking was unregulated.

The National Milk Producers Federation opposed regulation of trucking in the agricultural field in 1935 when the basic law and the agricultural exemptions were first enacted. Lower costs of marketing agricultural products and greater flexibility of service were two of the points stressed in favor of exemptions for agriculture.

Thirty years of experience with part II of the Interstate Commerce Act and with the agricultural exemptions have not changed our position. During this period, we have consistently defended the exemptions against attacks upon them by the Interstate Commerce Commission and the regulated truckers. As recently as last November, our membership reaffirmed support for the agricultural exemptions.

DAIRY COOPERATIVE TRUCKS

In a study made by the Department of Agriculture in 1963 (General Report 109), dairy cooperatives accounted for about one-third of all trucks reported by marketing cooperatives. This is partly due to the local retail delivery operations of many dairy cooperatives.

About half of the dairy cooperatives operate trucks. About six percent of them had fleets of over 25 trucks. About 25 percent of the dairy cooperative trucks are rated at 2½ tons and over. Seventy-four percent of the dairy cooperatives had no over-the-road trucking operations.

A follow-up study made by the Department of Agriculture in 1964 (General Report No. 121), is not broken down into type of cooperative. However, it shows that trucks operated by farmers' cooperatives had back-hauls on about one-fifth of their trips and that about 93 percent of the back-hauls were the cooperatives' own goods. The study indicates that general freight accounted for about .9 of 1 percent of the back-haul trips.

The study also shows that farmers' cooperatives are good customers of the for-hire motor-truck and rail carriers. Nineteen large cooperatives which operate trucks spent $100 million on transportation in 1962; $86 million of this went to the for-hire carriers with about $12 million incurred for transportation in the cooperatives' own trucks.

In the case of dairy cooperatives, much of the equipment is not suitable for back-hauling general freight; and, as indicated above, much of the space available on back-haul is needed for the goods of the cooperative.

But to the extent that dairy cooperatives can back-haul general freight and thus reduce the overall cost of transporting farmers' commodities to market, we want to retain the exemption which Congress provided.

Running trucks empty on return trips would be a needless waste of resources which Congress ought not to condone or require.

.00027 OF 1 PERCENT

The volume of trucking involved in this hearing is estimated at .00027 of 1 percent of total trucking operations.

There are two fairly recent studies made by the United States Department of Agriculture which bear upon the volume of trucking operations performed by farmers' cooperatives. These are General Report 109, issued in February 1963, and General Report 121, issued in June 1964. Both are reports of actual surveys made by the Farmer Cooperative Service.

These reports have been cited by proponents of legislation attacking the agricultural exemptions to emphasize the fact that as of January 1, 1961, cooperatives were operating an estimated 33,000 motor-trucks.

Failure to regulate these trucks, proponents have argued, would impair the transportation industry of the country and cause great hardship to regulated carriers.

The reports show that in the 10-year period 1951 to 1961 the number of trucks operated by cooperatives increased about 18 percent as against an increase in total truck registrations of about 32 percent.

The relative proportion of trucks operated by cooperatives is therefore decreasing, and the relative proportion of trucking business done by cooperatives today is probably less than the proportion indicated by the surveys.

In terms of trucks registered, the surveys show that in 1960, less than .3 of 1 percent of total trucks registered were operated by cooperatives.

Truck mileage of all farmers' cooperatives in 1960 was estimated in the reports at about .5 of 1 percent of all truck mileage over rural and urban roads.

Out of the .5 of 1 percent of cooperative truck mileage, about 72 percent was local pick-up and delivery and movements from farms to local concentration points. In the case of dairy cooperatives, which account for a large proportion of total cooperative trucks, this would be hauling from farm to plant and on local home and store distribution routes. This type of operation is not involved in this proceeding.

Only about 28 percent of the cooperative trucking operations are over-the-road trucking.

Information obtained from 18 of the larger cooperatives doing over-the-road trucking shows that the cooperatives had back-hauls on about 21.8 percent of their trips. Smaller cooperatives would probably have less back-hauls, because their operations would be more irregular and back-hauls would be more difficult to arrange.

In 92.9 percent of the back-hauls, the cooperative was hauling its own goods. Goods of other cooperatives accounted for 5.9 percent of the back-hauls and exempt agricultural commodities for .3 of 1 percent. Back-hauls of the type complained about at this hearing, non-agricultural supplies hauled for non-members, accounted for only .9 of 1 percent of the back-haul trips.

Putting these figures together, we come up with the conclusion that the type of hauling done by farmers' cooperatives, about which the Interstate Commerce Commission and the regulated truckers are concerned, is approximately .00027 of 1 percent of the total trucking operations of the country.

Certainly this does not show any abuse by farmers' cooperatives of the agricultural exemption granted them by Congress.

Neither does it show any need for remedial legislation.

It has been suggested that non-member, non-agricultural back-hauls by farmers' cooperatives may increase following the decision in the Northwest Agricultural Cooperative case.

The over-the-road mileage of farmers' cooperative trucks is only about .14 of 1 percent of total truck mileage. If every outbound load were matched with an inbound load of non-member, non-agricultural freight, the business lost to regulated carriers would still be only about .07 of 1 percent of total truck mileage.

Furthermore, the U.S.D.A. surveys show that a high percentage of the back-haul trips of farmers' cooperatives are used in transporting the cooperatives' own goods and the goods of other cooperatives. These trips, of course, would not be available for other freight. Also, in many cases, the equipment is not suitable for back-hauling general freight, for example, milk tank trucks.

Although the volume of non-member, non-agricultural business handled by farmers' cooperatives is a very infinitesimal part of total trucking operations, it is important to these farmers' organizations to be free of regulation by the Interstate Commerce Commission and to be able to do the most economical job possible in transporting farmers' products to market.

All savings made by utilizing trucks of farmers' cooperatives for back-hauls are passed back to the farmers, since the cooperative operates on a cost basis without profit to itself.

Even though the pending legislation might open a relatively small hole in the dike, we fear its passage would encourage the Interstate Commerce Commission to intensify its attacks on the whole agricultural exemption.

The Commission has a long history of persistent and aggressive attacks upon farmers and their cooperatives and on the agricultural transportation exemptions granted them by Congress.

NONQUALIFIED COOPERATIVES

Practically all of the objections of the Commission and the regulated carriers have been directed against the trucking operations of organizations which they allege are not qualified cooperatives.

There is very little complaint against the back-hauls of qualified farmer cooperatives of the type which we represent. In fact, how could there be where the percentage of general freight hauled by farmers' cooperatives is so very small.

Nevertheless, the legislation sought by the Interstate Commerce Commission and the regulated truckers has attacked directly the farmers' agricultural cooperatives. Similar attacks in the past have been leveled against other parts of the agricultural exemptions.

We are concerned that the proposed legislation is merely another attempt, in a long series of attempts on the part of the Commission and the regulated truckers, to undermine the agricultural exemptions.

We hold no brief for non-qualified organizations which seek to avoid the regulation of their trucking operations by claiming the cooperative exemption.

Such organizations are not protected under either the law or the court decisions. They are subject to action by the Interstate Commerce Commission, and the Commission has successfully maintained actions against them.

The Commission has complained that when one improper operation is stopped the same men set up another organization and resume the same type of operation.

We are not aware that other agencies have encountered similar enforcement difficulties. An injunction against the officers would appear to be adequate to put an end to similar operations under another name.

In effect, the Commission has proposed that it be relieved of the burden of proving that the guilty operator is guilty by requesting, instead, that Congress limit the operations of qualified agricultural cooperatives which are performing efficient and economical transportation services for farmers.

The farmers' cooperative exemption should be left alone, and the Commission should enforce the present law against non-qualified organizations which have no valid exemption.

THE NORTHWEST CASE

At Congressional hearings on this issue, the Commission has relied heavily on the decision of the United States Court of Appeals in the Northwest Agricultural Cooperative Association case (350 F.2d 252).

That decision, the Commission told Congress, would permit a farmers' cooperative to haul non-member, non-agricultural freight in unlimited amounts so long as the total non-member business done by the cooperative did not exceed the total value of member business.

The court's opinion does not support such an interpretation of the case.

The court was quite specific, it seems to us, in limiting the volume of such freight to that which is incidental to the agricultural objectives of the cooperatives. The issue in the Northwest case was whether a farmers' cooperative hauling agricultural products to market for its members could utilize its trucks on the return trips to haul non-farm related freight. The court held that such transportation was incidental to its agricultural objectives and therefore exempt from economic regulation by the Interstate Commerce Commission.

The court said [emphasis added]:

* * * * *

"a cooperative would not be of the character contemplated by the statute if its non-farm related business exceeded that which was necessary and incidental to its farm-related business, *and in no conceivable circumstances*

could non-farm related business approach fifty percent of the total and remain incidental and necessary to that which was farm-related."

* * * * *

"The construction which we give the term does not open the door to unrestricted competition by exempt cooperatives with regulated carriers. If a cooperative engages in transportation for hire which is not incidental and necessary to the performance of an activity permitted by the Agricultural Marketing Act, it will lose its status as a 'cooperative association' and its transportation activities will be subject to economic regulation by the Commission under the Interstate Commerce Act."

* * * * *

The Commission has since reviewed its interpretation of the Northwest case in an enforcement action and has there taken quite a different view from that which it presented to Congress.

Its present interpretation of the Northwest case appears in the decision of the full Commission in the case of Cache Valley Dairy Association (No. MC–C–3876, decided May 2, 1967) as follows:

* * * * *

"The guiding principle enunciated by Northwest is plain: a cooperative which otherwise meets in all respects the requirements of the Marketing Act definition lawfully may transport non-farm related traffic on a for-hire basis for non-members to the extent and only to the extent that such non-farm-related transportation is shown to be, as a matter of fact, incidental and necessary to the effective performance of its primary farm related functions specifically authorized by that act."

* * * * *

As we have pointed out elsewhere in this statement, even if every outbound load of agriculture products were matched with an inbound load of general freight, the volume involved would be less than .07 of 1 percent of total truck mileage.

CONCLUSION

The right to back-haul general freight and thus make the most economical use of transportation equipment is important to farmers' cooperatives. All savings made in overall transportation costs through such back-hauls are passed back to the farmers and result in lower transportation costs for moving agricultural commodities to market.

The agricultural exemption is limited to qualified farmers' cooperatives. Non-qualified operators have no exemption and are subject to action by the Interstate Commerce Commission. Most of the complaints have been directed against non-qualified operators. The present law provides a remedy for controlling such operations, and it should be enforced instead of attacking the farmers' cooperatives.

The volume of non-member, non-agricultural freight hauled by farmers' co-operatives is estimated at .00027 of 1 percent of total truck mileage. This is much too small to cause any adverse effect on the nation's regulated transportation system or to justify legislation for the benefit of the regulated carriers at the expense of the American farmer.

The present system of regulating the great majority of truck transportation but leaving transportation in the agricultural field subject to the benefits of vigorous competition has worked well for 30 years, and it should be continued.

We strongly oppose legislation such as H.R. 6530 which is an unjustified attack upon farmers agricultural cooperatives by the Interstate Commerce Commission and the regulated carriers.

S. 752, as it passed the Senate, is a compromise bill and is much less objectionable. If any legislation in this area is to be reported by the Committee, it should be along the line of the Senate bill.

The volume of non-member, non-agricultural freight hauled by farmers' co-operatives, .00027 of 1 percent of total truck mileage, does not indicate any need for legislative relief of the regulated truckers at the expense of the American farmers and their agricultural cooperatives.

RAILWAY LABOR EXECUTIVES' ASSOCIATION,
Washington, D.C., July 9, 1968.

HON. SAMUEL N. FRIEDEL,
Chairman, Subcommittee on Transportation and Aeronautics,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: Your subcommittee has under consideration S. 752. The RLEA, a voluntary association of the chief executive officers of the twenty-three standard national and international railroad labor organizations wishes to express its support for S. 752 as it was passed by the Senate.

For some years, Section 203(b)(5) of the Interstate Commerce Act has been attracting, by its exemption, carriers who could be considered agricultural cooperative associations only in the most nominal of senses as well as encouraging bona fide agricultural cooperative associations to transport and on a large scale, commodities with little or no relationship to the farm or farm related commodities. The existence of this situation is, of course, in contravention of the spirit of purpose embodied in Section 203(b)(5) and against the grain of the Interstate Commerce Act.

The diversion of transportation in interstate commerce into unregulated forms certainly runs contrary to the principles of effective administration of an equitable and efficient transportation system for the country. Furthermore, the diversion of this traffic results in employment of a high ratio of non-union labor which is paid at a lower wage scale, and this constitutes a threat to the wage scale of union members in the railroad industry. Consequently, the movement to curtail non-farm related hauling of legitimate agricultural co-ops and to curtail the nominal agricultural cooperative is one which this association wholeheartedly supports. The bill that is presently before you is one which represents a good deal of consultation with the government, motor carriers, agricultural cooperatives, and rail carriers. Their consultation has in our minds resulted in legislation which achieves the need of a coherent transportation policy while doing as little damage as possible to the legitimate interests of the agricultural cooperative associations. For these reasons, we would encourage your committee's favorable disposition toward the bill as passed by the Senate.

Yours very truly,

DONALD S. BEATTIE,
Executive Secretary.

NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS,
Washington, D.C., December 11, 1967.

HON. HARLEY O. STAGGERS,
Chairman, House Committee on Interstate and Foreign Commerce,
Rayburn House Office Building, Washington, D.C.

DEAR CHAIRMAN STAGGERS: On November 2, 1967, this Association, in meeting assembled in Hollywood, Florida, adopted a resolution Supporting S. 752—90th Congress, sponsored by the Honorable Walter R. McDonald, Commissioner of the Georgia Public Service Commission, Atlanta, Georgia.

Pursuant to the directive contained in the resolution, a copy of this resolution is attached for your information and consideration.

Very truly yours,

EVERETTE KREEGER, *Secretary.*

RESOLUTION SUPPORTING S. 752—90TH CONGRESS

Whereas, The National Association of Regulatory Utility Commissioners (NARUC) is an organization whose membership consists of the public utility regulatory commissions of each of the states of the United States; and

Whereas, Regulation of both motor carriers and railroads in the public interest is an important function of the member commissions; and

Whereas, The economic well being of the motor carrier and railroad industries is a vital factor to the economy of the member states and the nation and to the nation's defense; and

Whereas, Many of the member commissions of the NARUC have for a number of years been actively engaged in the enforcement of their motor carrier laws, rules and regulations to the end that illegal transportation be curtailed; and

Whereas, The National Association of Regulatory Utility Commissioners has

frequently supported the enactment by the Congress of legislation to remedy the major problem of illegal transportation, the most recent such action being its support of P.L. 89–170; and

Whereas, Since the decision of the United States Court of Appeals for the Ninth Circuit in Northwest Agricultural Cooperative Association vs. Interstate Commerce Commission, 350 F. 2d 252, numerous agricultural cooperatives and psuedo agricultural cooperatives have and are engaging in the transportation for compensation for non-members of any commodity at any rate, to, from or between any point subject only to the restriction that they do not exceed the non-member limitation provided in the Agricultural Act; and

Whereas, It is the opinion of the NARUC that such transportation is not only contrary to the intent of the Congress when it enacted the agricultural cooperative exemption (Sec. 203(b)(5) of the Interstate Commerce Act) but it also provides a further breeding ground for illegal operators making the state enforcement task much more difficult; and

Whereas, Such transportation is clearly detrimental to the economy of the motor carrier and the railroads; and

Whereas, the Interstate Commerce Commission has recognized the problem and repeatedly has recommended remedial legislation to the Congress; therefore be it

Resolved, That the NARUC recommends and strongly urges that the Congress of the United States at the earliest possible date enact S. 752 or appropriate corrective legislation to the end that the transportation activities of the agricultural cooperatives be limited to the movement of farm related items and that such cooperatives not be permitted to engage in the general transportation business;

Resolved Further, Copies of this resolution be transmitted to the Chairman of the appropriate Senate and House Committees of the United States Congress, the Chairman of the Interstate Commerce Commission and the Secretary of the Department of Transportation.

Sponsored by the Honorable Walter R. McDonald of Georgia.

Certified a true copy of a Resolution duly adopted by the National Association of Regulatory Utility Commissioners in Convention at Hollywood, Florida, on November 2, 1967.

EVERETTE KREEGER, *Secretary, NARUC.*

NORTHWEST AGRICULTURAL CO-OPERATIVE ASSOCIATION,
Ontario, Oreg., July 5, 1968.

Subject: House Counterpart of S. 752

Hon. HARLEY O. STAGGERS,
House of Representatives,
Washington, D.C.

DEAR MR. STAGGERS: The following is the text of a letter I have sent to members of the House Committee on Interstate and Foreign Commerce regarding the amendment of Section 203(b)(5) of the Interstate Commerce Act. This proposed amendment greatly affects the ability of farmers located in sparsely settled areas to market their products. Please give the House Bill your careful consideration and vote no.

"S–752 constitutes a legislative preference for the regulated transportation industry over agriculture. This proposed amendment of a statute that has been in effect for more than 30 years is not required by any changed circumstances. In fact, the need for implementation of the provisions of the Agricultural Marketing Act for an efficient and economic distribution of farm products is greater now than it was in 1935 when Congress sought to fulfill those provisions with the passage of the agricultural cooperative exemption in Section 203(b)(5) of the Interstate Commerce Act.

"For more than 30 years agricultural cooperatives have been exempt from economic regulation by the Interstate Commerce Commission. The boundaries of that exemption lie in the requirement that the cooperative must be a legitimate cooperative engaged exclusively in providing its farmer members with an efficient and economic transportation service. In the course of performance of this service, the coperative may handle that nonmember business which is reasonable and necessary to the maintenance of its primary function. Cooperatives have always been subject to the hours, safety and other regulations of the Interstate Com-

merce Commission. We do not object to this and, indeed, consider such regulation desirable. We do, however, object to any change in the present practice which will place in the jurisdiction of the Interstate Commerce Commission the transportation future of farmers. Such action will add to the already difficult problem of transportation and marketing of farm products. Regulated transportation has done little to provide service to farmers in out-of-the-way and sparsely settled rural areas, and it has done nothing to furnish transportation of agricultral products from the farm to warehousing or storing areas. Yet, that industry has mounted a terrifying legislative campaign to restrict the farmer from serving himself through organization.

"This legislation is not necessary. In the report of Senator Lausche from the Senate Committee on Commerce, he recommends that S. 752 pass because:

"1. It is in conformance with, and implements, the National Transportation Policy, and

"2. Farmer cooperative transportation could undermine regulated transportation and has contributed to a decline of the common carrier system.

"Both these statements are false.

"There is no statistical evidence in the Record of Hearings before the Subcommittee on Service Transportation of the Commerce Committee, July 24, 25 and 26, 1967, to justify them. With the exception of opinion testimony by lobbyists for the transportation industry, all evidence is to the contrary.

"The Office of the Secretary of Transportation, charged with the responsibility of implementing the National Transportation Policy, recommended against amendment of 203(b)(5) and, in a letter to the Chairman of the Senate Committee on Commerce dated July 24, 1967, stated in part:

" 'The present exemption has permitted the agricultural cooperatives to conduct efficient and economic operations by allowing a limited amount of for-hire truck transportation.

* * * * * * *

" 'In sum, the Department is of the opinion that the present exemption is consistent with Congressional intent and that it has not been abused in any sense to the significant detriment of regulated carriers.

* * * * * * *

" 'Section 203(b)(5) is a carefully drawn statute which properly recognizes that the needs of agriculture and those of the regulated for-hire industry must be carefully balanced if the public interest is to prevail.'

"The representative of the United States Department of Agricultural who testified before the Senate committee in opposition to S-752 described a survey made by the Department clearly showing that growth in national trucking greatly exceeded cooperative trucking and pointed out that for the year 1966 cooperative trucking miles constituted less than one half of one percent of the estimated United States truck miles.

"The American Trucking Association annual report for 1966 reported that tonnage for that year was up 7 percent over 1965 and up 17.1 percent over 1964. Furthermore, the industry reported tonnage increases in nine of the major commodity classes—including agricultural commodities.

"Clearly, cooperative transportation is not a threat to the regulated industry.

"S-752 is a result of a massive lobbying campaign by regulated carriers—a campaign that cannot be matched by farmers or their organizations; a campaign that has been successful in spite of the opposition of the governmental agencies charged with the balancing of the various interests involved, and with the expertise to do so—agencies such as the Department of Agriculture, the Department of Transportation and the Department of Defense.

"That campaign was successful in the Senate in spite of the overwhelming factual evidence that change in the present law is not necessary. I urge that you give this bill your careful consideration and that the interests of the farmers as articulated in the Agricultural Marketing Act are not sacrificed merely to eliminate this insubstantial competition to the American Trucking Association and to allow it to gain control over the distribution of agricultural products."

Very truly yours,

EVAN P. GHEEN, *President.*

STANLEY, SCHROEDER, WEEKS, THOMAS & LYSAUGHT,
Kansas City, Kans., July 6, 1968.

Re Senate Bill 752.
Hon. HARLEY O. STAGGERS,
Chairman, House Interstate and Foreign Commerce Committee,
Rayburn House Office Building, Washington, D.C.

DEAR CONGRESSMAN STAGGERS: As a result of the hearing before the House subcommittee, you should surely realize that the co-operatives opposed to the above mentioned legislation are few and far between. Without exception none of the co-operatives were aware of the pending legislation when the Senate subcommittee held its hearings nearly a year ago nor were any of their views incorporated in the pending Bill. As a consequence, the attitude of those few co-operatives, which have taken advantage of the exemption of 49 U.S.C. 303 (b) (5), was not heard or determined by the Senate subcommittee. Nor did these cooperatives have adequate time to prepare for the July 1 hearing of Mr. Friedel's subcommittee, since we received notice of it only on June 28, and only then because of your good offices. The record will show that there are approximately 6 or 7 bona fide agricultural co-ops subjected to the provisions of the above legislation and that, in each instance, the legislation is so unduly restrictive as to amount to a termination of the services of the co-op. The Department of Agriculture originally opposed the pending legislation on the basis that restricting the income of farm cooperatives would be in opposition to the national policy in view of falling farm prices and income. As we have been able to determine, the Department of Agriculture has approved the pending legislation only on a "last resort" basis as a possible compromise with the American Trucking Association.

Under the circumstances and by reason of the tremendous time problem involved in connection with the pending legislation, we attach herewith two separate proposals which we submit, respectfully, should be incorporated in amendment of the pending legislation so as to comport with the present congressional intent and to support present farm prices and farm income.

Attached Proposal No. 1 preserves substantially the language of Senate Bill 752 as passed. Subparagraph (i) of the proposal, however, spells out definite standards for qualifications of co-operative associations in accordance with the Agricultural Marketing Act. This, we feel, would provide the Commission with a simple and straightforward means of determining the qualifications of co-ops engaged in a transportation business. It is our feeling that there are two types of co-operatives: those which are qualified as *agricultural* co-ops—i.e., dealing in, processing, etc. of farm products, goods, supplies and so forth—under the Marketing Act; and second, those co-operatives which are engaged in selling goods or services which are essentially not farm-related. Examples of the latter would include those co-ops who sell insurance, gasoline and oil, auto parts, batteries, etc. We feel that the former type of co-operative was the only type included to be benefited by Section 203(b) (5), and that other co-ops could not qualify for the exemption. We certainly have no ax to grind with the other co-operatives, but if the matter is considered closely, they have never been entitled to the exemption.

"The second through the fifth paragraphs embody, with only minor changes, the terms of the Senate Bill. The balance of this proposal is an authorization for "grandfather rights" in essentially the same language as that found in Section 206(a) of the Interstate Commerce Act, subject to proof of the co-op's qualifications in subparagraph (i). Grandfather rights were accorded the transportation industry upon passage of the Motor Carrier Act of 1935 and in the subsequent legislation in 1958. According to the hearings before the committees involved, Grandfather Rights would, in accordance with the attached Proposal No. 1, be accorded very few co-operatives who could qualify under the Agricultural Marketing Act. The final proviso in this proposal would eliminate a co-op's carriage of explosives or combustibles falling within the scope of the Explosives and Combustibles Act, 18 U.S.C. § 831 et seq. This should satisfy the most important interests of the regulated industry by forcing any co-ops intending to transport munitions or explosives to obtain Commission authority to do so and to prove public convenience and necessity in so doing.

Proposal No. 2, attached herewith, would permit the present cooperatives to exist with their relative transportation divisions, but would basically be uneconomical and wasteful from the standpoint of the Nation's transportation problems by requiring the co-operative truck to return empty in a substantial proportion of its trips.

For these reasons, we seriously urge the amendment to Senate Bill 752 incorporated by Proposal No. 1 herein or, as a last resort, the amendment to such Bill as incorporated by Proposal No. 2, herein, in the event you cannot personally oppose the pending legislation.

Very truly yours,

ROBERT H. BINGHAM,
General Counsel for Milk Producers Marketing Company,
A Co-operative Corporation.

PROPOSAL NO. 1

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

That at the end of section 203 (b) (5) of the Interstate Commerce Act delete the semicolon and add the following language: ", subject to the following conditions and limitations:

(i) That such cooperative association or federation shall have been determined to be qualified under the said Agricultural Marketing Act by the Farm Credit Administration, or by such other office, bureau, service, division, commission or board in the Executive branch to which authority to make such determination may have been transferred or retransferred by the President;

(ii) That any such cooperative association or federation which performs interstate transportation for nonmembers who are neither farmers, cooperative associations or federations thereof, except transportation otherwise exempt under this part, shall notify the Commission of its intent to perform such transportation prior to the commencement thereof;

(iii) That any interstate transportation performed by such a cooperative association or federation of cooperative associations for nonmembers who are neither farmers, cooperative associations, nor federations thereof for compensation, except transportation otherwise exempt under this part, shall be limited to that which is incidental to its primary transportation operation and necessary for its effective performance and shall in no event exceed 15 per centum of its total interstate transportation services in any fiscal year, measured in terms of tonnage;

(iv) That, for the purposes hereof, notwithstanding any other provision of law, transportation performed for or on behalf of the United States or any agency or instrumentality thereof shall be deemed to be transportation performed for a nonmember;

(v) That in no event shall any such cooperative association or federation which is required hereunder to give notice to the Commission transport interstate for compensation in any fiscal year of such association or federation a quantity of property for nonmembers which, measured in terms of tonnage, exceeds the total quantity of property transported interstate for itself and its members in such fiscal year;

Provided, however, That, subject to Section 210, if any such cooperative association, federation or predecessor in interest was so qualified and in bona fide operation as a common carrier by motor vehicle on _____ over the route or routes or within the territory for which application is made and has so operated since that time, or if engaged in furnishing seasonal service only, was in bona fide operation on _____ during the season ordinarily covered by its operation, except in either instance as to interruptions of service over which the applicant or its predecessor in interest had no control, the Commission shall issue such certificate without requiring further proof that public convenience and necessity will be served by such operation, and without further proceedings, if application for such certificate is made to the Commission as provided in section 206(b) of this part and within one hundred twenty days after this Act shall take effect. The application for such certificate shall be decided in accordance with the procedure provided for in section 207(a) of this part and such certificate shall be issued or denied accordingly. Pending the determination of any such application the continuance of such operation shall be lawful: *Provided further,* That this paragraph shall not be so construed as to require any such carrier lawfully engaged in operation solely within any State to obtain from the Commission a certificate authorizing the transportation by such carrier of passengers or property in interstate or foreign commerce between places within such state if there be a board in such state having authority to grant or approve such certificates and if such carrier has obtained such certificate from such board.

Such transportation shall, however, be otherwise subject to the jurisdiction of the Commission under this chapter; *And provided further*, That in no event shall any provision of this section be construed to permit the transportation of any commodity regulated under the Explosives and Combustibles Act, as codified June 25, 1948, as amended, [18 U.S.C. § 831, *et seq.*] by any such cooperative association or federation, unless there is in force and effect with respect to such cooperative association or federation a certificate of public convenience and necessity issued by the Commission authorizing the carriage of such commodities, and no such certificate shall be issued to such cooperative association or federation except in accordance with the procedure provided for in section 207(a), and then only to the extent that such service is or will be required by the present or future public convenience and necessity, as shall have been proved by reliable, probative, and substantial evidence."

PROPOSAL No. 2

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

That at the end of section 203(b)(5) of the Interstate Commerce Act delete the semicolon and add the following language: ", subject to the following conditions and limitations:

(i) That such cooperative association or federation shall have been determined to be qualified under the said Agricultural Marketing Act by the Farm Credit Administration, or by such other office, bureau, service, division, commission or board in the Executive branch to which authority to make such determination may have been transferred or retransferred by the President;

(ii) That any such cooperative association or federation which performs interstate transportation for nonmembers who are neither farmers, cooperative associations or federations thereof, except transportation otherwise exempt under this part, shall notify the Commission of its intent to perform such transportation prior to the commencement thereof;

(iii) That no transportation service rendered for any nonmembers who are neither farmers, cooperative associations or federations thereof, shall exceed 35 per centum of the total gross dollar revenues of any such cooperative association or federation from all operations during any fiscal year;

(iv) That any transportation service rendered by such cooperative association or federation for nonmembers who are neither farmers, cooperative associations or federations thereof, shall be restricted to agricultural commodities, processed or unprocessed, whether or not otherwise exempt under this section, and to those commodities reasonably related to the production, processing, distribution and marketing of agricultural products, or which would otherwise promote, foster or develop the activities contemplated by the said Agricultural Marketing Act, *Provided, however*, that in no event shall any cooperative association or federation transport any commodity subject to the provisions of the Explosives and Combustibles Act, codified June 25, 1948, as amended [18 U.S.C. § 831, *et seq.*]."

(Whereupon, at 3:10 p.m., the hearing was adjourned.)

○

13