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JAY E. SILBERG, P.C.

May 5, 1986

Mr. Harold R. Denton, Director
Office of Nuclear Reactor Regulation
U. S. Nuclear Regulatory Commission
Washington, D. C. 20555

Re: Cleveland Electric Illuminating Company
(Perry Nuclear Power Plant, Units 1 and 2)
Docket Nos. 50-440 and 50-441

Duquesne Light Company
(Beaver Valley Power Station, Unit 2)
Docket No. 50-412

Toledo Edison Company
(Davis-Besse Nuclear Power Plant)
Docket No. 50-346

Dear Mr. Denton:

My letters of August 14, 1985, November 13, 1985, January 8, 1986, January 31, 1986 and February 13, 1986 transmitted documents that had been filed with the Securities and Exchange Commission in connection with the proposed affiliation between The Cleveland Electric Illuminating Company (CEI) and The Toledo Edison Company (TE). By order dated April 29, 1986, the Securities and Exchange Commission approved the proposed

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transaction. A copy of the order is enclosed for your information. On April 29, 1986 the affiliation became effective. As of that date, CEI and TE became wholly owned subsidiaries of Centerior Energy Corporation. CEI and TE continue as electric utility companies and as NRC operating licensees and construction permittees.

Very truly yours,

Jay E. Silberg

Jay E. Silberg
Counsel for The Cleveland Electric
Illuminating Company,
Duquesne Light Company, and
The Toledo Edison Company

JES:L

SECURITIES AND EXCHANGE COMMISSION

(Release No. 35-24073 ; 70-7149)

Centerior Energy Corporation (formerly North Holding Company)

Order Denying Request for Hearing and Approving Proposed Acquisition of the Cleveland Electric Illuminating Company and the Toledo Edison Company.

April 29, 1986

On August 23, 1985, a notice was issued (HCAR No. 23806) of the filing of an application pursuant to Sections 9(a)(2) and 10 of the Public Utility Holding Company Act of 1935 ("Act") seeking Commission approval of the acquisition by North Holding Company (since renamed Centerior Energy Corporation) of all of the outstanding common stock of the Cleveland Electric Illuminating Company and the Toledo Edison Company by means of the transaction proposed in the application (and the six amendments thereto, the last of which was filed on February 26, 1986), which is summarized below.

I. BACKGROUND

The Cleveland Electric Illuminating Company ("CEI") is a publicly-held Ohio electric utility serving 644,904 residential and 69,455 commercial and industrial customers primarily in a five-county, 1700 square mile service area extending 100 miles along the south shore of Lake Erie in northeast Ohio with a total population of approximately 1,850,000. CEI reported total assets of $5.7 billion and gross revenues of $1.25 billion as of and for the fiscal year ended December 31, 1985. In addition to its conventional generating capacity, CEI owns 51.4% of the Davis-Besse nuclear plant. The Toledo Edison Company ("TE"), also a publicly-held Ohio electric utility, serves 243,912 residential and 27,811 commercial and industrial customers in a ten-county, 2500 square mile service area extending 75 miles along the south shore of Lake Erie in northwest

Ohio with a total population of approximately 750,000. TE reported total assets of $3.4 billion and gross revenues of $595 million as of and for the fiscal year ended December 31, 1985. In addition to its conventional generating capacity, TE owns 48.6% of the Davis-Besse nuclear plant. CEI also owns 31% and TE 20% of each of the two Perry nuclear plants. Perry Unit 1 is expected to be in commercial operation sometime during 1986; Perry Unit 2 is under review, and the companies do not project a start-up date. In addition, CEI owns 24.5% and TE 20% of the Beaver Valley 2 nuclear plant, scheduled to be completed by the end of 1987. The service areas of CEI and TE are not adjacent to each other; they are separated by the service area of the Ohio Edison Company ("Ohio Edison").

CEI and TE are both members of the Central Area Power Coordination Group ("CAPCO"), which was formed in 1967 by CEI, TE and three other regional electric utility companies: Duquesne Light Company, Ohio Edison, and the latter's wholly-owned subsidiary, Pennsylvania Power Company. CAPCO was established to afford greater reliability of interconnections, and lower cost of service through coordinated generating unit maintenance and generating reserve back-up among the five companies. In 1980 CAPCO discontinued joint planning for construction of future generating units.

Last June, CEI and TE entered into a definitive agreement ("Agreement") to combine the two companies as separate, wholly-owned subsidiaries of a newly-formed holding company. 1/ Shortly thereafter, CEI organized North Holding

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1/ The question of the new holding company's status under the Act is not before us at present; however, based on the facts in the application, it appears likely that the new holding company would be entitled to the exemption provided in Section 3(a)(1). According to the application, the new holding company will file a claim of exemption pursuant to Rule 2 under the Act immediately following consummation of the proposed transaction.

Company ("North"), an Ohio corporation since renamed Centerior Energy Corporation ("Centerior"), for the purpose of acquiring all the outstanding common stock of both CEI and TE.

On August 8, 1985 North filed an application requesting the Commission's approval of the proposed transaction. On August 23, 1985, the Commission issued a notice giving interested persons until September 19, 1985 to request a hearing on the application. Requests for a hearing were received from the Western Reserve Alliance ("WRA") and the Office of the Consumers' Counsel of the State of Ohio ("OCC"). 2/ Counsel for Centerior entered into discussions with WRA and OCC in an attempt to meet the concerns they raised in their hearing requests. As a result of those discussions, and in response to comments on the application given by the staff of the Commission, Centerior filed six amendments to its application between November 1, 1985, and February 26, 1986, and the OCC withdrew its request for a hearing. By a letter dated January 13, 1986, the chairman of the Ohio Public Utilities Commission ("PUCO"), Thomas V. Chema, expressed PUCO's support for Centerior's application and urged the Commission to approve the proposed transaction.

2/ Both WRA and OCC styled their filings "Motion to Intervene and Request For a Hearing". A motion to intervene filed before a hearing has been ordered by the Commission is premature. Nonetheless, because the submissions filed by WRA and OCC met the procedural and substantive requirements for hearing requests, the Commission has treated them as such.

The Commission has received a number of other letters commenting on the proposed transaction, which are included in the record of this matter and discussed at pp. 19-20 and 25-26, below.

II. CENTERIOR'S APPLICATION

Both CEI and TE are "electric utility companies" as defined in Section 2(a)(3) of the Act 3/ and thus "public utility companies" as defined in Section 2(a)(5) of the Act. 4/ Because Centerior would, in the proposed merger transaction, 5/ be acquiring more than five percent of the outstanding voting securities of each of two public utility companies, the transaction is subject to Section 9(a)(2) of the Act 6/ and thus cannot proceed without Commission appro-

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3/ Section 2(a)(3), in pertinent part, defines an "electric utility company" as "any company which owns or operates facilities used for the generation, transmission, or distribution of electric energy for sale, other than sale to tenants or employees of the company operating such facilities for their own use and not for resale."

4/ Section 2(a)(5) defines "public utility company" as "an electric utility company or a gas utility company."

5/ The proposed merger of CEI and TE is to be accomplished as follows. North organized two wholly-owned Ohio subsidiaries, East Merger Company ("East") and West Merger Company ("West"), for the purpose of merging with CEI and TE, respectively. The Agreement provides that when all documents required under Ohio law have been duly filed with the Secretary of State of Ohio (the "Effective Time") (a) East will be merged into CEI; (b) West will be merged into TE; (c) each share of common stock of CEI outstanding will be converted into the right to receive 1.11 shares of Centerior; (d) each share of common stock of TE outstanding will be converted into the right to receive one share of Centerior; and (e) all shares of Centerior owned by CEI and TE will be cancelled. As a result of the foregoing, immediately upon consummation of the transaction, the only holders of shares of common stock of Centerior would be the owners of the existing common stock of CEI and TE whose shares were converted into shares of Centerior. All other outstanding securities of CEI and TE will be unaffected. After the Effective Time holders of CEI and TE common stock will have no rights as shareholders of these companies except for dissenters' rights, and certificates representing common stock of CEI and TE as to which dissenters' rights have not been exercised will be exchangeable for certificates representing shares of Centerior.

6/ Section 9(a)(2) provides that it is unlawful for any person to acquire any security of any public utility company if that person owns, or by virtue of that transaction will come to own, five percent or more of the voting securities of that public utility company and of any other public utility company, unless the acquisition has been approved by the Commission under Section 10 of the Act.

val pursuant to Section 10 of the Act. The criteria that Section 10 requires the Commission to consider in deciding whether to approve the proposed transaction are set forth in Sections 10(b), 10(c), and 10(f).

A. Sections 10(b)(1) and 10(b)(3) - Concentration of control, capital structure complexities and other system effects

Section 10(b)(1) of the Act requires the Commission to approve a proposed acquisition unless the Commission finds that it "will tend towards ... the concentration of control of public utility companies, of a kind or to an extent detrimental to the public interest or the interest of investors or consumers." This provision is intended to prevent utility acquisitions that result in an undue concentration of economic power. It allows the Commission to exercise its best judgment as to the maximum size of a holding company in a particular area, considering the state of the art and the area or region affected. 7/ In Section 1(b)(4) of the Act, in its statement of abuses and conditions which adversely affect the public interest, Congress condemned the

> growth and extension of holding companies [that] bears no relation to economy of management and operation or the integration and coordination of related operating properties;

Hence, the Commission's determination of whether to prohibit enlargement of a system by acquisition is to be made on the basis of all the circumstances, not on the basis of size alone. Compared with the 12 registered holding company systems, which must meet the same integration and size standards, Centerior would be roughly fourth in total assets - a sizeable company, but certainly not one that would exceed the economies of scale of current electrical generation

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7/ American Electric Power, Inc. 46 S.E.C. 1299, 1309 (1978); HCAR No. 20633, July 21, 1978.

and transmission technology. There appear to be no circumstances in this proposed transaction that would call into question the concerns expressed in Section 1(b)(4).

Section 10(b)(1) also requires the Commission to consider possible anti-competitive effects of the acquisition. As discussed below (p. 22), the Commission does not find that the creation of Centerior will result in any significant diminution of competition in the market for bulk power sales.

Section 10(b)(3) of the Act requires a proposed acquisition to be approved unless the Commission finds that it would

> unduly complicate the capital structure of the holding-company system of the applicant or will be detrimental to the public interest or the interest of investors or consumers or the proper functioning of such holding-company system.

The only securities Centerior will be issuing will be common stock. Accordingly, the Commission makes no adverse findings under Section 10(b)(1) or Section 10(b)(3).

B. Section 10(b)(2) - Fairness of the Exchange

Section 10(b)(2) of the Act requires that the Commission approve Centerior's acquisition of the securities of CEI and TE unless it finds that the consideration is not reasonable in light of "the sums invested in or the earning capacity of ... the utility assets underlying the securities to be acquired". As noted earlier, 8/ when the proposed transaction is consummated, non-dissenting shareholders of TE will receive one share of Centerior common stock for each share of TE common stock they presently hold; non-dissenting shareholders of CEI will receive 1.11 shares of Centerior common stock for each share of CEI common stock they presently hold. The Commission therefore assessed the reasonableness of

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8/ See footnote 5, above, p. 4.

the consideration received by the shareholders of CEI and TE by examining the reasonableness of the different exchange ratios applicable to the securities of the two companies. Among the factors considered were the respective earnings, dividends, market values, and book values of CEI and TE. The accompanying tables compare the two companies' historical per share market value, earnings, dividends, and book value. Traditionally, the Commission's analysis has emphasized market values as a measure of "the sums invested in" and earnings as a measure of the "earning capacity" of the utility assets in question. 9/

The application states that the exchange ratio of 1.11:1 was arrived at by arm's-length negotiation between the two companies. In those negotiations CEI was advised and represented by its investment banker, Morgan Stanley & Co. Incorporated ("Morgan Stanley"); TE engaged Merrill Lynch Capital Markets ("Merrill Lynch") as its investment banker. The parties agreed on the form of the proposed affiliation between CEI and TE, a holding company above the two utilities, at an early stage of their discussions. Once that framework was established, negotiations focused on determining appropriate exchange ratios, i.e., the number of shares of Centerior common stock to be issued in exchange for each share of CEI and the number to be issued in exchange for each share of TE. The application states that the two investment banking firms performed extensive studies for their respective clients in addition to in-house studies conducted by the managements of both companies.

TE initially proposed relative unadjusted book value as the foundation for the exchange ratio; CEI proposed the relative market value of the companies'

9/ See Northeast Utilities 42 S.E.C. 963, 968-974 (1966); National Fuel Gas Company 36. S.E.C. 489, 495 (1955).

FINANCIAL COMPARISON OF CEI AND TE

	As of	CEI	TE	Ratio
MARKET VALUE per share	12/31/81	$15.83	$16.13	.98
	12/31/82	$19.75	$21.00	.94
	12/31/83	$18.63	$18.00	1.035
	12/31/84	$19.38	$18.50	1.048
	12/31/85	$25.50	$22.00	1.159
	2/28/86	$25.50	$22.63	1.127

	As of	CEI	TE	Ratio
EARNINGS per share	12/31/81	$2.52	$2.77	.91
	12/31/82	$3.01	$3.18	.95
	12/31/83	$3.28	$3.50	.94
	12/31/84	$3.64	$3.70	.98
	12/31/85	$3.53	$3.54	1.00

	As of	CEI	TE	Ratio
DIVIDENDS per share	12/31/81	$2.08	$2.30	.90
	12/31/82	$2.19	$2.38	.92
	12/31/83	$2.31	$2.46	.94
	12/31/84	$2.43	$2.52	.96
	12/31/85	$2.55	$2.01	1.27

	As of	CEI	TE	Ratio
BOOK VALUE per share	12/31/81	$19.63	$23.46	.84
	12/31/82	$19.86	$23.53	.84
	12/31/83	$20.79	$24.12	.86
	12/31/84	$21.51	$23.76	.91
	12/31/85	$22.46	$24.44	.92

common shares. According to the application, neither suggestion was mutually acceptable, and the exchange ratio of 1.11:1 finally adopted was reached through a process of extensive and vigorous arm's-length negotiation and compromise. Both investment banking firms then analyzed that exchange ratio and furnished to the Boards of Directors of CEI and TE opinions (which are set forth in the merger proxy statements filed with the Commission on Form S-4 (Registration No. 2-99531) and as exhibits to the present application) that the proposed transaction, at the agreed-upon exchange ratio, was fair to the shareholders of the two companies.

We are persuaded that the relevant financial and operating factors were analyzed by the investment banks, and that both companies pursued negotiations at arm's length and in the best interests of their respective shareholders. In addition, the Commission has independently analyzed the financial and operating performances of CEI and TE for the past five years. Clearly, there is a range of possible reasonable exchange ratios from .92:1 to 1.27:1 based on the analysis of relative market values, book values, earnings per share, and dividends per share. The Commission is satisfied that the proposed 1.11:1 exchange ratio is not unfair or unreasonable in light of the statutory criteria of Section 10(b)(2).

CEI and TE have acknowledged the possibility that they may be obliged to write off some portion of their investment in their unfinished nuclear generating plants. Therefore, it remains for us to consider whether such an eventuality might affect the fairness of the exchange ratio. As mentioned earlier, CEI and TE are partners in the Davis-Besse, Perry, and Beaver Valley nuclear power generating plants. These are the only nuclear plants in which either has any interest. It is reasonable to assume that any write-off of investment in those plants mandated by the PUCO will be proportional to their respective shares in

the nuclear plant in question. Since their shares of each of those plants are not highly disproportionate to their relative sizes, 10/ any write-off would affect each company roughly proportionately to its size. The fairness of the exchange ratio would thus not be materially affected regardless of the size of the write-off.

Section 10(b)(2) also requires the Commission to consider the reasonableness of the fees involved in a transaction. The Commission finds that the record before us does not enable it to evaluate the reasonableness of the fees payable to the investment bankers upon consummation of the proposed transaction: a total of $3,794,000 to Morgan Stanley and $3,100,000 to Merrill Lynch. The application states that these fees are based on the current market prices of the common stock of CEI and TE and includes a listing of mergers and acquisition from 1983 to the present, with publicly-disclosed fees paid in those cases. (If the proposed transaction is not consummated, Morgan Stanley and Merrill Lynch are to be compensated on a time and effort basis.) Rather than delay the merger, and thus realization of the attendant benefits for the companies' consumers and investors, the Commission reserves jurisdiction over the fees of the investment bankers and authorizes its Division of Investment Management to approve those fees by delegated authority if satisfactory justification is submitted.

C. Section 2(a)(29)(A) - Integrated Public Utility System

Section 10(c)(2) of the Act requires that an acquisition, in order to be approved by the Commission, must "serve the public interest by tending toward the economical and efficient development of an integrated public utility system." Before considering the economies and efficiencies CEI and TE assert will result from their affiliation, the Commission must determine whether the

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10/ See pp. 1-2, above.

new system, Centerior, to be formed from the combination of CEI and TE will be an "integrated public utility system," as defined in Section 2(a)(29)(A) of the Act:

> As applied to electric utility companies, a system consisting of one or more units of generating plants and/or transmission lines and/or distributing facilities, whose utility assets, whether owned by one or more electric utility companies, are physically interconnected or capable of physical interconnection and which under normal conditions may be economically operated as a single interconnected and coordinated system confined in its operations to a single area or region, in one or more states, not so large as to impair (considering the state of the art and the area or region affected) the advantages of localized management, efficient operation, and the effectiveness of regulation.

Under Section 2(a)(29)(A) the Commission must consider whether CEI and TE are "physically interconnected or capable of physical interconnection" within the meaning of that section. The service areas of CEI and TE are not contiguous. They are separated at their closest points by a distance of 50 miles across the service area of Ohio Edison. The physical interconnection requirements of the section are met if the two service areas are connected by power transmission lines that the companies have the right to use whenever needed. 11/

CEI and TE rely on a 345 kilovolt CAPCO transmission line to establish that they are "physically interconnected" within the meaning of Section 2(a)(29)(A) of the Act. CEI and TE each own the portion of that transmission line that is located in its service area. The portion of the line between their service areas is owned by Ohio Edison, another member of CAPCO. Under CAPCO's Transmission Agreement, however, investment responsibility for CAPCO transmission lines is shared by the CAPCO companies and paid for over the life

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11/ In Electric Energy, Inc. 38 S.E.C. 658 668-671 (1958), the right to use a transmission line owned by a different company (with power dispatch coordination by voice communication, rather than centralized dispatch,) was found sufficient to satisfy the standards of Section 2(a)(29)(A). See also Cities Service Power & Light Co., 14 S.E.C. 28, 53 note 44 (1943).

of the lines as if the companies owned the lines as tenants in common. The capacity of each CAPCO transmission line is available for the use of individual member companies so long as their use does not materially interfere with the purposes of the Transmission Agreement, i.e., to facilitate intra-CAPCO power sales and coordination. The CAPCO agreements have no termination date and remain in effect as long as CAPCO facilities are in existence.

According to the application, technical studies indicate that even a worst-case power transfer scenario (all power needs of TE being supplied from the CEI system, an extreme emergency condition) would not result in material interference with Ohio Edison's use of the transmission line; no loading problems would exist, and there would remain a significant margin between the line's loading level and its rating. In view of these studies and the provisions of the CAPCO agreements, the Commission finds that the CEI and TE systems are "physically interconnected" within the meaning of Section 2(a)(29)(A) of the Act.

Those studies and the present voice communication coordination of power dispatch between the two utilities' control areas demonstrate that the Centerior system could under normal conditions be operated as a single interconnected and coordinated system, whose operations would be confined to the state of Ohio. Since Centerior will be headquartered in Ohio and its management drawn from the present management of CEI and TE, the advantages of localized management will not be compromised. As described below, increased efficiency can be expected to result from the affiliation. Finally, the effectiveness of regulation will not be diminished; CEI and TE will remain subject to regulation by the PUCO, which supports the affiliation, and the Ohio legislature will decide whether and to what extent the PUCO should have

jurisdiction over Centerior. 12/ The Commission thus finds that the Centerior system would be an integrated public utility system within the meaning of Section 2(a)(29)(A) of the Act.

D. Section 10(c)(2) - Economies and Efficiencies

Having concluded that the Centerior system would be an integrated one, we must determine whether the affiliation will tend toward Centerior's economical and efficient development. Traditionally, that determination has been approached by attempting to identify the opportunities for savings likely to result, and, to the extent possible, to estimate the dollar amounts of those savings. 13/ However, specific dollar forecasts of future savings are not necessarily required; a demonstrated potential for economies will suffice even when these are not precisely quantifiable. 14/

As part of the application, CEI and TE presented reports prepared by their staffs examining the anticipated benefits of the affiliation. Each study group analyzed the current operations of the two companies, determined how the affiliation could result in economies of operation, and attempted, where possible, to quantify the expected savings. The anticipated savings range from $700,000 (annually) in computer-aided drafting to $53.4 million (1986-2000) from the deferral of construction of new generating plants, joint economic coordination of power dispatch, and improved coordination of off-peak power generation. Other anticipated annual savings are inventory and material purchasing ($4.2

12/ See p. 25, below.

13/ See, generally, Eastern Gas and Fuel Associates, 43 S.E.C. 524, 527-35 (1967).

14/ In the Matter of American Electric Power, HCAR No. 20633, July 21, 1978, p. 27.

million), management information systems ($2.1 million), personnel consolidation and consolidation of similar functions in a service company ($7.2 million), marketing and industrial sales stabilization (no estimate given), improved financial stability and net savings achievable as a result of changes in credit ratings ($1.1 million), and generating capacity rationalization (no estimate possible until agreement is reached on ownership and cost of generating capacity).

The experience of the Commission in prior cases involving electric utility mergers confirms the significant savings achievable as a result of personnel, service company, and management information systems consolidations. Given the structual similarities between these two companies and other electric utility companies, our experience with previous acquisitions suggests that savings from eliminating such overlapping functions are highly probable. The record before us, including the company's projected savings, also confirms that savings are probable. Accepting the companies' estimates, the affiliation would result in savings of $9.3 million annually in these two areas alone. Assuming the savings from the other factors materialize, the merger would result in additional benefits of nearly $10 million annually; savings could thus aggregate approximately $300 million for the 15-year period ending in the year 2000. This compares very favorably with an initial cost of $10 million.

Even though the Commission is satisfied that Centerior satisfies the requirements of Section 2(a)(29)(A), in order to sustain movement toward achievement of anticipated economies (through, e.g., centralized dispatch of power as opposed to the present joint economic dispatch via voice communication) Centerior, CEI, and TE have agreed to enter into and file with the Commission, within one year after the effective date of this order, an Operating Agreement

describing the manner in which they will effect the further economic and efficient development of the integrated public utility system as described in the application.

E. Section 10(f) - Applicable State Law

Section 10(f) of the Act prohibits Commission approval of any acquisition under Section 10 unless it appears to the Commission's satisfaction that applicable state laws have been complied with (unless the Commission finds that such state laws would be detrimental to the carrying out of the provisions of Section 11). The corporations involved in this transaction are organized and operate exclusively in Ohio. The application states that no state regulatory authority has jurisdiction over the proposed transaction, but that the PUCO has been advised of the proposed transaction, and would be provided with a copy of the Form S-4 filed with the Commission. As noted above, the chairman of the PUCO has expressed the PUCO's support for Centerior's application and urged the Commission to approve the proposed transaction. The Agreement provides that as a condition to the obligation of both CEI and TE to consummate the proposed transaction each shall have received from counsel for the other company and from counsel for Centerior opinions dated the date of the closing to the effect that all regulatory approvals required for the consummation have been obtained and remain in full force and effect. Based on the foregoing, it appears to the Commission's satisfaction that applicable state laws have been complied with.

F. Conditions in the application

Besides filing with the Commission the Operating Agreement referred to earlier, Centerior has agreed to:

1. File with the Commission, prior to March 1 of each year, (a) consolidating financial statements including a balance sheet, statement of income and retained earnings, and statement of changes in financial position for the prior year; and (b) financial statements of Centerior's service company using the same form required to be used by service companies of holding companies registered under the Act; and (c) until March 1, 1991, an annual update of the activities undertaken during the prior year to increase the integration, coordination, interconnection, and communication of the CEI and TE electrical facilities.

2. Following consummation of the proposed transaction, to utilize the chart of accounts authorized by the Federal Energy Regulatory Commission as set forth in 18 CFR §101.

3. Following consummation of the proposed transaction, to use the "work order system" of accounting for all services Centerior's service company will provide to CEI and TE.

As noted above, 15/ the OCC agreed, after negotiations with counsel for Centerior, to withdraw its request for a hearing. As part of that agreement, Centerior amended its application to include the following terms and conditions and requested that they be reflected in any order the Commission issued approving

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15/ P. 3.

the proposed transaction. OCC informed the Commission that it had no objection to the approval of Centerior's application if the following paragraphs were included as conditions of any Commission order approving the proposed transaction:

1. Centerior will provide to the Public Utilities Commission of Ohio ("PUCO") and to the OCC its initial, and thereafter its annual exemption statement submitted on Form U-3A-2 and filed pursuant to Rule 2 under the Act (17 CFR 250.2), and all other documents filed with the Commission pursuant to the Act and rules promulgated thereunder. In the event that Centerior should ever request exempt status by order under Section 3(a)(1) of the Act and as a result is no longer required to make a Form U-3A-2 filing, it will prepare and submit annually to the PUCO and the OCC an annual statement containing the same information which is required to be contained in the Form U-3A-2.

2. Neither Centerior, CEI, TE nor any other company directly or indirectly controlled by Centerior will object in the context of a proceeding before the PUCO to a request for discovery of books, records, or other documents in the possession of Centerior or any of its subsidiaries on the grounds that the particular person or entity having possession of the same is not subject to the PUCO's jurisdiction.

3. Centerior, CEI and TE agree that following consummation of the affiliation, Centerior will not permit a minority common stock ownership interest to be held in either CEI or TE.

4. CEI and TE agree that neither shall invest in, lend funds to, guarantee the obligations of or otherwise finance any entity in the Centerior

system before January 1, 1987 unless they have received authorization from the PUCO to do so. After January 1, 1987 such authorization shall not be required if the PUCO disclaims jurisdiction over the transaction presented for approval. It is understood that this limitation does not apply to transactions in the ordinary course of the companies' business operations in which CEI or TE acts on behalf of, or with respect to, the other.

5. Centerior will provide to the PUCO and to the OCC, on an annual basis, financial statements of its service company using the same form that the Commission currently requires or in the future may require to be filed by registered holding company systems pursuant to the Act.

6. Centerior, TE and CEI shall, for a period of five years commencing with the issuance of this order, individually or jointly sponsor testimony in all TE and CEI base rate and annual electric fuel component proceedings before the PUCO setting forth information regarding the implementation of the reorganization and the benefits and costs derived as a result of their affiliation; however, neither Centerior, CEI nor TE shall be required to do so more than once in any calendar year.

7. Centerior agrees to notify the OCC of any change to the service company agreement at least sixty days prior to its implementation, to enter into good faith discussions with the OCC regarding any objections it may have to any such change, and to recognize the right of the PUCO to examine any such change in the course of base rate case or annual electric fuel component proceedings to the extent it affects charges being made by the service company to CEI or TE.

8. CEI and TE shall not transfer any assets to any affiliate within the Centerior system, other than another public utility within the Centerior system, prior to January 1, 1987, unless they have received authorization from the PUCO to do so. After January 1, 1987 such authorization shall not be required if the PUCO disclaims jurisdiction over the transaction presented for approval. In presenting such proposed transfers to the PUCO for approval, CEI and TE agree to request that the PUCO delay final action for at least forty-five days after filing of the application in order to afford interested persons the opportunity to submit objections and request a public hearing.

III. THE HEARING REQUESTS

On September 18, 1985, WRA filed a request for a hearing on Centerior's application. WRA identified itself as a tax-exempt "non-profit consumer utility corporation ... engaged in the education of people and organizations regarding energy issues" that "has been an intervenor in numerous cases against utility companies since its inception, including CEI." As noted earlier, the OCC also filed a hearing request, which has since been withdrawn.

A number of other organizations and individuals also wrote to the Commission regarding Centerior's application. Between January 22 and April 1, 1986, the Commission received twenty-three letters from individuals and organizations in the Cleveland area urging that a hearing be held on Centerior's application. None of those letters complied with the procedural requirements for requesting a hearing set forth in the notice of the filing of the application published in the Federal Register, and none was filed within the time period set forth in that notice. Moreover, most of those letters raised no issues of fact or

law, and none raised any issue not raised by WRA.

A. WRA's Hearing Request

WRA's hearing request and three subsequent "amplifications" raised various contentions, which are summarized below.

In analyzing a request for a hearing, the Commission applies the criteria of Rule 23(d) 16/ by determining whether the request raises a significant issue of fact or law that is relevant to the issues the Act requires the Commission to consider in deciding whether to grant the application. A simple assertion that a particular standard of the Act has not been met does not alone suffice to raise a significant issue of fact or law.

The Commission has reviewed all of the issues presented in WRA's hearing request, and finds that a hearing on the application is not warranted. The Commission notes the following in response to WRA's hearing request: 17/

The utilities' nuclear plants - WRA asserts that CEI and TE have mismanaged the construction of their nuclear power plants, that the Perry plants are "riddled with the influence of organized crime" (Hearing request, pp. 1, 3-4; Amplification No. 1, p.14), and that the utilities' primary motive in setting up a holding company is to "cover up the problems at their nuclear plants" (Hearing request, p.3).

16/ 17 C.F.R. §250.23(d):

> If the Commission deems that a hearing is appropriate in the public interest or the interest of investors or consumers, it will issue an order thereon, and in that event a declaration or application shall not become effective except pursuant to further Commission action.

17/ As indicated, the Commission has considered all of the issues presented, and others. To the extent it does not discuss them here, it has considered them and concluded that they do not warrant a hearing.

The Commission has considered these allegations and has determined that they do not implicate any policies underlying the Act, and thus do not require the Commission to reach a different result in this case.

Diversification by exempt holding companies into non-utility business - WRA contends that one of the main motives for the proposed transaction is to create an exempt holding company that would enable the utilities to diversify into non-utility businesses so that they "can gain greater political and social power by controlling and influencing local businesses" (Amplification No. 2, p. 6). According to WRA, the Act was meant to restrict diversification by exempt holding companies into non-utility operations in the same manner as diversification by registered holding companies (Amplification No. 2, pp. 5-7), that the Commission's decision to the contrary in Pacific Lighting Corp. 45 S.E.C 152 (1973) was in error (Amplification No. 2, p.6).

WRA's unsupported allegation regarding the companies' motives has no bearing on the subject matter of the application. In addition, the Commission, in its decision in Pacific Lighting Corp., held that exempt holding companies are not subject to the diversification restrictions that Section 11 of the Act imposes on registered holding companies.

Commission approval of securities issuances - WRA raises a question regarding the application of Section 7(f) of the Act, which deals with declarations by registered holding and subsidiary companies regarding securities transactions, to the proposed transaction (Amplification No. 2, p. 7).

Commission approval of the issuance of shares of Centerior's stock is not required under Sections 6 and 7 of the Act, which deal with issuance of securities by registered holding companies, because Centerior is not, and will not by

virtue of the proposed transaction become, a registered holding company.

Anti-competitive effects - WRA asserts that the formation of Centerior will result in anti-competitive behavior by CEI and TE to the detriment of Ohio's municipal electric utilities (Amplification No. 2, p. 7).

The Commission does not find that Centerior's creation will disadvantage the municipal electric utilities. The proximity of several other sizeable electric utilities able to supply power, Ohio Power and Ohio Edison, with combined assets of $10.9 billion serving approximately 1.6 million customers, should prevent any significant diminution of competition in the market for bulk power sales to municipal electric utilities. We are unable to conclude on the basis of the information presented by WRA that a hearing on this issue is warranted. WRA sets forth no facts regarding anti-competitive concerns as a result of the merger, including possible economic barriers to entry by potential competitors to Centerior, percentage of the wholesale market share to be controlled by Centerior versus existing competitors, and lack of access to power at reasonable terms by wholesale customers of Centerior. Moreover, American Municipal Power-Ohio, Inc. ("AMP-Ohio"), a non-profit corporation created by Ohio's municipal electric utilities, which initially expressed some concerns in this regard, has notified the Commission that discussions with CEI and TE have alleviated those concerns, and that it does not oppose approval of the application.

Basis for the issuance of Centerior's securities - WRA contends that the proposed transaction would involve "the issuance of securities on fictitious or unsound asset values" within the meanings of Section 1(b)(1) of the Act because the utilities' nuclear plants are valueless (Amplification No. 1, pp. 12-13, 15; Amplification No. 2, pp. 2, 8, 9).

In condemning "the issuance of securities on fictitious or unsound asset values," Congress was concerned with the practice of "write-ups": artificially inflating asset values by means of intercorporate transfers among related entities to provide a basis for raising additional capital from public investors. 18/ That abuse was facilitated by the lack at that time of audited financial statements. That situation is not presented here. CEI and TE are not proposing to sell securities to the public based on inflated asset values. The asset values of those two companies are carefully examined in the context of state rate proceedings. The PUCO has not brought to our attention any fictitious or unsound assets held by CEI or TE. Further, the chairman of the PUCO has expressed strong support for the proposed transaction.

Section 2(a)(29)(A): Physically interconnected or capable of physical interconnection - WRA questions whether the Centerior system would meet the criteria set forth in Section 2(a)(29)(A) of the Act (Amplification No. 1, pp. 16-17) on the ground that the system does not own the CAPCO 345 kV line.

As set forth above (pp. 10-13), the Commission has concluded that the Centerior system will meet the standards of Section 2(a)(29)(A).

Fees to be paid to the investment bankers - WRA asserts that the fees of the investment bankers in the proposed transaction are excessive (Amplification No. 3, pp. 2-3).

The record before us does not permit us to evaluate the proposed fees fully and the Commission therefore reserves jurisdiction over them. There is, however, no reason at this time to order a hearing on the matter.

18/ See Section 1(b) of the Act.

Ohio law - WRA asserts that the proposed transaction would result in Ohio consumers being charged for unneeded and non-functioning nuclear power plants, which, it alleges, would violate Ohio law (Amplification No. 2, pp. 18-19).

Nowhere in its submissions does WRA cite any Ohio law that it alleges would be violated by the proposed transaction. As noted above (p. 15), the application, part of the record before us, states that no state regulatory authority has jurisdiction over the proposed transaction, opinions of counsel to that effect are preconditions to consummation, and the PUCO has urged the Commission to approve the proposed transaction. Nor did the OCC's hearing request allege, or even suggest, that the transaction was questionable under any state law. On the foregoing basis, it appears to the satisfaction of the Commission that such state laws as may apply in respect of the acquisition have been complied with.

Substitution of FERC regulation for PUCO regulation of Centerior's nuclear plants - WRA asserts that the Federal Energy Regulatory Commission ("FERC") has proved more receptive to requests for rate increases than state regulatory bodies and that the formation of a holding company would allow CEI and TE to evade PUCO regulation of their troubled nuclear plants by transferring them to a subsidiary of Centerior yet to be formed, which would then sell the generated power at wholesale to CEI and TE in transactions subject to regulation not by the PUCO but by the FERC. (Amplification No. 1, p. 23).

Were Centerior to transfer its nuclear plants into a new subsidiary, which sold power not at retail, but only to other utilities, rate setting for those wholesale power sales would be the responsibility of the FERC, rather than of the PUCO. Although the PUCO would of course retain jurisdiction over the retail rates CEI and TE charged consumers, in effect it might lose jurisdiction

over the nuclear plants since it might be obliged to accept the wholesale rates set by the FERC as part of the utilities' cost of service. Although we are sympathetic to consumers' concerns about the impact this might have on their utility rates, even if CEI and TE were planning such a course of action it would raise no questions having a direct bearing on the subject matter of the application. The Act does not confer rate-making authority on the Commission. In any event, a bill presently is pending before the Ohio legislature providing for state regulation of utility holding companies that would subject any such transfer of utility assets by CEI or TE into a subsidiary of Centerior to PUCO approval. OCC's agreement with Centerior includes a condition that prevents any such transfer until the Ohio legislature has had the opportunity to complete action on this legislation. In addition, the chairman of the PUCO has written to the Commission to express PUCO's support for the application. The Commission believes that in a matter such as this it is appropriate to give considerable weight to the opinion of the regulatory body most familiar with the interests of Centerior's consumers and to the decision of the Ohio legislature.

B. Other Submissions

On July 31, 1985, AMP-Ohio wrote to the Commission's Office of Public Utility Regulation to express its members' concern over potential anti-competitive effects of the proposed combination of CEI and TE. Subsequently, AMP-Ohio participated in a series of meetings and discussions with CEI and TE and reached an understanding with them that alleviated its concern. On October 18, 1985, AMP-Ohio filed a Motion to Intervene stating that it did not in any way oppose or wish to delay Commission approval of the application, but wished to intervene "simply to assure that it has an opportunity to participate if the applicants, any other party, or the Commission itself requests or requires

a modification which would materially or adversely affect AMP-Ohio's interests." On September 19, 1985, the City of Toledo filed a Motion to Intervene "in order to preserve its rights to participate in any hearings that may be held . . ." but did not raise any issue or make any comments.

Neither of these submissions requested a hearing or raised any issues of fact or law. They merely asked, prematurely, for the right to participate in a hearing that had not yet been, and might never be, ordered. Because of the action we take today on the question of ordering a hearing, the Motions to Intervene filed by the City of Toledo and by AMP-Ohio are moot.

On December 2, 1985 the Commission received a letter from the Consumers League of Ohio ("League") expressing a number of concerns regarding the proposed holding company, all of which are dealt with in our discussion of WRA's hearing request, above, but making no request for a hearing. On January 13, 1986, the Commission received a letter from Mr. Joseph P. Meissner, an attorney in the Urban Development Office of the Legal Aid Society of Cleveland seeking to intervene on behalf of the League. The Office of Public Utility Regulation replied with a letter explaining, among other things, that Mr. Meissner's letter did not constitute a valid request for a hearing; it raised no issues of fact or law and did not comply with the procedural requirements.

IV. FINDINGS

On the basis of the foregoing, the Commission concludes that neither WRA nor any other person has raised any issue of fact or law that would warrant the ordering of a hearing on Centerior's application. Therefore, it finds that a hearing on the application is not appropriate in the public interest or in the interest of investors or consumers. Accordingly,

IT IS ORDERED that the request for a hearing is denied. The matters presented in the application have been considered, and it is hereby found that the applicable standards of the Act and the rules thereunder are satisfied except with respect to the fees of the investment bankers, and that no adverse findings are called for. Accordingly,

IT IS ORDERED that the proposed transaction, as set forth in the application, as amended, is hereby approved, effective forthwith, subject to the Commission's reservation of jurisdiction with respect to fees, subject to the terms and conditions of Rule 24 under the Act, and subject to the following undertakings, to which Centerior has agreed:

1. Within one year of the effective date of this order, Centerior, CEI and TE will enter into and file with this Commission an operating agreement describing the manner in which they will effect the development of an integrated public utility system as described in the application.

2. Prior to March 1 of each year, Centerior will file with the Commission (a) consolidating financial statements including a balance sheet, statement of income and retained earnings, and statement of changes in financial position for the prior year; (b) financial statements of Centerior's service company using the same form required to be used by service companies of holding companies registered under the Act; and (c) until March 1, 1991, an annual update of the activities undertaken during the prior year to increase the integration, coordination, interconnection and communication of the CEI and TE electrical facilities.

3. Following consummation of the proposed transaction, Centerior will utilize the chart of accounts authorized by the Federal Energy Regulatory Commission as set forth in 18 CFR §101.

4. Following consummation of the proposed transaction, Centerior's service company will use the "work order system" of accounting for all services it provides to CEI and TE.

5. Centerior will provide to the PUCO and to the OCC its initial, and thereafter its annual, exemption statement submitted on Form U-3A-2 and filed pursuant to 17 CFR §250.2, and all other documents filed with the Commission pursuant to the Act and the rules promulgated thereunder. In the event that Centerior should ever apply for exempt status by order pursuant to Section 3(a)(1) of the Act and as a result ceases to file Form U-3A-2 annually, it will prepare and submit annually to the PUCO and the OCC an annual statement containing the same information that is required to be submitted in Form U-3A-2.

6. Neither Centerior, CEI, TE, nor any other company directly or indirectly controlled by Centerior will object in the context of a proceeding before the PUCO to a request for the discovery of books, records, or other documents in the possession of Centerior or any of its subsidiaries on the grounds that the particular person or entity having possession of the same is not subject to the PUCO's jurisdiction.

7. Centerior, CEI and TE agree that following consummation of the affiliation Centerior will not permit a minority common stock ownership interest in either CEI or TE.

8. CEI and TE agree that neither shall invest in, lend funds to, guarantee the obligations of, or otherwise finance any entity in the Centerior system before January 1, 1987 unless they have received authorization from the PUCO to do so. After January 1, 1987, such authorization shall not be required if the PUCO disclaims jurisdiction over the transaction presented for approval. It is understood that this limitation does not apply to transactions in the ordinary course of the companies' business operations in which CEI or TE acts on behalf of, or with respect to, the other.

9. Centerior will provide to the PUCO and to the OCC, on an annual basis, financial statements of its service company using the same form that the Commission currently requires or in the future may require to be filed by registered holding company systems pursuant to the Act.

10. Centerior, CEI, and TE shall, for a period of five years commencing with the issuance of this order, individually or jointly sponsor testimony in all CEI and TE base rate and annual electric fuel component proceedings before the PUCO setting forth information regarding the implementation of the reorganization and the benefits and costs derived as a result of their affiliation; however, neither Centerior, CEI, nor TE shall be required to do so more than once in any calendar year.

11. Centerior agrees to notify the OCC of any change to the service company agreement at least sixty days prior to its implementation, to enter into good faith discussions with the OCC regarding any objections it may have to any such change, and to recognize the right of the PUCO to examine any such change in the course of base rate case or annual electric

fuel component proceedings to the extent it affects charges being made by the service company to CEI or TE.

12. CEI and TE shall not transfer any assets to any affiliate within the Centerior system other than another public utility within the Centerior system, prior to January 1, 1987, unless they have received authorization from the PUCO to do so. After January 1, 1987, such authorization shall not be required if the PUCO disclaims jurisdiction over the transaction presented for approval. In presenting such proposed transfers to the PUCO, CEI and TE agree to request that the PUCO delay final action for at least forty-five days after the filing of the application in order to afford interested persons the opportunity to submit objections and request a public hearing.

By the Commission.

John Wheeler

John Wheeler,
Secretary