mission in those instances in which he has been granted that right.

As stated above, this advisory member only has full and complete rights and privileges when matters are considered that affect the limited area specified in the Act. Thus it seems that it would be imperative for the Commission to decide when it is going to consider matters affecting those particular areas in order to determine whether or not the advisory member has and can exercise full and complete rights as a member of the Commission. Therefore, in construing the sections of this Act in conformity with the rules of construction stated above it is my opinion that both of your questions should be answered in the affirmative.

OFFICIAL OPINION NO. 55

Mr. Roscoe C. O'Byrne, Chairman,
Public Service Commission of Indiana,
State House, Room 401,
Indianapolis, Indiana.

Dear Sir:

I am in receipt of your letter of May 8, 1949, which is as follows:

"I hand you herewith copy of the letter from William E. Steckler, Public Counsellor, bearing date of May 9, 1949 and bearing reference to the above subject matter. I am transmitting the same with the request by the Public Service Commission of Indiana that you submit all opinions called for by the enclosure, for the advice and information of the Commission."

Accompanying this letter was enclosed a letter from Mr. William E. Steckler, Counselor, which embraces the matter on which you desire an opinion. This letter is as follows:

"The evidence in the above captioned matter, which is now pending before the Commission, establishes the
fact that Indianapolis Railways, Incorporated is the parent corporation of its wholly owned subsidiary, the Traction Terminal Corporation. The evidence in said Cause also establishes the fact that the Indianapolis Railways, Incorporated is the lessee and as such, is engaged in the real estate business.

“Inasmuch as the record in this Cause further indicates that the Indianapolis Railways, Incorporated, a public utility, has sustained net losses to the extent of approximately Six Hundred Thousand Dollars through its operations as lessee of the Tractional Terminal Corporation property since the year 1932, there is a serious question in the mind of the writer regarding the validity of the lease existing between the Indianapolis Railways, Incorporated and its wholly owned subsidiary corporation. Obviously, such losses have no doubt affected the present financial stability of the Indianapolis Railways, Incorporated, which in turn affect the public's interests in the utility. In other words, it appears to the writer that such arrangement may tend to weaken the financial stability of a public utility and therefore is against public policy.

“In an effort to prove good faith between the parent corporation and the wholly owned subsidiary, the petitioner has introduced its Exhibit No. 35, which purports to be a copy of a legal opinion, dated March 23, 1945, from the law firm of Baker & Daniels, 810 Fletcher Trust Building, Indianapolis, Indiana.

“Since it appears to the writer that this exhibit places before the Commission the question of the validity of the lease existing between the two corporations, it is the desire of this office, and we now request, that the Public Service Commission of Indiana ask for an official opinion of the Attorney General of Indiana in regard to the validity of such lease.

“The writer also requests that the Commission seek an opinion of the Attorney General in regard to the admissibility and the weight of the petitioner's Exhibit No. 35, which purports to sustain the validity of the lease between the two corporations. It is also
the request of the writer that the Attorney General render an opinion as to the authority of, and what steps may be taken by, the Public Service Commission of Indiana, if the lease is declared to be invalid.

"Your prompt attention to this matter will be appreciated, inasmuch as it is essential that these questions be disposed of before the conclusion of the public's evidence in the above matter."

There are four questions embodied in the letter from the Public Counselor upon which you request an opinion:

(a) Is the lease executed by the Indianapolis Traction Terminal Corporation, lessor, and the Indianapolis Railways, Inc., lessee, a valid contract?

(b) Is the letter of Baker and Daniels, Attorneys, addressed to the lessee on March 23, 1945 competent evidence in the present rate case?

(c) If it is, what weight or probative force should be attached to such letter?

(d) If the lease is invalid what steps can be taken by the Commission and what authority does it have in reference thereto?

I will answer these questions in the order just stated.

(a) It is noted that the lease is between Traction Terminal Corporation and Indianapolis Railways, Incorporated, a public utility, operating under the terms and provisions of an indeterminate permit issued pursuant to terms of the "Spencer Shively Utility Act," and therefore subject to the proper control and regulation of the Public Service Commission of Indiana. The Indianapolis Railways, Incorporated, was incorporated under the laws of Indiana and authorized by the Public Service Commission to operate a street transportation utility. As such it was duly authorized to issue and sell its stock and bonds with which to acquire the transportation property franchise and equipment at a receiver's sale of a former street railway operated in the City of Indianapolis, and to rehabilitate said former properties and make additions thereto. It was not authorized by the Commission to engage in any other type of different business. Of course, there would
be implied under the law the right to do such other and further things as might reasonably be necessary, incidental and proper to carry out and fulfill its corporate functions and purposes.

It appears that the Indianapolis Traction Terminal Corporation, the lessor, is a subsidiary of the lessee, all of the common stock of which is owned by the lessee. The lessor had fewer members on its Board of Directors than lessee but all of its members were also members of the Board of Directors of lessee. Mr. Chase was president of both companies and Mr. Watson was vice-president of both and the same secretary served each company—in fact there existed the most complete example of interlocking directorate possible. Mr. Chase signed the lease as president of lessee and Mr. Watson signed it as vice-president of lessor.

By reason of this stock ownership and interlocking directorate the lessee, at the time of the execution of the lease, had and now retains complete control over the property of the lessor and has shaped its destiny. It follows that any profit that might be earned would inure to the exclusive benefit of the lessee and likewise any losses to the lessor corporation would fall on the lessee. Since both companies came under the same ownership, in the last analysis, the parent company was really making a contract with itself. It was not a case where there was a meeting of two minds so generally recognized in the law as an essential to the making of a valid contract. There are cases, however, where the courts have upheld such contract where it clearly appears that the rights of the subsidiary were not infringed upon by the parent company, and the contract is fair, reasonable and equitable in all of its terms and conditions.

A study of the lease gives no hint just why this lease was executed. In many respects it is unilateral in its terms, notably in favor of the lessor. It might be said it was made to give relief to the subsidiary in financial distress, mayhap to assist the Street Railways in some modern financing scheme whereby its stockholders would ultimately be the beneficiary.

The lease by its terms obligates the Street Railways, the utility, to assume many of the obligations, present and future, of a non-utility engaged chiefly in the real estate business, owning and renting business rooms, office rooms, parking
spaces, etc. The only part of the leased premises of use to the lessee in its operation is space used for ticket offices, baggage, storage room, for use of executives and administrative offices. These, however, constitute a minor part of the leased premises so it is apparent that it was wholly unnecessary for the utility to go into the real estate business to secure the necessary accommodations for these purposes.

The lease requires the lessee, to pay not only out of the earnings or rents of the premises, but from its corporate revenues, perhaps out of earnings, which would be available for dividends to its stockholders, the following obligations of the lessor:

(a) Interest on the mortgage bonds of lessor.
(b) All taxes assessed against lessor including federal and state income taxes.
(c) Insurance on all buildings and personal property of lessor.
(d) All repair and alteration on buildings.
(e) All corporate expenses to maintain the corporate identity of lessor.
(f) To keep party walls in repair.
(g) To pay all debts and obligations of lessee at the date of the contract whether arising out of the contract or tort.
(h) To pay all cost of litigation that may arise by reason of lessor being a party to the contract, including attorney fees.

To guarantee the payment of the obligations covered by the lessor and the fulfilment of its obligations according to the terms and tenor of the lease—the lessee agrees to pledge with the trustee of the first mortgage bonds $300,000.00 principal amount of the five percent gold bonds and 3,000 shares of the capital stock of the lessor corporation which it held. Their pledged securities may, under certain conditions and circumstances, be used by the trustee in payment and liquidation of lessor’s indebtedness.

In consideration of these obligations the lessee shall have full and complete possession of the leased premises, may rent and collect and retain all the earnings of every kind and character from all and singular the leased premises.
It must be presumed that since the Railways, the parent company, elected the officials of the lessor that it was thoroughly familiar with the earnings and expenses of the lessor corporation and knew full well the nature and extent of its undertaking when it executed the lease.

The letter of the Public Counselor which you enclose indicates that the Railways corporation has sustained net losses of approximately $600,000.00 since the year 1932 in meeting its obligations under this lease.

It does not appear that the lease was submitted to you for approval either before or after its execution. I am informed, however, that the lessee has annually made consolidated reports to your Commission and its predecessors in which it has shown the relationship existing by virtue of this lease and that no objection or exception has ever been made by the Commission or any member of its staff. It is possible that this might be construed as a ratification thereof so far as your Commission has the authority to approve such action under the law.

The question of the validity of such a lease by a public utility is one of first impression in this state and my research does not disclose that it has been presented in any other state either in its identical or similar form, so the answer as to its validity must be found from a consideration of all the elements involved, and the results that may follow from such a practice, the decision of the case in the last analysis requires us to keep in mind that the interest of the public, for whose benefit the utility law was enacted, must be of paramount importance. If such a contract is inimicable, or may become inimicable to the public interest, it must be condemned, but on the other hand, if it is not harmful to the public or if beneficial, it should not be held invalid because the owners of a utility should be allowed to conduct their business according to their best business judgment so long as their conduct does not infringe upon the rights of the public. The following authorities may be considered in arriving at a decision as to the validity of the contract:

1. One cannot contract with himself, because it requires the meeting of two minds, that is true of corporations having the same directors. It was a principle of the common law

2. In some of the states it is held that if the same persons are directors of both companies transactions between them are void.

In Alabama it is held that:

"This doctrine is founded upon that rigorous rule of morality, to be found, perhaps, in every enlightened system of jurisprudence, which recognizes one of the commonest of the infirmities of human nature, and sternly forbids the unequal conflict between duty and self-interest. * * *

Alabama Fidelity Mortgage & Bond Company v. Duberly, 73 So. 911.

The rule is followed in Nebraska, New Hampshire and Tennessee and others. Though the great weight of authority holds that such contracts are only voidable if bad faith or unfairness prevails to the detriment of the stockholders it may be set aside.

The rule just stated is the one applied to private corporations but in the case of public utility corporation, the rule is different, if a contract made in such manner is injurious to the public or interferes with the utility in discharging its full duty to its patrons then any such contract would be invalid, and should be canceled. In Massachusetts it was held that a lease of corporate property made by persons who are directors of the corporation, "is a suspicious circumstance, which calls for careful scrutiny, but of itself alone it does not necessarily render the transaction void." (William F. Nye v. Heman E. Storer et al. (1897), 168 Mass. 50, 46 N. E. 402.)

3. Contracts between two corporations having identical directors are not void but may be voidable depending on whether the same are fair and reasonable and do not infringe the right of others, especially the rights of the public. (Fletcher on Contracts, Vol. 4, pp. 3632-3634.)

4. "* * * 'where the same directors act in two companies their contracts are closely scrutinized, and
will not be upheld unless manifestly fair.' * * * 'while a contract between two corporations having common directors may be voidable, it is only so when the contract is in fraud of the interests of one of the corporations, and will never be set aside by the courts where the honesty of the transaction is manifest.'"

Evansville Public Hall Co. v. Bank of Commerce (1895), 144 Ind. 34, 36 and 37.

5. A railway company as a common carrier cannot enter into a contract that contravenes the rights of the general public because it would be against public policy, but it may enter into special engagements concerning matters in which the public has no interest.

Niederhaus v. Jackson, Receiver (1923), 79 Ind. App. 551;
Louisville, New Albany & Chicago Railway Co. v. Keefer (1896), 146 Ind. 21.

6. If it be claimed that the lessor was a public utility at the time it leased its property to the Street Railways Company then such lease would be invalid unless the consent of the Public Service Commission was first obtained. (Burns' 1933, 1947 Supplement, Section 54-509, 54-510, Acts 1939, Chapter 19, p. 34.)

7. The Commission shall inquire into neglect or violation of the law of this State or the ordinances of any city or town by any public utility doing business therein and it shall have the powers, and it shall be its duty, to enforce the provisions of this act and other laws relating to public utilities * * * any forfeiture or penalty shall be recovered in a suit in the name of the State of Indiana in the Circuit or Superior Court. (Burns' 1933, Section 54-714.)

8. No public utility shall issue any bonds, stock notes or other evidence of indebtedness except for labor or property at its current fair value as determined by the Commission actually received by it. (Burns' 1933, Section 54-502.)

9. Where the purchase of stock in one company by another amounts to engaging in a business other than that authorized in its charter, such purchase is ultra vires, and
this is so, not because the purchase is stock, but because the business is outside the scope of its charter.

Hill et al. v. Nisbet et al. (1884), 100 Ind. 341.

10. In the case of Kitchen v. St. Louis, etc., Railway Company (1878), 69 Missouri 224 it is held that although the trustees who made the sale were also members which made the purchase, this fact did not render the sale void. This case is cited with approval in Hill, et al. v. Nisbet, et al., supra, and also in Bristol Milling Company v. Probasco (1878), 64 Ind. 406 and Ward v. Polk (1880), 70 Ind. 309, such contracts are voidable not void. Pratt v. Luther (1873), 45 Ind. 250; Port v. Russell (1871), 36 Ind. 60.

Validity of the Lease.

From the consideration of the facts and principles of law hereinabove stated, I am of the opinion that:

(a) The pledge of $300,000.00 principal amount of the lessee's general mortgage five percent gold bonds referred to in Article 32 of the lease is invalid if these bonds are some of the bonds issued by lessee pursuant to the order of the Public Service Commission of Indiana with which to acquire the property of the predecessor corporation. Such pledge would be and is in violation of the authority under which they were issued. If my assumption is correct as to the issue of these bonds the Public Service Commission of Indiana should order that such pledge bonds be rescinded and the bonds restored to the lessee.

Burns' 1933, Section 54-505.

This section provides that the Commission shall have power to impose such conditions upon a public utility in issuing securities as it may deem reasonable. Such public utility shall not, without the consent of the Commission, apply said issues or any proceeds thereof to any purpose not specified in such order.

(b) The decision of the validity of the lease in its general scope is more difficult of solution. Its provisions are of such character by reason of interlocking directors that at first blush it seems that the lease would be void because the
directors of two corporations were involved in making the contract. These directors are identical in both companies and to further involve the situation the lessee owns all the stock of the lessor and by reason of the conditions which existed, had control of both corporations. A study of the situation under which the lease was executed subjects the lease to the closest scrutiny as to its validity. The decisions of the courts of the various States of the Union are not wholly in accord with the construction to be placed upon such contracts. Some of the states hold that a contract made between two corporations who have identity of directors is void, while other states hold that such contracts are not void but are voidable if the rights of others are affected. This seems to be the rule generally accepted with respect to corporations in general but in the case of a public utility where the interests of the public are involved a stricter rule is frequently applied. However, I am of the opinion that the weight of authority holds to the principle that unless a contract so made is violative of the rights of others or of the public and is fair and reasonable in all of its provisions that the contract is valid.

The public counselor in his letter included in your letter of transmittal alleges that the Street Railways Company as such public utility has sustained net losses since the year 1932 of approximately $600,000.00 through its operation of the traction terminal corporation contract, and in his opinion such losses seriously affect the financial stability of the Street Railways Company and no doubt make it difficult to properly finance its operations. If you find that the contention of the public counselor is correct and that the lease does materially affect the financial stability of the Street Railways Company then in my opinion such lease is void but I cannot say as a matter of law that it is void from a consideration of the language of the lease itself. Any contract made by a public utility which would improperly affect its financial stability would be against public policy and on that account void. This is a matter which you will have to determine because I do not have the necessary information in regard to just how and in what manner and to what extent the lease is inimicable to the public interest.

(c) As to the second question involved, namely, the letter offered in evidence as Exhibit number 35 purporting to be a
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copy of the legal opinion dated March 23, 1945 from the law firm of Baker and Daniels, you asked me to determine the admissibility of such letter and the weight to be given to it. The contract in question was dated June 1, 1932. This letter was written nearly thirteen years after the lease was executed. I am unable to see how the letter would tend to prove the good faith of the parent corporation in its execution. It rather indicates that someone had doubts about the validity of the lease and on that account asked for an opinion. It is merely a self-serving statement and its admissibility in evidence is doubtful. If accepted in evidence I cannot see that it has any weight or probative force. I do not think that an ex parte letter such as this would carry any weight as to the validity of the lease and it should therefore be rejected.

(d) Your next question is for information as to what steps might be taken by the Public Service Commission of Indiana if the lease is held to be invalid. The original Spencer Shively Act contains ample provisions for the Commission to enforce its orders.

Burns’ 1933, Section 54-714, Acts of 1913, Chapter 76, page 167 says:

“The commission shall inquire into any neglect or violation of the laws of this state or the ordinances of any city or town by any public utility doing business therein, or by the officers, agents or employees thereof, or by any person operating the plant of any public utility, and shall have the power, and it shall be its duty, to enforce the provisions of this act, as well as all other laws, relating to public utilities. Any forfeiture of penalty herein provided shall be recovered and suit therein shall be brought in the name of the state of Indiana in the circuit or superior court where the public utility has its principal place of business. Complaint for the collection of any such forfeiture may be made by the commission or any member thereof, and, when so made, the action so commenced shall be prosecuted by the general counsel.”

It is noted that said section provides, among other things, that the Commission or any member thereof may collect any
forfeiture that may be made by complaint filed in the circuit or superior court of any county in which the public utility has its principal place of business and that the "action so commenced shall be prosecuted by the general counsel." Since the general counsel of the Public Service Commission of Indiana is the Attorney General of Indiana it would be his duty to prosecute any action. The effect of the section just cited warrants the Public Service Commission of Indiana to file an information in *quo warranto* if it finds that a utility is violating the utility law and declines to end such violations. This is a special proceedings and should always be carefully and prudently invoked especially against a public utility because of injurious results that might follow such an action if such proceedings are erroneously brought.

In conclusion it may be stated that all of the terms and considerations of the lease agreement as obligations of the lessee embrace virtually every obligation of ownership. This in itself is not especially indicative of fraud or bad faith but is subject to the consideration of the Commission and its opinion is exactly discretionary as to whether or not such lease is feasible from an economic viewpoint in that it may cause expenses which are against public policy generally. The Commission must decide this question as a matter of fact and public policy rather than one of law.

CHJ:vb

**OFFICIAL OPINION NO. 56**

June 23, 1949.

Honorable Bernard E. Doyle, Chairman,
Indiana Alcoholic Beverage Commission,
201 Illinois Building,
Indianapolis, Indiana.

Dear Sir:

Your letter of May 26, 1949 received requesting an Official Opinion on the following question:

"Is the department (Indiana Alcoholic Beverage Commission) authorized to employ and with the ap-