

Decision No. 1264

ORIGINAL

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA.

In the matter of the application of
 San Diego and Arizona Railway Company,
 a corporation, for an order authorizing
 the issue of bonds.) Application No. 808.

Harry L. Titus, R. C. Dilworth and W. I. Brobeck
 for applicant.

EDGERTON and LOVELAND, Commissioners.

O P I N I O N

This is an application by San Diego and Arizona Railway Company for an order authorizing the issue of \$15,000,000 face value of bonds, and for an order authorizing said company to execute a mortgage or trust deed upon all of its property to secure the payment of said bonds.

The purposes for which the bond money is proposed to be used are to pay off and discharge indebtedness amounting to \$3,007,908.55, and with the remainder to finish the construction of its railroad.

Applicant was incorporated on June 14, 1906 by John D. Spreckels and A. B. Spreckels for the purpose of building a standard gauge steam railroad from San Diego eastward, passing through the northern part of Lower California, Mexico, and extending eastward to Yuma, Arizona, a distance of 200 miles. Later the plans were changed, making Seeley, Imperial County, the eastern terminus.

The line as now projected will extend from San Diego to Seeley, Imperial County, where it will connect with the Southern Pacific branch line from El Centro. The length of this railway will be 139.39 miles. Of this 44.29 miles will be located in Lower California, Mexico and 95.10 miles will be located in

California.

Portions of this line have been completed, as follows:

From San Diego to Tia Juana, on the Mexican border,	15 miles
From Seeley west,	<u>10</u> "
Total constructed in California,	25 "
Constructed in Mexico from Tia Juana eastward, approximately,	<u>40</u> "
Total constructed, approximately	65 "
Still to be constructed, approximately	75 "
To be constructed in Mexico	5 "
To be constructed in California	70 "

The portion of the road already built is of standard gauge and of first class construction. The grades have been skilfully conceived, and the engineering has been of a high type. The materials used have been of good quality and nowhere is there any evidence of skimping in the construction. In brief, the type of road being built is, in our judgment, of the best, and it is proposed to use this same type of construction in building the remainder of the railroad.

There is submitted an estimate of the cost of the railroad in the sum of \$13,846,956.37. The company adds for bond interest during construction \$867,000, making the total \$14,713,956.37. The engineers of the company testified that by substituting lighter rails on side tracks and by using less yardage for the present, and by making other changes, this estimate could be reduced approximately \$1,000,000, leaving a balance, as the revised estimate of \$13,713,956.37.

This includes block signals and everything necessary to complete the line, but makes no provision for equipment. The representatives of the company stated that the road would be operated either by lease to another company, or equipment would be purchased through the equipment trust certificate plan.

The company has an authorized stock issue of 60,000 shares of the par value of \$100 per share, or a total of \$6,000,000 par value. It has issued 20,000 shares of a total par value of \$2,000,000, and has received therefor \$2,000,000. It has also borrowed approximately \$3,000,000, as set forth in Exhibit "D" attached to the application. This indebtedness is represented chiefly by notes payable to the Bank of Commerce and Trust Company of San Diego, Union Trust Company of San Francisco, and the Wells Fargo Nevada National Bank of San Francisco.

The \$2,000,000 realized from stock and \$3,000,000 borrowed has been invested in the construction of the road. We therefore, have the following condition:

Estimated cost of road	\$13,713,956.37
Money already invested	5,000,000.00
Cost of balance	8,713,956.37

Authority is now asked to issue \$15,000,000 of general first lien 5 per cent 40 year gold bonds, under a proposed deed of trust to Union Trust Company of San Francisco and to sell these bonds at not less than 80 per cent of face value. If sold at 80 the net proceeds would be \$12,000,000, and with this the company proposes to pay off the floating indebtedness of \$3,000,000, and to use the remaining \$9,000,000 to complete the road.

The ownership of this railroad is in doubt. J. D. and A. B. Spreckels assert that although the stock stands in their names, the \$2,000,000 with which it was purchased was supplied by the Southern Pacific Company upon the understanding that the Southern Pacific Company would later take over the road. The Southern Pacific Company claims that it had the privilege of selling this stock to J. D. and A. B. Spreckels. It appears that the Southern Pacific tendered the stock to Messrs. Spreckels and they refused to take it. Suit was thereupon brought by the Southern Pacific to recover the money theretofore advanced by it, which suit is being contested by the Spreckels, and it is expected that the decision in

this suit, which is before the Federal Court, will determine the question of ownership.

A stipulation has been entered into, under which the bonds may be issued, without committing either the Spreckels or the Southern Pacific to the ownership of the road.

Applicant plans to organize a separate corporation under the laws of Mexico to hold that part of its property which is and will be located in Mexico, which will consist of 44.29 miles of road with appurtenances. The company's estimate of the cost of this portion of its road already constructed in Mexico is \$2,319,104.60, and that it would require to complete the line in Mexico \$1,139,444.57 or a total of \$3,458,549.17 for the Mexican properties.

It is proposed to have the Mexican corporation take over its portion of the property and to issue the stock of the Mexican corporation to applicant. Thereupon applicant will place this stock with the trustee named in the trust deed, to be held as security for the bonds.

The portion of the road in Mexico is being built under a 99 year concession held in the name of John D. Spreckels.

There is a wide spread demand on the part of the citizens of San Diego and Imperial Valley that this road be built. Seldom has this Commission been urged from so many different quarters to grant an application.

Particularly on the part of the citizens of San Diego it has been believed for years that the building of this road, furnishing as it will, an outlet to the East from San Diego, will greatly enhance the prosperity of that community. It is now necessary to reach the East by rail, to travel first to Los Angeles.

The people of San Diego have long felt that by reason of the location of their city upon an excellent harbor, and because of the proximity of the rich and rapidly growing Imperial Valley, direct rail connection to the eastern part of this country is essential to their full economic development.

We concur in the view that this community is of sufficient commercial and traffic importance to warrant the construction of a railroad as is now proposed.

There was introduced in evidence at the hearing estimates of the traffic which would be offered this road, not only from and to San Diego and Imperial Valley points but from and to points intermediate.

These estimates, if correct, would result in such huge earnings for this road that we hesitate to accept them as conservative. Of course, an estimate of this kind made prior to the construction of a railroad is only an estimate and must receive consideration as such. In this case it is so difficult to determine in advance what the resulting development of the country will be when traversed by a railroad, that we think it unwise for us to speculate in an attempt to fix a probable amount of traffic which will be furnished.

We believe that in this application we must confine ourselves to a conclusion whether, considering the value of the property, the issuance of securities asked for is proper, and if not, what is the proper amount of securities to be issued, and next, is the road one for which there is a real need, and which has a probable chance for success.

We have shown above that there is real need of this road, but we do not feel warranted at this time in permitting the issuance of all of the bonds asked for. We do feel, however, that with a somewhat less amount of bonds issued and additional money invested by way of purchase of stock the capitalization of the road would be upon a more reasonable basis. Applicant has estimated its property to be worth at least \$6,500,000, deducting \$3,000,000 of indebtedness leaves property of the value of \$3,500,000, which will be under the lien of the bonds.

Therefore, if there be issued \$3,000,000 of stock at par the proceeds from which are to be used to pay off the floating in-

of bonds
indebtedness of \$3,000,000 and \$10,000,000 to be issued and sold at not less than 80 per cent of face, we will have property which will have cost \$13,000,000, and upon which applicant places a value of at least \$14,500,000, as security for the payment of bonds of the face value of \$10,000,000. This, we think, is a basis upon which applicant could and should finance the building of this road.

We are convinced that the Messrs. Spreckels have made this application with no purpose of indulging in high finance, but that they have been actuated by a desire to have this road built. However, the evils of over-capitalization, particularly the over issue of bonds, have proven so severe in the past, that the people have delegated to this Commission authority to supervise the capitalization of public utilities. Clearly, the purpose of vesting this power in the Commission was to prevent the evil conditions of the past, and for us now to permit the issuance of a greater amount of bonds than we believe should be issued, is for this Commission to nullify the wishes of the people and to disregard the experiences of the past. In recommending, as we have, the above proposed issuance of stocks and bonds, we do so with the belief that upon this basis this road can be financed.

As is customary, we are authorizing the execution of a trust deed providing for \$15,000,000 of bonds, whereas we are only at this time authorizing the issuance of \$10,000,000 of bonds. The \$5,000,000 of bonds not at this time authorized by the Commission will, of course, remain in the treasury of the company to be used for any proper future needs and cannot be issued without the further authorization of this Commission.

We recommend therefore that applicant be authorized to issue \$10,000,000 face value of its bonds, to be sold at not less than 80 per cent of face value, and that it be authorized to mortgage or encumber its property for the purpose of securing an issue of \$15,000,000 of bonds, provided, that before issuing any of such bonds applicant shall have furnished to this Commission satisfactory

evidence that it has sold at par \$3,000,000 par value of its common capital stock, this order to authorize such issue of stock, the proceeds of the sale of said stock to be used to pay off the present indebtedness of applicant, and provided also, if applicant proposes to build this road, or any considerable part thereof, by contract rather than on force account, that any such contract be submitted to this Commission for its approval before its execution.

We submit herewith the following form of order:

O R D E R

Application having been made by San Diego and Arizona Railway Company for an order authorizing the issuance of \$15,000,000 of bonds, and authorizing the execution by it of a mortgage or trust deed to secure the payment of said bonds, and a public hearing having been held, and it appearing to the Commission that the purposes for which the proceeds of the sale of said bonds and the stock herein authorized to be issued are to be used are not in whole or in part reasonably chargeable to operating expenses or to income, and that said application should be granted in part and under certain conditions,

IT IS HEREBY ORDERED that the Railroad Commission of the State of California does hereby authorize the issue by San Diego and Arizona Railway Company of \$10,000,000 face value of its general first lien 5 per cent sinking fund 40 year gold bonds, under a proposed deed of trust to Union Trust Company of San Francisco, which provides for the issuance of \$15,000,000 of bonds, a copy of which is annexed to the application herein, and applicant is hereby further authorized to execute said trust deed, and applicant is further authorized to issue \$3,000,000 par value of its capital stock.

Said bonds and said stock to be issued under the following conditions, and not otherwise:

1. The bonds herein authorized shall be sold to net ap-

plicant not less than 80 per cent of their face value and accrued interest at the date of their delivery to the purchasers.

2. None of the above bonds shall be issued until applicant shall have obtained the approval of the Commission of a plan for the sale at par of \$3,000,000 of its capital stock.

3. Before any of the bonds or stocks herein authorized shall be issued there shall be submitted for the approval of the Commission a complete plan for the organization of the Mexican corporation which is to hold that part of applicant's railroad project which is and will be built in Mexico, and the placing of the assets of said corporation under the lien of the bonds herein authorized.

4. Before executing any contract for the construction of this road, or any part thereof, calling for an expenditure of \$10,000 or more, applicant shall first obtain the approval of this Commission thereto.

The purposes for which the bonds and the stock herein authorized to be issued are to be used, are as follows:

The payment of the indebtedness of applicant represented by promissory notes in the aggregate sum of \$3,007,908.55, said notes being described in Exhibit "D" on file with the application herein.

To build and construct the railroad and appurtenances from the City of San Diego through the northerly portion of Lower California, Mexico, into the Imperial Valley to Seeley, all as more particularly described in the maps on file herein and the inventory attached to the application herein.

Said company shall keep separate, true and accurate accounts showing the receipt and application in detail of the proceeds of the sale of the bonds and stock hereby authorized to be

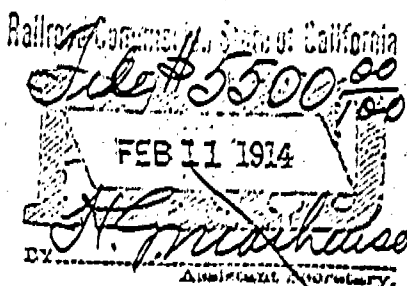
issued and on or before the 25th day of each month the company shall make a verified report to the Commission in accordance with the Commission's General Order No. 24, stating the sale or disposition of such bonds and stock during the preceding month, the terms and conditions of such sale or other disposition, the numbers of the bonds disposed of, the moneys realized from the disposal of said stocks and bonds, and the use and application of such moneys.

The authority hereby given to issue such bonds and stock shall apply only to bonds and stock issued by said company on or before the 1st day of February, 1915.

This order shall not be effective until applicant shall have first paid the fee prescribed by Section 57 of the Public Utilities Act.

The foregoing opinion and order are hereby approved and ordered filed as the opinion and order of the Railroad Commission of the State of California.

Dated at San Francisco, California, this 9th day of February, 1914.



John M. Eschman
H. D. L. Leland
W. L. Gordon
Max Theles
Edwin O. Edgerton
Commissioners.