

ORIGINAL

Decision No. 179

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA.

In the Matter of the Application of
NORTHERN CALIFORNIA POWER COMPANY,
Consolidated, for an order authorizing
it to issue \$500,000 face value of
five year 6 per cent debenture notes.

Application No. 156.

Appearances.

Edward Whaley, for applicant.

OPINION

Gordon, Commissioner.

This is an application for an order authorizing the issuance by Northern California Power Company, Consolidated, of its Series B, 6 per cent gold debenture notes of the face value of \$1000 each, to a total face value of \$500,000, to be dated July 15th, 1912, and to mature July 12th, 1917, and to sell same at a price of not less than \$960 for each debenture of \$1000 face value or a total price of \$480,000; and to apply the proceeds of such sale to the liquidation of its outstanding obligations.

The condition of the capitalization of applicant is as follows:

- Capital stock, all common authorized and outstanding \$10,000,000.
- Bonds authorized \$10,000,000.
- Bonds outstanding \$ 3,964,000.
- Bonds outstanding on companies consolidated into applicant \$1,003,000.
- Bonds outstanding on Sacramento Valley Power Company Under contract to be purchased by applicant \$900,000.
- Debenture bonds of applicant outstanding on above contract of purchaser \$300,200.

It should be said at the outset that it has been impossible to obtain adequate information concerning the value of the property owned by applicant, or its real net earnings as distinguished from a sum which is claim^{ed} to be net, but which may not be because of the failure to set aside proper amounts for depreciation. The officials of this corporation are wholly unable to produce either from their books or from their knowledge of the business any reliable information on the above subjects, and it must be apparent that where the managers of a utility business have no such information it becomes extremely difficult, if not impossible, for the Commission to arrive at any definite conclusion, short of having a complete physical valuation of the plant made, which would consume months. Applicant has urged speed on the part of the Commission in coming to a conclusion as to whether or not this request for a debenture note issue will be granted and has earnestly urged that no harm could result in granting this application, notwithstanding the slight amount of information obtainable as to the real condition of this corporation, because the transaction proposed amounts in essence to a refunding of existing obligations, as a result of which the company would gain five years time in which to pay its debts.

The fact that the granting of this application will in effect merely bring about the refunding of present outstanding indebtedness is urged by the managers of this corporation as sufficient reason for the granting of the application. This may or may not be true. The Commission has in several instances in passing upon applications such as this been con-

fronted with a condition analogous to the one we find here to exist. The system of financing which has heretofore prevailed in the State placed many utilities in a financial condition which this Commission expects to prevent as to utilities hereafter organized, and hopes to correct, at least in part, as to utilities whose financial condition has been brought about by action in the past which this Commission will not tolerate in the future.

The question that is here presented is, shall the Commission allow the contracting of new indebtedness by a utility regardless of its present financial condition so long as the new indebtedness does not add to its already existing obligations, but merely substitutes a new obligation for one that now exists? Or shall the Commission in every case take into consideration the present financial condition of the utility applying to issue stocks and bonds, and when the financial condition is shown to be unsound, shall the Commission require a correction of the bad financial condition as a prerequisite to the issuance of any stocks or bonds whether for refunding purposes or otherwise?

I believe that under ordinary circumstances the financial condition of a utility should always be considered in allowing the issuance of stocks and bonds whether the same are for refunding purposes, or will result in additions to the already outstanding obligations.

There can be no doubt that the Commission's approval of the issuance of stocks and bonds will be used by utilities in the sale thereof. Speaking as an abstract proposition, if the Commission should authorize the issuance of stocks and bonds for refunding purposes of a concern which is plainly

insolvent, such action on our part might be used to work fraud upon the purchasers of these new securities, and when the accounting comes, this Commission, of course, will be held accountable for having permitted new creditors to be substituted for other creditors. The original creditors of the concern, it is presumed, assumed their relationship with the utility at a time when its financial condition was good, while at times the new creditors will be led partly by the action of this Commission in approving the securities, to assume their relationship with the utility when the utility may be financially unable to redeem its obligations.

We recognize the fact that we owe a duty to the utility and its patrons, and to a certain extent to the investors as well. While, as we have stated in several instances, we do not guarantee the success of any undertaking of any utility, still we would be remiss in our duty if we failed to take into consideration the financial condition of the concern desiring to issue securities, knowing, as has already been said, that our approval will be used by the utility in the sale of such securities.

We have been dealing herein with those cases where the financial condition of the applicant is plainly insecure. There may be many instances where the financial condition will not be such as we believe it should be, and the utility still be in no danger of insolvency. In such cases the issuance of additional securities for the purpose of refunding already existing obligations to the extent permitted by law, is not subject to the same objection as exists with reference to an insolvent or tottering concern.

The proper parties to bear losses of utilities as well as of any other corporations, are the stockholders.

To be sure, there is a stockholders' liability which legally holds the stockholders to account, but too often in the case of utilities at least, bad financial conditions brought about by high financing are cured by exploiting the public through high rates, or by more high financing, and through re-organizing and unloading upon new stockholders and new bondholders securities that have nothing behind them except water and the desire of the promoters to reap a profit.

Investigation into the affairs of this concern shows that most of its stock was issued without consideration to the corporation, but that it had thereafter been sold to the public and has reached the hands of present stockholders at prices reaching as high as Sixty-five (\$65.00) Dollars per share of the par value of One Hundred (\$100.00) Dollars. Likewise it appears that many of the obligations which are sought to be liquidated by this issue of securities are obligations that are properly chargeable to operating expenses. The Public Utilities Act provides that stock and bonds shall not be issued for obligations "in whole or in part reasonably chargeable to operating expenses or to income." The operating expenses of a utility should be taken care of from the income derived annually from rates, or, where necessary, by assessment; and likewise depreciation should be provided for ahead of most expenditures other than operating expenses. Bond interest of course must be paid, but bond interest should come out of the profit which a reasonable rate gives to a concern over its operating expenses, depreciation and other charges which are directly connected with the furnishing of a utility.

It appears, as nearly as we can judge from the records, that this company owes in the neighborhood of \$750,000 for

which funds must be secured in the immediate future. We do not believe it is in danger of insolvency, and hence are not inclined to prevent it from securing a part of this money from the refunding issue such as is applied for in this application, but we do not propose to allow it to issue these debenture notes and use the proceeds thereof for the payment of obligations which are properly chargeable to operating expenses or depreciation.

It is urged that although the claims presented to the Commission to be liquidated by this issue of debenture notes show among them items properly chargeable to operating expenses, that this company has used the funds which properly should have paid such claims in extending its plant and constructions. The importance of this statement, while the actual condition does not appear clearly from the evidence, is that consideration should be given to such expenditure.

We are disposed under all the circumstances to allow the issuance of these debenture notes, but it will be necessary that each claim before its payment from the proceeds thereof, shall be presented to this Commission so that it may be determined whether or not such claim is one in the payment of which the proceeds of these debenture notes should be used.

If the condition of this company is as urged by its officers, then no doubt the proceeds from the sale of these debenture notes will put it into such a condition as regards its creditors that in its regular course of business it may take care of its other obligations.

If on the other hand it shall develop that there have not been expenditures made upon the plant in which funds were used that might properly have been devoted to the payment of

taxes and other operating expenses of the concern, we will have left obligations which can legally be paid from the proceeds of these debenture notes, and which should not in justice to the patrons of this utility be paid from future rates, and therefore an assessment of the stock will be necessary.

The permission to issue debenture notes as applied for should be contingent upon a stipulation signed by the officers of this company that at any time within eighteen months from date an assessment will be levied upon the stockholders of the company in an amount designated by the Commission, which shall be the amount necessary to pay outstanding obligations that are properly chargeable to income or operating expenses.

The following form of order is submitted:

O R D E R .

Application having been made to the Railroad Commission of the State of California by the Northern California Power Company, Consolidated, for an order authorizing the issuance by it of its series B, 6 per cent gold debenture notes of the face value of \$1000 each to a total face value of \$500,000 to be dated July 15th, 1912, and to mature July 15th, 1917, and to sell the same at a price not less than \$960.00 for each debenture note of \$1000 face value, or a total price of \$480,000, and to apply the proceeds of such sale to the liquidation of its outstanding obligations, and hearing having been duly held upon said application; and it appearing to the Commission that the issue of said debenture notes is reasonably required by said company for the discharge and lawful re-

funding of its obligations, to the extent that such obligations are not in whole or in part reasonably chargeable to operating expenses or to income, and that while said outstanding obligations are not specifically set out in the application and do not specifically appear from the evidence, yet under the restrictions hereinafter imposed the result will be that the purposes for which said debenture notes are issued herein are not in whole or in part reasonably chargeable to operating expenses or to income.

IT IS HEREBY ORDERED as follows:

Northern California Power Company, Consolidated, is hereby authorized to issue five hundred debenture notes, each of the face value of \$1000, bearing numbers 1 to 500 inclusive, said debenture notes to bear date July 15th, 1912, and to mature July 15th, 1917, and the same to bear interest at six (6%) per cent per annum, and the same to be sold at a price of not less than \$960.00 for each debenture note of the face value of \$1000.00, subject to the conditions following and not otherwise, to-wit:

(a). All moneys received from the sale of said debenture notes shall be placed in the Treasury of the said applicant, and no moneys paid out therefrom in the liquidation of outstanding indebtedness, or for any other purpose, until the claim which it is intended to pay shall be presented to the Railroad Commission so that it may be determined by said Commission that said claim is not in whole or in part reasonably chargeable to operating expenses or income.

(b). Applicant shall keep a true record showing the disposition made of all moneys received from such sale of debenture notes, and expended under the authority of the

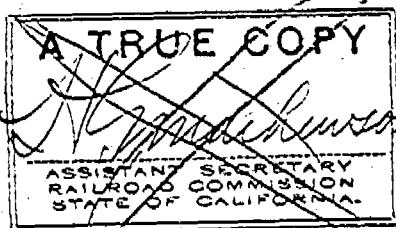
Commission, and shall indicate in said record the approval of the Railroad Commission to said expenditures, and the date thereof, and on or before the 25th day of each month the applicant shall make a verified report to the Commission showing said disbursements, and in this and all other respects applicant shall comply fully with the Commission's order, and with General Order No. 24, which in so far as applicable is made a part of this order.

(c). As a condition precedent to the approval by this Commission of the issuance by the applicant of the debenture notes herein specified, said applicant shall file with this Commission a stipulation in form satisfactory to the Commission, agreeing that at any time within eighteen months from date hereof, it will when directed by this Commission, levy an assessment upon its stockholders in an amount to be determined by this Commission.

(d). The authority hereby granted to issue debenture notes shall apply only to notes issued by applicant prior to the 30th day of June, 1913.

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, San Francisco, California, this 14th day of August, 1912.



John M. Eshleman
Max Theless

Commissioners.