

Decision No. _____

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA.

Decision No. 2863

ORIGINAL

In the matter of the application)
of CLEAR LAKE RAILROAD COMPANY)
for an order authorizing the issue)
of bonds of the face value of)
\$500,000 and capital stock of the)
par value of \$200,000.)
.....)

Application No. 651.

Haven and Athern, for applicant.

EDGERTON, Commissioner.

SECOND SUPPLEMENTAL OPINION

The petition of the Clear Lake Railroad Company for an order authorizing the issuance of stocks and bonds has been the subject of two former decisions by this Commission (Decision No. 1046 and Decision No. 1507) to which reference is hereby made.

In the first application to the Commission, filed July 25, 1913, authority was sought to issue stocks and bonds for the purpose of constructing a standard gauge railroad from Hopland, in Mendocino County, to Lakeport, in Lake County, together with branch lines from Lakeport to Kelseyville and from Lakeport to Upper Lake, in Lake County. The Commission granted the application under certain conditions and authorized the issue of 2617 shares of capital stock of a par value of \$100 each and \$500,000 face value of 6 per cent first-mortgage bonds. This authorization was based on the construction of a line from Hopland to Lakeport at a cost estimate of \$742,102.75.

Thereafter supplemental application was made by the Company based on a revised cost estimate. It was proposed to construct the railroad on force account, paying the contractor the cost of the work plus 12 per cent, which twelve per cent was to include contractor's profit, engineering and the marketing of the bonds

for at least 84 per cent of their face value. A responsible contractor was willing to build the road from Hopland to Lakeport, a distance of 24 miles, on this basis and at a maximum cost of \$470,000.

The Commission, on May 14, 1914, issued its supplemental opinion authorizing the issue of 750 shares of common capital stock of the par value of \$100 each and \$500,000 face value of 6 per cent first-mortgage bonds.

Seven miles of the road from Hopland easterly were graded and considerable construction material, especially bridge timber, tunnel timber and ties were purchased, and on March 31, 1916, the Company had expended for construction the sum of \$85,954.93.

The second supplemental application now before the Commission states that under present market and labor conditions it is impossible to construct the railroad from Hopland to Lakeport upon the location heretofore made within the estimate of cost of \$470,000. It is proposed to enter into a contract for the construction, equipment and initial operation of a standard gauge steam railroad and to pay the contractor a lump sum of \$500,000 face value of 25-year, first-mortgage, 6 per cent bonds, \$50,000 par value of the common capital stock heretofore authorized by the Commission and \$50,000 additional par value of common capital stock to be authorized by the Commission, making a total payment to the contractor of \$500,000 face value of bonds and \$100,000 par value of common capital stock.

The applicant also desires to issue \$25,000 par value of its common capital stock in exchange for terminal properties at Lakeport, California.

It is further stated in the application that applicant, through inadvertence or misunderstanding issued certificates of

stock and took subscriptions for stock in excess of the amount authorized by the Commission, to the par value of \$7,900 and authority is now desired to issue certificates to cover this amount and to have such certificates as have been issued confirmed by the Commission.

Applicant also desires authority to issue certificates of indebtedness, in exchange for capital stock to be surrendered, to such stockholders of the common capital stock of applicant who, since the purchase of such stock, have ceased to have any interest in the construction of this railroad.

In order to make the proposed issue of \$500,000 face value of first-mortgage bonds salable, authority is desired to issue \$500,000 face value of "Cumulative Participating" bonds, and to take subscriptions for \$350,000 face value thereof under an agreement, copy of which was filed with the Commission.

It will be noted that the second supplemental application of the Clear Lake Railroad Company now before the Commission amounts to a complete reorganization of its financial plans. It also contemplates a complete change in the plans for the construction of the proposed railroad.

The estimates heretofore submitted to the Commission and upon which its former orders were predicated, provided for the building of a standard gauge steam railroad according to maps and profiles on file with the Commission. This location was based on a line with a maximum grade of 4 per cent, compensated, and a maximum curvature of 240, all curves over 10 being spiralled. The alignment profile and adopted construction standards show that the building of what might be considered a first-class branch line was contemplated. Grading quantities were figured on a 16' road-bed; ties were to be cut from local timber, and the steel was to

be 65-lb. relay for the main line and 50-lb. relay for sidings. The summit of the divide between Hopland and Lakeport was to be crossed by a 1300' timbered tunnel, and the Russian River, immediately east of Hopland, was to be crossed by 2 - 90' spans second-hand steel trusses with pile trestle approaches.

The application now before the Commission contemplates the construction of the road on a much less favorable location and with less favorable grades and curvature. The maximum curvature, according to the present plan, is to be increased from 240 to 450 and the maximum gradient from 4% to 4½%. The line is to be located as closely as possible along the grade line contour and in side hill cutting, eliminating the cuts and fills of the former profile.

The width of the roadbed is reduced from 16' to 12'. The weight of steel for the main line is reduced from 65-lb. to 50-lb. relay steel. It is proposed to either eliminate the tunnel altogether and cross the divide by an open cut or to build a very much shorter tunnel than contemplated for the former line. The proposed construction will make it impossible to operate standard locomotives and passenger cars over the road, and it is proposed to equip the line with Shay geared locomotives and with specially designed gasoline passenger cars.

In spite of the cheaper and much less satisfactory construction standards and the greatly reduced grading quantities, and also in spite of the elimination or the material shortening of an expensive tunnel, applicant asks the Commission to approve a larger construction allowance than was estimated for the better line.

While the compensation to the contractor is fixed in the application at \$600,000 face value of securities, there is submitted to the Commission no estimate of construction upon which this compensation is based. The engineer of the road, Mr. J. B. Rogers,

testified at the hearing on this supplemental application, October 28th, that no definite construction estimate could be made until the location of the revised line was fixed and a profile compiled.

The Commission will not be in a position to pass intelligently on the estimate of cost of construction until surveys for the new line are made.

There is attached to the application as Exhibit "A" an agreement dated September 23, 1916, entered into between Guy L. Hardison and the Clear Lake Railroad Company, which the Commission is asked to approve. This agreement provides that Mr. Hardison shall, within eight months from date of contract, build the railroad, finance the purchase of all materials and equipment, pay all labor, engineering, legal and contingent expenses and all interest accruing on bonds during the construction period and to operate the railroad for a period of thirty days after completion. Thereupon Mr. Hardison, through ownership of the majority of the stock, will retain complete control of the property.

This agreement, in its present form, is so indefinite that I do not believe the Commission can authorize the issuance and sale of securities on the basis of such a contract. The location of the railroad and the amount and class of construction is left indefinite to a very large degree and remains largely at the discretion of the contractor. It is evident, however, that the road would be of cheaper and of a less desirable and permanent type of construction than contemplated in the application heretofore before the Commission.

I am also convinced that the proposed low construction standards and the limitations placed upon the operation of the road, if these standards are adopted, will seriously impair its usefulness after completion and will jeopardize its success as a business venture. I am of the opinion that the applicant should

revise its construction estimate on higher standards and should reduce the maximum grade and the maximum curvature. Operation of the line as now proposed is bound to be not only hazardous but also more costly by reason of increased maintenance and other operating expenses. This increase, I believe, will more than offset what savings may be effected in fixed charges through lower first cost.

The proposed plan of financing the construction of the railroad is reasonable, but it is impossible to pass upon the details as they have not been fully presented.

The Commission has heretofore expressed its belief that Lake County should have a railroad and has declared its willingness to aid to the fullest extent in the consummation of a project if it promises a fair measure of success. I reiterate those statements.

I do not believe, however, that the Commission should cancel its former orders and approve the new plan of financing until the location of the road, as now proposed, is more definitely known, the standards and type of construction more definitely fixed and a detailed construction estimate is available. This information must be secured in any event before construction can be commenced and it should be furnished to the Commission before securities are authorized and put upon the market. I do not believe it necessary, therefore, to go into the questions of operation, traffic, revenues and expenses until the fundamental information referred to is available, especially since I am convinced that the construction of a railroad into Lake County is justified and that with a proper type of construction the road will be able to earn its operating expenses, including depreciation, and, in addition, has a fair chance of being able to take care of its fixed charges out of earnings provided such charges are kept within reasonable limits.

At this time I recommend that no order be made but that a final determination of the issues involved be deferred until the

applicant has made a complete presentation of its engineering and financial plans.

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

Dated at San Francisco, California, this 9th day of November, 1916.

H. D. Loveland
Alex. Gordon
Edwin O. Egerton
Frank R. Wheeler
Commissioners.