

ORIGINAL

Decision No. 5057

BEFORE THE RAILROAD COMMISSION OF  
THE STATE OF CALIFORNIA

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In the Matter of the Application of  
SOUTHWESTERN HOME TELEPHONE COMPANY,  
a corporation, asking permission to  
issue other securities in place of  
bonds and provide for the payment of  
floating debt.

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Application  
No. 3055

R. Holtby Myers. for applicant.

GORDON, Commissioner

O P I N I O N

In this application, as amended, SOUTHWESTERN HOME TELEPHONE COMPANY asks authority to issue two-year 6 per cent notes in the aggregate face amount of \$89,050.00; to pledge \$177,500.00 face value of its first mortgage bonds to secure the payment of said notes and to issue trustee's certificates in amounts and for purposes hereinafter stated. The purpose of the application is mainly to refund outstanding indebtedness, to be secured by the same amount of bonds now outstanding.

The Railroad Commission in its Decision Number 1296, dated February 24, 1914, (Vol. 4, Opinions and Orders of the Railroad Commission of California, p. 247) reviewed the financial history of Southwestern Home Telephone Company and called attention

to the unsatisfactory financial condition of this company. To improve such condition, the Commission suggested a reduction of applicant's bonded indebtedness by the conversion of a portion of this indebtedness into stock or by some method equally satisfactory; a reduction of applicant's floating indebtedness by the amount paid as dividends during the past three or four years, or by such other means as shall reduce this indebtedness to a conservative basis; the cancellation of the 300,000 shares of "contract stock" as well as the cancellation of the stock held by the trustee under applicant's mortgage. The testimony shows that the 300,000 shares of stock and the stock held by the trustee have been canceled. Applicant has, however, been unable to induce any of its bondholders to convert a part of their bonds into stock nor has it been successful in obtaining funds to reduce its floating indebtedness.

Southwestern Home Telephone Company has reported to the Railroad Commission during the years 1914, 1915 and 1916 revenues and expenses as follows:

| I t e m                        | <u>1916</u>      | <u>1915</u>      | <u>1914</u>      |
|--------------------------------|------------------|------------------|------------------|
| Operating Revenues             | \$80,252.16      | \$79,069.94      | \$77,772.48      |
| Operating Expenses             | <u>47,484.40</u> | <u>38,552.38</u> | <u>31,539.79</u> |
| Net Operating Revenues         | \$32,767.76      | \$40,517.56      | \$46,232.69      |
| Taxes assignable to operations | <u>4,504.63</u>  | <u>4,262.83</u>  | <u>4,171.34</u>  |
| Operating Income               | \$28,263.13      | \$36,254.73      | \$42,061.35      |
| Non-operating Revenue-Net      | 175.00           | 952.81           | 102.55           |
| Gross Income                   | 28,438.13        | 37,207.54        | 42,163.90        |
| <u>Deductions:</u>             |                  |                  |                  |
| Rent for lease of plant        | 4,343.30         | 4,015.00         | 4,015.00         |
| Rent for telephone offices     | 916.00           | --               | 861.00           |
| Rent for poles, conduits, etc. | 631.27           | --               | 68.75            |
| Rent for instruments           | 300.00           | --               | --               |
| Interest on Funded Debt        | 16,125.00        | 15,900.00        | 15,900.00        |
| Other Interest                 | 8,084.96         | 8,051.50         | 8,188.49         |
| Miscellaneous                  | --               | --               | 32.56            |
| Total deductions               | <u>30,420.53</u> | <u>27,966.50</u> | <u>29,065.80</u> |
| Net Income - Surplus           | --               | 9,241.04         | 13,098.10        |
| Loss,                          | 1,982.40         | --               | --               |

The variations in the company's surplus account are shown by the following statement:-

| Item                                | 1916        | 1915       | 1914      |
|-------------------------------------|-------------|------------|-----------|
| Surplus beginning of Year           | \$12,802.97 | \$1,273.23 | \$ ---    |
| Miscellaneous Items                 | 852.17      | *2,288.70  | 1,273.23  |
| Surplus from operations             | ---         | 9,241.04   | 13,098.10 |
| Total Surplus and Additions         | 13,655.14   | 12,802.97  | 14,371.33 |
| Deductions:                         |             |            |           |
| Loss for year                       | 1,982.40    | ---        | ---       |
| Depreciation not covered by Reserve | 8,251.55    | ---        | 10,906.03 |
| Miscellaneous                       | 3,312.57    | ---        | 12,192.07 |
| Total Deductions                    | 13,546.52   | ---        | 13,098.10 |
| Surplus end of Year                 | 108.62      | 12,802.97  | 1,273.23  |

\*Difference to balance.

The maintenance expenses of the company in 1915 are reported at \$6,387.36 and in 1916 at \$21,162.12. The 1916 maintenance expenses include \$12,793.07 allowed for depreciation of plant and equipment. The general and miscellaneous operating expenses of the company were reduced from \$12,693.93 in 1915 to \$7,224.39 in 1916.

On June 30, 1917 Southwestern Home Telephone Company reported assets and liabilities in the following amounts:-

ASSETS:

|   |              |
|---|--------------|
| Capital.....                            | \$505,888.05 |
| Construction in Progress.....           | 628.67       |
| Cash in Hands of Trustee .....          | \$369.10     |
| Exchange Petty Cash.....                | 110.00       |
| First National Bank, Redlands.....      | 2,634.93     |
|   | 3,114.03     |
| Bills Receivable.....                   | 167.29       |
| Accounts Subscribers and Agents.....    | 694.75       |
| Miscellaneous Accounts.....             | 1,041.27     |
| Materials and Supplies.....             | 23,358.06    |
|   | 25,261.37    |
| Redlands Bonds in hands of Trustee .... | 3,500.00     |
| Prepaid Directory Expenses .....        | 104.05       |
| Advance Taxes. ....                     | 420.34       |
| Unamortized Debt Discount & Expense.... | 91,365.85    |
| Inventory Expense.....                  | 7,348.96     |
|   | 102,739.20   |
| Total Assets - - - - -                  | \$637,631.32 |

LIABILITIES:-

|  |                  |
|--|------------------|
| Capital Stock . . . . .                  | \$88,769.50      |
| Bonds . . . . .                          | 422,500.00       |
| Redlands Home . . . . .                  | \$100,000.00     |
| Southwestern . . . . .                   | 322,500.00       |
| Bills Payable . . . . .                  | 89,237.50        |
| Advance Payments - Subscribers . . . . . | 1,024.62         |
| Accounts Payable . . . . .               | 4,194.56         |
| Miscellaneous Liabilities . . . . .      | 254.46           |
| J. E. Logie, Trustee . . . . .           | 2,120.05         |
| Customer's Deposits . . . . .            | 1,261.94         |
| Pay Roll . . . . .                       | 1,081.05         |
| Matured Interest Funded Debt, . . . . .  | 5,697.90         |
| Matured Other Interest, . . . . .        | 1,105.82         |
| <br>Depreciation Reserve . . . . .       | <br>20,317.14    |
| Surplus . . . . .                        | 66.78            |
| <br>Total Liabilities . . . . .          | <br>\$637,631.32 |

The balance sheet of June 30, 1917, does not include the \$177,500.00 face value of bonds pledged to secure the payment of short term notes.

Counsel for applicant frankly admits that the company is unable because of the small net earnings, its large indebtedness and the condition of the security market at present, to secure funds through the issue of either stock or bonds. It has, therefore, become necessary to devise a plan for re-financing the company through funds obtained from the owners and holders of the company's stock, bonds and notes. These funds are to be obtained through the payment of an annual stockholders' assessment of not less than \$2,000.00 for a period of ten years; through the appropriation of net earnings in the sum of \$2,000.00 annually for a period of three years and \$3,000.00 annually for a period of seven years; through the waiver for a period of ten years of the sinking fund provision of the trust deed securing the payment of the Southwestern Home Telephone Company bonds; through the postponement of the collection of the April interest coupons attached to said bonds and through the reduction of the annual interest on applicant's outstanding notes from

7 and 8 per cent to 6 per cent per annum.

Applicant estimates that through the carrying out of this plan, it will secure funds sufficient to pay its \$89,050.00 of short term notes and thereby regain possession of the \$177,050.00 of bonds pledged to secure the payment of the notes. Any surplus remaining after the payment of the \$89,050.00 of notes and the deferred April interest coupons will be used to pay in part the \$100,000.00 of bonds issued by the Redlands Home Telephone Company. The Southwestern Home Telephone Company owns all of the outstanding stock of the Redlands Home Telephone Company and operates its properties under a lease, paying as a rental all of the expenses and fixed charges of the Redlands Company.

Applicant has an authorized stock issue of \$1,000,000.00 divided into 1,000,000 shares of the par value of \$1.00 each. On June 30, 1917, it reported 88,769-1/2 shares of stock outstanding. It appears that the ownership of this stock is widely scattered, there being about 70 stockholders. In "Exhibit No. 4", applicant reports that at a stockholders' meeting held December 14, 1917, 73,912-1/2 shares of stock were represented. The stockholders by unanimous vote authorized the Board of Directors to levy for a period of ten years a \$2,000.00 assessment annually. The authority granted to the Board of Directors is contingent upon all of the provisions of the reorganization plan being carried out.

In addition to paying \$2,000.00 annually for ten years in the form of an assessment, the plan requires the stockholders to appropriate from net earnings \$2,000.00 per annum during a period of three years and \$3,000.00 per annum during a period of seven years for the purpose of paying off the note indebtedness and the deferred interest coupons. Mr. Charles A. Rolfe, president of the Southwestern Home Telephone Company testified that in his opinion the company will have sufficient net earnings to make these appropriations.

He expects a gradual increase in the earnings and hopes through this reorganization plan to eliminate all attorneys' fees and expenses incidental to re-financing.

Southwestern Home Telephone Company has issued \$500,000.00 of bonds. All of the bonds are outstanding. Bonds in the amount of \$322,500.00 have been sold, while \$177,500.00 are pledged to secure the payment of \$89,050.00 of notes

The trust deed securing the payment of the bonds requires the company to pay to the trustee on October 1, 1917, and annually thereafter, until the maturity of the bonds, for sinking fund purposes, a sum equal to 2 per cent of all the bonds outstanding. Applicant has requested its bondholders to suspend this sinking fund provision of the trust deed for a period of ten years. It reports that up to December 18th, the owners and pledgees of \$375,500. of bonds have agreed to the suspension. It should be said in this connection that the suspension of the sinking fund provision is not contingent upon the proposed re-financing plan being carried out.

As said, the company proposes to ask the owners of Southwestern Home Telephone Company bonds to defer collecting the April interest coupons for a period of ten years. To prevent the deferred interest coupons from falling into the hands of innocent purchasers, the company will require the owners of bonds who approve this plan to detach the April interest coupons and deposit the same with a trustee. The trustee in turn will issue to the depositor trustee's certificates equal in face amount to each interest coupon deposited. The certificate will show on its face that it is issued in exchange for an interest coupon of like amount. Any purchaser of the certificate will be put on notice.

There are outstanding and in the hands of the public \$322,500.00 face value of 5 per cent bonds issued by Southwestern Home Telephone Company. The face amount of the April interest coupons aggregates \$8,062.50. The ownership of these bonds is

widely scattered. The company contemplates some difficulty in securing all of the bondholders to subscribe to this plan. For the purpose of calculating the results of the plan, applicant assumes that the owners of \$250,000.00 of bonds will defer collecting the April interest coupons. In such case, the annual payments made by the stockholders to the trustee will be augmented by the sum of \$6,250.00, the amount of the April interest due on \$250,000.00 of bonds. These annual payments will be further increased by the saving in the interest paid on the \$89,050.00 of notes, such saving resulting, first- from the reduction in the annual interest rate from 7 and 8 per cent to 6 per cent, and second- through the payment of the notes.

Applicant estimates that the amounts paid to the trustee under this plan will be sufficient to pay all of the \$89,050.00 of notes on or before April 1, 1924, and that as of that date it will have available \$8,049.00 to apply to the payment of deferred interest coupons. The aggregate face amount of deferred interest coupons, together with 5 per cent interest thereon, on April 1, 1924, will amount to \$42,835.00. Subsequent to this date all amounts paid by the stockholders, as well as an amount equal to the interest now being paid on the \$89,050.00 of notes will be used to liquidate the \$42,835.00 of indebtedness.

Applicant asks that as the \$177,500.00 of pledged bonds are being released through the payment of the \$89,050.00 of notes, it be permitted to deliver said bonds to the trustee as additional security for the payment of the deferred interest coupons. In the opinion of counsel for applicant, the deferred interest coupons constitute a lien on the properties of Southwestern Home Telephone Company. Regardless of this fact, applicant requests permission to secure the payment of the deferred interest coupons, together with the interest thereon, by depositing with

the trustee, as the notes are paid off, the \$177,500.00 of bonds. As indicated, the maximum amount of the indebtedness to be secured by the pledging of these bonds aggregates \$42,835.00.

The financial difficulties of Southwestern Home Telephone Company are in a large measure due to the conversion of stock into bonds, to which the Commission referred in its decision of February 24, 1914. The conversion of stock into bonds took place in 1907 and 1908. The logical step at this time would be to exchange some of the outstanding bonds for stock. Such a procedure, however, it is alleged is fraught with endless litigation.

The plan herein outlined is designed to improve the financial condition of Southwestern Home Telephone Company. It has as its one objective, the payment of the \$89,050.00 of notes and the return to the company's treasury of the \$177,500.00 of pledged bonds. To bring about these results, the holders of all classes of securities are asked to co-operate. The stockholders are requested to contribute \$47,000.00; the note-holders to extend the time within which they demand payment of their notes and in the meantime accept a lower rate of interest, and the bondholders to defer for ten years, if necessary, the collection of the April interest coupons. The plan contemplates the payment in full of the April interest coupons, together with the interest thereon at the rate of 5 per cent per annum. The bondholders are not asked to surrender any rights. They are asked to postpone the enforcement of their rights under the deed of trust. If the plan for any reason fails, the interest coupons deposited with the trustee will be returned to the respective bondholders. Under the circumstances and having in mind the financial condition of this company, I do not believe that it is an unreasonable request upon the bondholders to ask them to co-operate in carrying out the financial



plan, to such a degree so that the bonds now pledged will be returned to applicant's treasury as the \$89,050.00 of notes are being paid off. The order herein will so provide.

Applicant has submitted to the Commission for approval a copy of the proposed agreement to be entered into by and between Southwestern Home Telephone Company, certain bondholders of said company and a banking institution as trustee; also a copy of a proposed trustee's certificate to be issued in exchange for the deposited April interest coupons. Under the proposed agreement, the application of the moneys paid to the trustee under the plan vests in the final analysis with a committee of five bondholders. While it is necessary for this committee to act in an impartial manner, nevertheless it is expected that it will give due consideration to the claim of the holders of notes and that whenever it can, without doing an injustice to other noteholders, it will pay the most urgent claims made upon it. I do not believe it is necessary for the Commission, either directly or indirectly, to approve the proposed agreement. It is necessary, however, that the proposed agreement be modified so as to be in accord with the order of the Commission. A copy of the agreement as finally executed shall be filed with the Railroad Commission.

I submit herewith the following form of order.

O R D E R.

SOUTHWESTERN HOME TELEPHONE COMPANY having applied to the Railroad Commission for authority to issue notes, trustee's certificates and to pledge bonds, as hereinbefore stated,

And a public hearing having been held and the Commission being of the opinion that this application should be granted subject to the conditions of the order herein,

IT IS HEREBY ORDERED that Southwestern Home Telephone

Company be, and it is hereby, granted authority to issue two-year 6 per cent notes in the aggregate sum of \$89,050.00 for the purpose of refunding the following notes:

| <u>Name</u>                    | <u>Amount</u> | <u>Maturing Date</u> |
|--------------------------------|---------------|----------------------|
| Mary G. Prendergast            | \$1,250.00    | April 30, 1918       |
| Prendergast Estate             | 10,000.00     | April 30, 1918       |
| F.H. Wells                     | 10,000.00     | April 25, 1918       |
| J.W. Brock                     | 5,000.00      | April 25, 1918       |
| Joseph S. Hale                 | 2,000.00      | May 3, 1918          |
| Mary G. Casselberry            | 2,500.00      | July 7, 1918         |
| Prendergast Estate             | 8,000.00      | May 15, 1918         |
| E.M. Izard                     | 4,500.00      | June 15, 1917        |
| Ellen A. Lewis                 | 2,000.00      | May 6, 1918          |
| Estate Mary S. Sargent         | 6,000.00      | May 3, 1918          |
| Alice P. and Mary Denison      | 2,250.00      | June 11, 1918        |
| Ellen A. Roberts               | 1,000.00      | April 3, 1917        |
| Henry Fisher                   | 1,800.00      | Sept. 1, 1918        |
| E.J. Wolverton                 | 1,000.00      | May 11, 1918         |
| J.O. Thompson                  | 1,000.00      | May 6, 1918          |
| C.H. Rohrer                    | 4,250.00      | June 1, 1918         |
| Gertrude A. Hayes              | 3,000.00      | June 29, 1918        |
| Henry Fisher                   | 1,500.00      | October 8, 1917      |
| Henry Fisher                   | 2,000.00      | January 22, 1919     |
| Mary J. Webster                | 10,000.00     | June 30, 1918        |
| First National Bank, Redlands, | 10,000.00     | February 1, 1918     |
| Total, . . . . .               | \$89,050.00   |                      |

IT IS HEREBY FURTHER ORDERED that Southwestern Home Telephone Company be, and it is hereby, granted authority to issue \$80,625.00 face value of trustee's certificates, or such an amount thereof as may be necessary to carry out the proposed re-financing plan outlined in the foregoing opinion, - said trustee's certificates to be substantially in the same form as the trustee's certificate filed with this Commission on January 3, 1918.

IT IS HEREBY FURTHER ORDERED that Southwestern Home Telephone Company be, and it is hereby, granted authority to pledge \$177,500.00 of bonds to secure the payment of the 2-year 6 per cent notes herein authorized to be issued, provided that said bonds be pledged in the same ratio as at present to secure the payment of the notes to be refunded, and provided further, that upon the

payment of said notes, or any of the notes to be refunded through the issue of the notes herein authorized to be issued, bonds pledged as security therefor shall be returned to applicant's treasury in such an amount so that the ratio of the face value of the bonds remaining in pledge to the face value of the unpaid notes shall be substantially as two to one. Any bonds returned to applicant's treasury through the payment of notes, shall be hereafter issued only upon further order of the Railroad Commission.

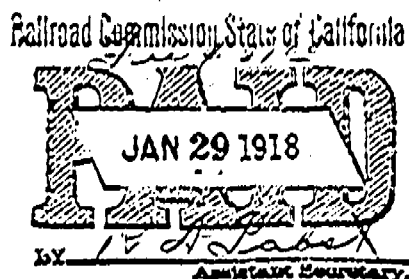
The authority herein granted is granted upon the following conditions and not otherwise.

- 1.- Applicant shall file with the Commission within 30 days after its execution a verified copy of the proposed agreement under the terms of which the plan herein outlined is to be carried out.
- 2.- Applicant shall file with the Commission within 30 days after the plan becomes operative a verified copy of the trustee's certificate.
- 3.- Applicant shall file with the Commission semi-annual reports showing in detail the payments made to the trustee under this plan and the application of such payments, and the amount and the number of the bonds returned to its treasury.
- 4.- The authority herein granted shall not become effective until applicant has paid the fee prescribed by the Public Utilities Act.

5.- The authority herein granted shall apply only to such notes, bonds and trustee's certificates as may be issued on or before November 30, 1918.

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 18th day of January, 1918.



Max Thelen  
H. S. Overland  
Wm. G. Adams  
Stam R. Decker

Commissioners.