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ORIGINAL

Decision No. 5848

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application
of SAN DIEGO AND ARIZONA RAILWAY
COMPANY for an order authorizing
the issue and sale of bonds and
approval of trust deed.

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Application No. 808.

R. G. Dilworth, for applicant.

LOVELAND, Commissioner.

FIRST SUPPLEMENTAL OPINION

Applicant in the above entitled matter has filed a supplemental petition asking authority to execute a mortgage securing the payment of \$12,000,000. of 6 per cent 40-year bonds payable July 1, 1957; issue not exceeding \$8,000,000. of said bonds and \$5,826,800.23 of 7 per cent cumulative preferred stock for the purpose of refunding its indebtedness and financing the completion of its line of railway.

Applicant in Exhibit Number "3" filed July 29, 1918
 reports its assets and liabilities as of June 30, 1918 as follows:-

ASSETS

Investment in Road and Equipment	\$7,707,900.14	
Miscellaneous Physical Property	148,775.20	
Investments in Affiliated Companies		
(a) Stocks	3,896,309.45	
(d) Advances	128,456.94	\$11,881,441.73
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Other Investments		
(a) Stocks	1.00	
(c) Notes	9,500.00	9,501.00
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Total		11,890,942.73

Current Assets:

Cash	97,367.39	
Special Deposits	11,378.87	
Traffic and Car Service Balances		
Receivable	886.20	
Net Balances Receivable from Agents and Conductors	11,517.53	
Miscellaneous Accounts Receivable	30,456.48	
Material and Supplies	427,792.53	
Other Current Assets	99.26	
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Total		579,478.26

Deferred Assets:

Working Fund Advances	212.16	
Other Deferred Assets	1,502.58	
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Total		1,714.74

Unadjusted Debits:

Rents and Insurance Premiums paid in advance	1,724.76	
Discount on Funded Debt	1,329.73	
Other Unadjusted Debits	760,446.24	
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Total		763,500.73

TOTAL ASSETS

\$13,235,636.46

LIABILITIES

Capital Stock		2,000,000.00
<u>Long Term Debt:</u>		
Non-negotiable Debt to Affiliated Companies		10,040,751.01
<u>Current Liabilities:</u>		
Audited Accounts and Wages Payable	103,817.47	
Miscellaneous Accounts Payable	1,569,789.48	
Other Current Liabilities	2.85	1,673,609.80
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<u>Deferred Liabilities:</u>		
Other Deferred Liabilities		188,673.49
<u>Unadjusted Credits:</u>		
Tax Liability (Credit)	604.84	
Accrued Depreciation-Equipment	53,574.96	
Other Unadjusted Credits	138,487.04	191,457.16
Profit and Loss - Debit Balance		858,855.00
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TOTAL LIABILITIES

\$13,235,636.46

In Decision Number 1264, dated February 9, 1914, (Vol. 4, Opinions and Orders of the Railroad Commission of California, p. 177) as amended, the Railroad Commission authorized San Diego and Arizona Railroad Company to issue on or before June 30, 1917, \$3,000,000.00 of common stock and \$10,000,000.00 of general lien 5 per cent sinking fund 40-year gold bonds for the purpose of refunding an indebtedness of \$3,007,908.50 and financing the construction of a line of railway and appurtenances from the City of San Diego through the northern portion of Lower California, Mexico to Seeley in the Imperial Valley, all of which is more particularly described in the maps on file herein and in the estimate attached to the original petition. Applicant reports that it has issued none of the stock or bonds. In the meantime, applicant has proceeded with its construction work. In Exhibit Number "1" filed July 29, 1918, it reports its investment in road and equipment at \$11,596,902.09. Of this amount \$7,707,900.14 represents investment in California and \$3,889,001.95 investment in Mexico. The lines in Mexico are owned by Compania del Ferrocarril de Tijuana y Tecate, S.-A., a Mexican corporation. Applicant owns all of the stock of the Mexican corporation and intends to deposit it with the trustee under the mortgage which it now proposes to execute. The \$11,596,902.09 includes \$729,798.38 of interest during construction and \$1,192,774.13 representing the cost of the properties of the San Diego & Southeastern Railway Company acquired pursuant to an order of the Railroad Commission.

San Diego & Arizona Railway Company was organized December 15, 1906. Litigation between the Southern Pacific Company and J.D. & A.B. Spreckels relative to the ownership of \$2,000,000 of common stock of San Diego and Arizona Railway Company, the civil war in Mexico and the European war all contributed to the delay of the completion of the road.

In Exhibit 6, applicant reports the total distance between terminal points of its line of railway at 139.49 miles. Its completed road is reported as follows

- 1.-- From First to Fifth Street, San Diego,..... .27 miles
- 2.-- From Tenth Street, San Diego to International Boundary line at Tia Juana,..... 14.34 miles
- International Boundary line at Tia Juana to " " International Boundary line west of Campo,..... 44.37 miles
- 3.-- New River, Imperial County West to end of track at Carriso Pass,..... 31.34 miles
- 4.-- International Boundary line west of Campo east to end of track, Tecate Divide, Station "E" 650 + 00, 23.05 miles
- Total track laid main line,..... 113.37 miles
- Total siding spurs and wyes laid,..... 15.17 miles
- Total main line and sidings laid,.... 128.54 miles

Applicant further reports the section of line now under construction, Mountain Division, from end of track Station "E" 650 + 00, Carriso Pass, 24.78 miles, 13 miles of which is practically completed and ready for track. The remaining portion about 11.8 miles in the Carriso Gorge is about 50 per cent completed.

In its decision of February 9, 1914 the Railroad Commission referring to applicant's type of construction said:-

"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."

The evidence submitted at the recent hearing shows that the construction standards have been lowered as

compared with those to which the Commission refers in its decision of February 9, 1914. A portion of applicant's line of railway has been relocated. The testimony of Mr. E. J. Kallright, applicant's chief engineer, shows that expensive construction and a great many of the proposed facilities have been eliminated; that originally it was planned to put in concrete portals and concrete linings in some of the tunnels but since timber portals and timber linings have been decided upon; that in Carriso Gorge a number of temporary structures have been determined upon and the tunnel work in the Gorge reduced approximately 40 per cent; that the width of the road-bed has been reduced from 20 feet to 18 feet, and, in fill, from 18 feet to 16 feet; that 75 pound rail has been substituted for 90 pound rail on the mountain section; that a cheaper class of construction has been adopted for terminal facilities; that considerable smaller shops will be built than was originally planned; that less tracks will be put in the yards than was contemplated in the first estimate and that dock and wharf facilities for which in the original estimate \$352,800.00 was allowed will now be eliminated altogether for the reason that the company has a trackage agreement with the Santa Fe which will eliminate the dock and wharfage facilities. I am not saying that these changes are unwise and unwarranted in view of present conditions but merely call attention thereto for the purpose of indicating that applicant has modified its construction standard. Mr. Kallright believes that with the changes suggested by him, applicant's line can be completed prior to June 30, 1919.

The testimony shows that J. D. & A. B. Spreckels and the Southern Pacific Company have compromised the litigation relative to the ownership of the \$2,000,000. common stock issued by San Diego and Arizona Railway Company and have entered into an agreement dated October 1, 1916 providing for the financing of the construction of applicant's line of railway. The agreement, as amended, provides that the Southern Pacific Company shall advance to the San Diego and Arizona Railway Company the money necessary after October 1, 1916 to

complete the railway from San Diego to Seeley and equip the same, said equipment not to cost over \$700,000.00. In return for such advances San Diego & Arizona Railway Company shall deliver to the Southern Pacific Company its 6 per cent 40-year first mortgage bonds, the face value of the bonds so delivered to be equal to the amount of the advances made by the Southern Pacific Company subsequent to October 1, 1916, including interest at 6 per cent per annum from the date of such advances to the delivery of the bonds. According to the terms of the agreement the Southern Pacific Company and the Spreckels interests agree to pay in cash, in equal amounts, \$1,430,000.00 of bank loans together with the interest due on such loans. In exchange for these payments San Diego and Arizona Railway Company agrees to deliver to the Southern Pacific Company and the Spreckels interests an amount of its first mortgage bonds equivalent to the amount paid by the respective parties. The agreement further provides that from the advances by the Southern Pacific Company and the Spreckels interests prior to October 1, 1916, shall be deducted the \$2,000,000. of common stock issued and the balance refunded through the issue at par of 7 per cent preferred stock. To summarize the agreement provides for the refunding of the company's indebtedness other than bank loans up to October 1, 1916 through the issue of common and preferred stock and the refunding of the bank loans and advances by the Southern Pacific Company since October 1, 1916 through the issue of first mortgage 6 per cent 40-year bonds.

The advances by the Southern Pacific Company and the Spreckels interests to October 1, 1916 are reported in Exhibit "E" as follows:-

	<u>Principal</u>	<u>Interest</u>	
Spreckels interest	\$3,497,756.00	\$ 350,043.00	
Southern Pacific Company	2,867,000.00	1,112,000.00	
Total	6,364,756.00	1,462,043.00	
Total Principal and interest			\$7,826,799.00
Less Common Stock issued			2,000,000.00
To be refunded through issue of preferred stock			5,826,799.00
Preferred stock to be issued to Spreckels interest			2,847,799.00
Preferred stock to be issued to Southern Pacific Co.			2,979,000.00

The bank loans and accrued interest to be refunded through the issue of bonds, as per request of applicant, and the advances by the Southern Pacific Company from October 1, 1916 to June 30, 1918, as well as the estimated advances which are necessary to complete the road are reported in Exhibits 5, 4 and 6 respectively as follows:

Bank loans - $\frac{1}{2}$ paid by Southern Pacific Company, $\frac{1}{2}$ by Spreckels interests,.....	\$1,430,000.00
Interest thereon to June 30, 1918,.....	530,178.00
Advances by Southern Pacific Company from October 1, 1916 to June 30, 1918,.....	2,592,930.80
Interest on said advances from January 1, 1918 to June 30, 1918,.....	56,129.40
Estimated advances necessary to complete road,	2,439,850.00
Estimated interest accruals prior to completion of road,.....	<u>240,000.00</u>
Total to be refunded through the issue of bonds,.....	<u>\$7,289,088.20</u>

Assuming the Railroad Commission grants the supplemental petition now pending before it, applicant will have outstanding stocks and bonds as follows:

Common Stock,.....	\$2,000,000.00
Preferred Stock,.....	5,826,799.00
Bonds,.....	<u>7,289,088.20</u>
Total,.....	<u>\$15,115,887.20</u>

Amount of cash advanced by Southern Pacific Company and Spreckels interests, to June 30, 1918, exclusive of interest, as per applicant's reports,.....	10,354,906.00
Add estimated cost to complete,.....	<u>2,439,850.00</u>
Total Principal,.....	<u>\$12,794,756.00</u>
Less bonds which applicant proposes to issue,	<u>7,289,088.20</u>
	<u>\$5,505,667.80</u>

In arriving at the \$5,505,667.80, no account whatever was taken of interest during construction. Applicant has issued \$2,000,000 of common stock and now proposes to issue \$5,826,799.00 of 7 per cent preferred stock, which would mean that applicant's \$7,826,799 of stock would be issued on a basis of 70.3 per cent with no allowance for interest during construction. Not until the road

is completed can the Commission determine how much interest shall be charged to capital account. Any interest during construction allowed hereafter to be charged to capital account will go to increase the investment against which stock is herein authorized to be issued and will, of course, increase the figure against which the stock is being issued. Any interest which the Commission may hereafter allow to be charged to capital account shall not be urged as a reason for the issue of additional stocks or bonds.

I do not believe that the amount of securities which applicant desires to issue, taking into consideration the facts and circumstances surrounding the construction of this line of railway and the further fact that neither the Spreckels interests nor the Southern Pacific Company intend at this time to sell any of the stocks or bonds, is unreasonable. It is, of course, understood that only such an amount of the stock and bonds herein authorized will now be issued as may be necessary to pay or refund applicant's indebtedness payable to the Spreckels interests or to the Southern Pacific Company, and that the remainder of the bonds will be issued from time to time to the Southern Pacific Company to pay or refund advances by the Southern Pacific Company to the San Diego and Arizona Railway Company pursuant to the terms of the agreement attached to the supplemental petition herein and marked Exhibit "A". In its decision of February 9, 1914, the Railroad Commission refers to the testimony relative to the earnings of this road. At the recent hearing, no additional testimony was introduced on this point. Until, and even after the road is completed, the earnings are problematical. This is a development enterprise and there is no means by which I can determine its earnings with any degree of certainty. Both the Spreckels interests and the Southern Pacific feel confident that the road will pay and have shown their confidence by investing several million

dollars and by taking the securities now authorized at par with no intention of selling them to the public. The Southern Pacific expects to invest more than \$2,000,000 additional to complete the road.

I expect applicant to expedite in every way possible the completion of its line of railway and am proceeding on the theory that the line will be completed before June 30, 1919.

As said above, applicant asks authority to execute a mortgage to the United States Mortgage & Trust Company to secure the payment of \$12,000,000 of first mortgage 6 per cent bonds, payable July 1, 1957. Heretofore the Railroad Commission authorized applicant to execute to the Union Trust Company of San Francisco a mortgage to secure the payment of \$25,000,000 of 5 per cent 40-year bonds. Applicant reports that its Board of Directors and its officers have procured a satisfaction of the mortgage delivered to the Union Trust Company of San Francisco and the re-conveyance to applicant of the properties described and conveyed in said mortgage. The mortgage which applicant now proposes to execute covers the stock of the Compania del Ferrocarril de Tijuana y Tecate, S.A.

I herewith submit the following form of Order:

FIFTEENTH SUPPLEMENTAL ORDER

SAN DIEGO AND ARIZONA RAILWAY COMPANY having applied to the Railroad Commission for authority to execute a mortgage and to issue preferred stock and bonds as indicated in the foregoing Opinion, a public hearing having been held, and the Commission being of the opinion that the money, property or labor to be procured or paid for by such issue is reasonably required for the purpose or purposes specified in the Order;

IT IS HEREBY ORDERED that San Diego and Arizona

Railway Company be, and the same is hereby, authorized to execute a mortgage substantially in the same form as the mortgage filed in this proceeding on June 3, 1918.

IT IS HEREBY FURTHER ORDERED that San Diego and Arizona Railway Company be, and the same is hereby, granted authority to issue not exceeding \$5,826,799.00 par value of its 7 per cent cumulative preferred stock and not exceeding \$7,289,088.20 of its 6 per cent 40-year bonds upon the following conditions and not otherwise:

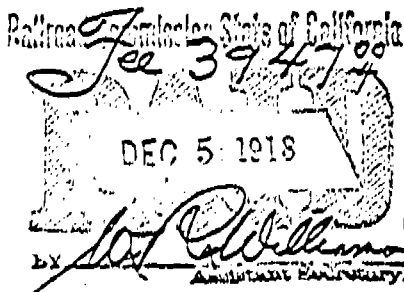
- 1.-- The stock herein authorized to be issued shall be issued to J.D. & A.B. Spreckels and the Southern Pacific Company for the purpose of paying or refunding in part the advances made by J.D. & A.B. Spreckels and the Southern Pacific Company prior to October 1, 1916, pursuant to the terms of the agreement attached to the supplemental petition and marked Exhibit "A".
- 2.-- The \$7,289,088.20 of bonds herein authorized to be issued shall be issued to J.D. & A.B. Spreckels and the Southern Pacific Company for the purpose of paying and refunding advances made by J.D. & A.B. Spreckels and the Southern Pacific Company to pay bank loans and to finance the construction of applicant's line of railway subsequent to October 1, 1916, pursuant to the terms of the agreement attached to the supplemental petition and marked Exhibit "A".
- 3.-- The approval herein given of said mortgage is for the purpose of this proceeding only and an approval in so far as this Commission has jurisdiction under the terms of the Public Utilities Act and is not intended as an

approval of said mortgage as to such other legal requirements to which said mortgage may be subject.

- 4.-- The authority herein granted to issue stock and bonds shall not be interpreted as authorizing applicant to charge to capital account any interest during construction, -the amount of interest to be so charged will be determined hereafter upon the completion of applicant's line of railway.
- 5.-- San Diego and Arizona Railway Company shall keep separate, true and accurate accounts showing the receipt and application in detail of the proceeds from the sale of the bonds and stock herein authorized to be issued, and on or before the twenty-fifth day of each month the company shall make verified reports to the Commission in accordance with this Commission's General Order Number 24, which order, in so far as applicable, is made a part of this Order.
- 6.-- The authority herein granted shall not become effective until applicant has paid the fee prescribed by the Public Utilities Act.
- 7.-- The authority herein granted shall apply only to such bonds and such stock as may be issued on or before March 30, 1919.

The foregoing First Supplemental Opinion and Fifteenth Supplemental Order are hereby approved and ordered filed as the First Supplemental Opinion and Fifteenth Supplemental Order of the Railroad Commission of the State of California.

Dated at San Francisco, California, this 11th day of October, 1918.



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COMMISSIONERS.