

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA.

In the Matter of the Application of SOUTHERN PACIFIC COMPANY for the approval of a lease of railroad equipment, dated September 2, 1913, from Commercial Trust Company to Southern Pacific Company, and an agreement dated September 2, 1913, between Harry E. Richter and William L. Fry with Commercial Trust Company and Southern Pacific Company, and for an order authorizing the issuance of trust certificates as provided in said lease and agreement.

Application No. 723.

Guy V. Shoup and Henley C. Booth for applicant.

THELEN, Commissioner.

OPINION.

This is an application for an order of this Commission approving a certain lease of railroad equipment, dated September 2, 1913, from Commercial Trust Company to Southern Pacific Company, and an agreement dated September 2, 1913, between Harry E. Richter and William L. Fry with Commercial Trust Company and Southern Pacific Company, and authorizing the issuance of Southern Pacific Company equipment trust certificates, Series B, of the aggregate principal amount of \$2,010,000, and further authorizing the Southern Pacific Company to guarantee the payment of the principal and the dividend coupons of said equipment trust certificates as provided in said agreement, and also authorizing said Southern Pacific Company in order to obtain subscriptions for said equipment trust certificates to pay discounts and commissions not to exceed 6 per cent on the basis of the average maturities of said equipment trust certificates.

Applicant alleges that because of deterioration and unserviceability, resulting from constant use, and also because of the increased demands of traffic, the equipment now owned by it and its

lessor and proprietary companies and used in the conduct of their business as common carriers, is not and will not be sufficient or adequate for the proper and efficient transportation of freight and passenger traffic over the operated lines of said Southern Pacific Company and its lessor and proprietary companies, and that in order to transport such traffic properly over such lines, it will be necessary for the Southern Pacific Company to acquire additional railroad equipment costing in the aggregate approximately \$2,238,083.26. In order to procure such equipment the Southern Pacific Company desires to enter into an agreement dated September 2, 1913, with Harry E. Richter and William L. Fry and the Commercial Trust Company, and a lease of such equipment from the Commercial Trust Company, of the same date, pursuant to such agreement, in substantially the form set forth in the printed copy of such proposed lease and agreement which are filed with the application and marked "Exhibit A."

The agreement provides, in effect, that Richter and Fry, hereinafter called the "vendors," are to deliver to persons designated by the Commercial Trust Company, hereinafter called the "trustee," the equipment which the Southern Pacific Company now desires to acquire, and which will hereinafter be referred to in greater detail. The agreement provides that the title to the equipment shall vest in the trustee. The trustee shall thereupon execute a lease of the equipment to the Southern Pacific Company. Upon receipt of the equipment and the execution of the lease to the Southern Pacific Company, the trustee will turn over to the vendors, Southern Pacific trust equipment certificates, Series B, not to exceed 90 per cent of the cost of the equipment. As an alternative, these equipment trust certificates may be turned over by the trustee to parties named by the vendors, upon deposit of the face value of said certificates. It is provided in the agreement that the Southern Pacific Company may, at stated times, after September 1, 1913, purchase the equipment.

The Southern Pacific equipment trust certificates are to be of a total issue of \$2,010,000, are to be in amounts of \$1,000 each, will bear a dividend at the rate of 4 1/2 per cent and will be due and payable in amounts of \$201,000 each year, beginning September 1, 1914, to and including the year ending September 1, 1923. The Southern Pacific Company, for a valuable consideration, unconditionally guarantees to the holder or registered owner of each of said certificates the payment of both principal and dividends. This guarantee is attached to each trust certificate. It is clear that it is, in effect, a note or promise to pay on the part of the Southern Pacific Company.

The lease between the Trust Company and the Southern Pacific Company refers to the agreement and then provides for the lease by the Trust Company to the Southern Pacific Company of the equipment which is the subject matter of this application. As the equipment is delivered by the trustee to the Southern Pacific Company, the latter is to pay in cash the difference between the cost price of the equipment and the face value of the equipment trust certificates issued against it. The lease is so drawn that this sum shall represent 10 per cent of the cost price, the balance, or 90 per cent, to be covered by the equipment trust certificates. Title to the equipment shall remain in the trustee until the Southern Pacific Company has completed the payment of principal and dividend on the equipment trust certificates, whereupon the title shall be transferred by the trustee to the Southern Pacific Company. The lease provides in part that the Southern Pacific Company may purchase the equipment at stated times after September 1, 1913, by paying the face value of the outstanding equipment trust certificates with a premium of 2 1/2 per cent, plus accrued interest, and other accumulations. The lease also provides that the equipment shall be lettered so as to show that the title remains in the trustee. The equipment trust certificates run for 10 years and all of the equipment will be paid for at least

by the end of that period.

The equipment which the Southern Pacific Company desires to acquire is as follows:

1. Six steel observation cars, to be used by the Southern Pacific Company and the Central Pacific Railway Company.
2. Thirteen steel combination baggage and postal cars, to be used by the Southern Pacific Company and the Central Pacific Railway Company and the Arizona Eastern Railway Company.
3. Thirty-four steel baggage cars, to be used by the Southern Pacific Company, the Central Pacific Railway Company, the Oregon and California Railway Company, the Houston and Texas Central Railway Company, the Galveston, Harrisburg and San Antonio Railway Company, and the Arizona Eastern Railway Company.
4. Sixty-three steel coaches to be used by the Southern Pacific Company, the Central Pacific Railway Company, the Galveston, Harrisburg and San Antonio Railway Company, the Houston East and West Texas Railway Company and the Arizona Eastern Railway Company.
5. Twenty steel chair cars, to be used by the Galveston, Harrisburg and San Antonio Railway Company, the Houston and Texas Central Railway Company and the Texas and New Orleans Railway Company.
6. Six steel diners, to be used by the Southern Pacific Company and the Central Pacific Railway Company.
7. Six steel buffet baggage cars, to be used by the Southern Pacific Company and the Central Pacific Railway Company.
8. Ten locomotive tenders, to be used by the Southern Pacific Company.
9. Three tank cars, to be used by the Arizona Eastern Railway Company.
10. One hundred box cars, to be used by the Arizona Eastern Railway Company.

The following equipment to be used by the Pacific Electric Railway Company:

- A. Ninety box cars;
- B. Sixty flat cars;
- C. Ten gondola cars;
- D. Ten stock cars;
- E. Twenty electric street cars;
- F. One hundred dump cars.

The Southern Pacific Company owns a majority of the capital stock of each of the foregoing railway companies. All of these companies operate either outside of the State of California, or partly outside and partly inside of the state, with the exception of the Pacific Electric Railway Company, a California corporation, whose mileage is located entirely within the State of California.

The testimony shows that all of the above mentioned equipment is necessary in the conduct of the business of the respective lines of railway on which it is to be used and that the price to be paid therefor is reasonable.

Applicant testified that for the fiscal year ending June 30, 1913, it had paid a six per cent dividend, amounting to \$16,360,344.30 upon 2,726,724.05 shares of its common stock, and that after the payment of all its interest and ~~xxx~~ other obligations and the aforesaid dividend, it had laid aside a surplus during the fiscal year ending June 30, 1913, of approximately \$25,962,690.

Applicant further testified that it would be necessary in order to obtain subscriptions for its said equipment trust certificates, to pay discounts and commissions not to exceed 6 per cent on the basis of the average maturities of its equipment trust certificates. It testified that the market for the sale of these certificates in New York at the present time is a favorable one, and that it is desirous of securing this Commission's speedy authorization.

Heretofore, on April 4, 1913, the Southern Pacific Company filed a similar application for authority to guarantee equipment trust certificates in the aggregate amount of \$10,120,000, being Application

No. 484, in which case this Commission on April 11, 1913, made its order granting the application in toto. Thereafter, on June 4, 1913, the Southern Pacific Company filed with this Commission Application No. 585, asking authority to issue its notes of the face value of \$30,000,000 for the purpose of making certain additions and betterments to its lines, which application was granted by this Commission in toto on June 7, 1913, three days thereafter. The equipment and other property to be used by the Southern Pacific Company in each of these two applications was to be used partly in interstate business and partly in state business. The Southern Pacific Company, however, made no segregation between these purposes, but asked the Commission to issue its authorization for the entire proposed issue in each case, which was done by this Commission in order to remove any possible doubt as to the authority of the Southern Pacific Company to issue its notes or guarantees, even though the applications included equipment and other property to be used both within and without the State of California. The Southern Pacific Company in neither case questioned the authority of this Commission and in each case asked that the Commission's authority cover the entire issue, and in each case the Commission's order did so for the purpose of assisting the Southern Pacific Company. While under the provisions of Section 57 of the Public Utilities Act, fees were collected on the entire authorized issue, the Commission was helpless to do otherwise, for the reason that the Southern Pacific Company made no segregation so that this Commission could ascertain what portion of the property to be acquired would be used solely in the State of California.

In its present application, the applicant has inserted paragraph 15, as follows:

✓ "In as much as Section 52 of the Public Utilities Act of this State provides that no evidence of indebtedness, payable at periods of more than 12 months after the date thereof for the acquisition of property or for the improvement or maintenance of its service shall be issued by any public service corporation until such public service corporation shall first have secured from this Commission an order authorizing such issue in accordance with the provisions of such statute and in as much as part of the equipment provided for in said lease and agreement will be used upon

lines of railroad within this state and subject to the jurisdiction of this Commission, and it is desirable that no claim shall hereafter be made that the Trust Certificates, or any of them, provided for in said lease and agreement and the payment of which is to be guaranteed by your petitioner, constitute evidence of indebtedness which are void within this state because not authorized by this Commission, your petitioner files this petition in order that it may secure this Commission's approval of the said lease and agreement and authorization of the issuance of such Trust Certificates with the guaranty of the payment thereof by the Southern Pacific Company endorsed upon each of such certificates as provided in the lease and agreement filed with this petition."

"This application is made without prejudice to the cause of action set forth in the complaint filed by petitioner against the members of this Commission and others in the United States District Court for the Northern District of California and now pending therein."

In view of this statement for the first time questioning formally the jurisdiction of this Commission in such a proceeding before it, it becomes necessary to give consideration to the question of this Commission's jurisdiction.

Section 52 of the Public Utilities Act provides in part that no public utility shall issue any stocks or stock certificates or bonds, notes or other evidences of indebtedness, with certain exceptions, without having secured from this Commission an order authorizing such issue. As the guarantee to be endorsed by the Southern Pacific Company upon its equipment trust certificates is "a note or other evidence of indebtedness," it seems clear that in so far as the nature of the indebtedness is concerned, the case falls within the provisions of Section 52 of the Public Utilities Act. This Section, however, must be construed in connection with Section 35 of the Public Utilities Act, reading as follows:

"Neither this act nor any provision thereof, except when specifically so stated, shall apply or be construed to apply to commerce with foreign nations or commerce among the several states of this Union, except in so far as the same may be permitted under the provisions of the Constitution of the United States and the acts of Congress."

That these two sections must be construed together is elementary. Consequently, I am of the opinion that this Commission has no authority over the car equipment trust certificates involved in this proceeding in so far as their proceeds are to be used to purchase equipment which runs "among the several states of this Union, except

in so far as the same may be permitted under the provisions of the Constitution of the United States and the acts of Congress."

I am of the opinion that the assumption by this Commission of jurisdiction over the issue by a foreign corporation of equipment trust certificates in a foreign state, the proceeds whereof are to be used to purchase equipment used exclusively in other states or moving in interstate commerce would be beyond its powers, under the provisions of Section 85 of the Public Utilities Act, which section reaffirms the well established principles of law governing commerce among the several states and with foreign nations.

On the other hand, it seems equally clear, that with reference to the equipment, if any, which is to be used solely and exclusively in the State of California, this Commission has undoubted jurisdiction, particularly in the absence of action by the ~~XXXXXX~~ Federal Government in the matter of the issue of stocks, bonds and other securities of common carriers. This is not a case of possible conflict with Federal regulations, such as exists with reference to safety appliances, but a case in which the Federal Government has taken no action whatsoever, and in which the equipment is used solely in the State of California, and largely, if not predominatingly for purely state business.

The Commission accordingly asked the applicant to make a segregation, if possible, so as to show what portion, if any, of the equipment which it is now desired to purchase is to be used exclusively within the State of California. The testimony, in response to this request, shows that the equipment to be purchased for all the lines of railway, other than the Pacific Electric Railway Company, is to be used either exclusively in other states or in journeys crossing state lines. While certain of the equipment to be acquired for the Southern Pacific Company and the Central Pacific Railway Company will at times be used entirely within this state, it appears that in general it will be used in interstate runs and that none of it will be used exclusively within this state.

On the other hand, the testimony shows that the equipment to be used by the Pacific Electric Railway Company is to be used exclusively within this state. The only doubt in the matter exists with reference to the box cars, and with reference to these, applicant's witness testified that it was unlikely that any of them would go out of the state. With reference to the flat cars, he testified that the chances for their going out of the state were even less than is the case with reference to the box cars, while the other classes of cars will all of them remain exclusively within this state.

I am accordingly of the opinion that this Commission has jurisdiction over this application in so far as affects the guarantee by the Southern Pacific Company of trust certificates to be used in purchasing the cars to be used by the Pacific Electric Railway Company and that with respect to the remaining portion of the application, this Commission has no authority.

I expressed a desire at the hearing to prepare the order in this case in such form as to be sure to cause no embarrassment to the applicant. Such embarrassment might follow if this Commission dismissed a portion of the application and if the bankers who are to loan the money thought that the Commission might, nevertheless, have jurisdiction with reference thereto or to any portion thereof. The applicant accordingly requested that the Commission issue its authorization with reference to the entire contemplated issue of certificates. In order to in no way embarrass applicant, I recommend that this course of procedure be adopted, but in so doing it should be distinctly understood that this Commission is not trying to exercise power which does not belong to it and that it is not trying to collect fees in excess of those to which it is properly entitled, but that it is animated by a desire to throw no stumbling blocks in the way of the Southern Pacific Company, and to be of all possible assistance to that company in its legitimate financing.

While I shall recommend the granting of the application in toto, I do not believe that this Commission should collect a fee in excess of that which under the provisions of Section 57 of the Public Utilities Act, is due on that portion of the certificates which are to be ~~xxxx~~ used in paying for equipment over which this Commission clearly has jurisdiction. I shall accordingly recommend that the fee be limited to a fee on the Pacific Electric Railway Company equipment. While I do not believe that it is necessary to secure this Commission's consent for the execution of the lease of the equipment, or for authority to enter into the agreement, apart from the guarantee of the certificates, I shall nevertheless recommend that, in accordance with the request of the Southern Pacific Company, the order cover this feature of the application, as well as the others, so that there may be no doubt as to whether or not the Southern Pacific Company has secured the complete necessary authorization.

I recommend the following form of order:

C O R D E R.

SOUTHERN PACIFIC COMPANY having applied to the Railroad Commission for an order authorizing it to enter into an agreement with Harry E. Richter and William L. Fry and Commercial Trust Company of Philadelphia, under date of September 2, 1913, and also a lease of railroad equipment from Commercial Trust Company of Philadelphia, dated September 2, 1913, a copy of which proposed agreement and lease are filed with the application herein and marked "Exhibit A;" and also for an order of this Commission authorizing the guarantee by said Southern Pacific Company of its car equipment trust certificates, Series B, of the aggregate principal amount of two million and ten thousand dollars (\$2,010,000), bearing dividends at the rate of four and one half (4½) per cent per annum, payable on the first day of March and the first day of September of each year, said certificates to be paid in ten (10) annual installments, payable respectively on

September first of each year from September 1, 1914 to September 1, 1923, inclusive, a form of said equipment trust certificates and of the guarantee of the Southern Pacific Company thereon being contained in said copy of agreement, and also authorizing said company, in order to obtain subscriptions for said equipment trust certificates, to pay discounts and commissions not to exceed six (6) per cent on the basis of the average maturities of said equipment trust certificates; and a public hearing having been held on said application, and it appearing to this Commission that the equipment to be obtained by the Southern Pacific Company under the terms of said lease and said agreement is reasonably required in the conduct of its business, and that the proceeds of said car equipment trust certificates are not reasonably chargeable to operating expenses or to income,

IT IS HEREBY ORDERED that said application be and the same is hereby granted, subject to the following conditions:

1. Southern Pacific Company shall keep separate, true and accurate accounts showing the receipt and application in detail of the proceeds of said car equipment trust certificates, in so far as they affect the equipment to be used by the Pacific Electric Railway Company exclusively within the State of California, and on or before the 25th day of each month, shall make a verified report to this Commission stating the sale or sales of said equipment trust certificates, with the terms and conditions thereof, the moneys realized therefrom and the use and application of such moneys, all in accordance with this Commission's General Order No. 24, which order, but only in so far as applicable, is made a part of this order.

2. The authority hereby given shall become effective only when the Southern Pacific Company shall have paid the fee prescribed in Section 57 of the Public Utilities Act, as amended, which fee shall be calculated only on the Pacific Electric Railway Company equipment and which amounts to four hundred and eight dollars (\$408.00).

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 13th day of September, 1913.

John W. Washburn

H. H. Loveland

W. H. Gordon

Max Fisher

Edwin O. Edgerton

Commissioners.