

ORIGINAL

Decision No. 34842

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application  
of

THE PACIFIC TELEPHONE AND TELEGRAPH  
COMPANY, a corporation,

Application  
No. 24414

for an order authorizing it to issue  
and sell 656,250 of its common shares  
of the par value of \$100 per share and  
aggregating \$65,625,000.

ALFRED SUTRO, for Applicant

RILEY, COMMISSIONER:

O P I N I O N

This is an application for an order of the Railroad Commission authorizing The Pacific Telephone and Telegraph Company to issue and sell 656,250 shares of its common stock, of the par value of \$65,625,000, at not less than the par value thereof, for the purpose of reimbursing its treasury for moneys actually expended, since October 31, 1922, from income and from other moneys in its treasury, and to offer said 656,250 common shares to the holders of its outstanding preferred and common shares for subscription, at the rate of \$100 a share, in the proportion of one share for each four shares of preferred and/or common shares standing in the

name of each shareholder of record.

As of July 31, 1941, the company reports its authorized and outstanding capital stock at 2,625,000 shares of the par value of \$100 each and of the aggregate par value of \$262,500,000 of which 1,805,000 shares were common shares and 820,000 preferred. Recently the company has increased its authorized capital stock to 3,281,250 shares of the par value of \$100 each, divided into 2,461,250 common shares and 820,000 preferred shares.

In making the present application for permission to issue the additional common shares of stock, the company has filed its balance sheet showing assets and liabilities as of July 31, 1941, as follows:

Assets

Telephone plant		\$315,731,580.43
Miscellaneous physical property		970,162.42
Investments in subsidiary companies		157,704,927.39
Other investments		597,218.88
Sinking funds		325,000.00
Current assets -		
Cash and special deposits	\$1,622,996.23	
Working funds	66,806.48	
Notes receivable	7,424.35	
Accounts receivable	8,001,166.33	
Materials and supplies	<u>4,838,788.95</u>	14,537,182.34
Deferred charges		<u>5,840,801.83</u>
Total assets		<u>\$495,706,873.29</u>

Liabilities

Common stock		\$180,500,000.00
Preferred stock		82,000,000.00
Funded debt		54,568,000.00
Notes sold to trustee of pension fund		9,749,171.36
Advances from The American Tel. & Tel. Co.		45,400,000.00
Current and accrued liabilities -		
Advance billing	\$1,546,102.18	
Accounts payable	6,693,626.66	
Accrued liabilities	<u>6,360,650.48</u>	14,600,379.32
Deferred credits		405,104.36
Depreciation and amortization reserves		98,458,555.19
Unappropriated surplus		<u>10,025,663.06</u>
Total liabilities		<u>\$495,706,873.29</u>

The amounts reported as advances from The American Telephone and Telegraph Company consist of one-day unsecured 5% notes issued over a period of time from September 16, 1940 to July 31, 1941.

The company reports that between October 31, 1922 and July 31, 1941, it expended for property, for the retirement of bonds and advanced to subsidiary companies, the sum of \$85,355,570.11 in excess of proceeds from the issue of stock and notes, and advances from The American Telephone and Telegraph Company. This amount was determined as follows:

Increase in telephone plant accounts	\$201,486,054.33
Increase in investment in securities of subsidiaries	118,236,001.54
Increase in advances to subsidiaries	7,620,754.12
Increase in other investments	<u>2,607,712.53</u>
Increase in miscellaneous physical property	773,009.57
Increase in cash deposited in sinking funds	198,823.32
Decrease in funded debt	<u>8,630,000.00</u>
	\$334,936,930.35
Less -	
Proceeds from sale of stock	\$194,432,188.88
Pension fund note	9,749,171.36
Advances	<u>45,400,000.00</u>
	<u>249,581,360.24</u>
Balance	<u>\$ 85,355,570.11</u>

According to the testimony of S. W. Campbell, applicant's vice president and general auditor, the \$85,355,570.11 was obtained from various sources, or is represented by adjustments, as follows:

From surplus earnings	\$ 4,860,143.93
From reserves	69,054,244.08
From current items	4,784,742.39
From deferred items	5,389,953.60
From adjustment of intangibles	<u>1,266,486.11</u>
Total	<u>\$85,355,570.11</u>

Although the company now asks permission to issue stock to reimburse its treasury, the record shows that it is its intention to use the proceeds, after reimbursement, to pay advances from The American Telephone and Telegraph Company, which advances were reported in the total amount of \$45,400,000 at the date of the balance sheet. It is expected that the advances will approach or exceed the par value of the stock proposed to be issued by the time such issue is completed. Applicant proposes to use the proceeds not needed to pay said advances for general corporate purposes.

The record shows that the company is in need of additional capital funds to improve its cash position, to pay indebtedness and to finance the cost of additions to its properties and investments, and that it has concluded that this need can be met more advantageously through the issue and sale of shares of common stock rather than bonds or some other form of security.

In testifying in support of the plan to issue shares of common stock at this time, M. R. Sullivan, the company's first vice president, estimated that at the close of this year, assuming the additional shares issued, the total outstanding capitalization would aggregate \$397,350,000, consisting of various classes of securities and obligations in relative proportions as follows:

<u>Item</u>	<u>Amount</u>	<u>Per cent</u>
Bonds	\$ 54,568,000	13.73
Advances	-	-
Pension notes	14,657,000	3.69
Preferred stock	82,000,000	20.64
Subtotal	151,225,000	38.06
Common stock	246,125,000	61.94
Total	<u>\$397,350,000</u>	<u>100.00</u>

While the proportion of common stock might appear to be relatively high, he pointed out that the company's debt is growing rapidly, and that following the issue of common shares, as now proposed, the debt proportion will again start to climb, due to the continuing necessity of borrowing additional sums from time to time for new construction. It is reported that with the present rate of growth and with the construction program outlined for 1942, the company will be called upon to borrow approximately \$32,000,000 during the coming year.

Thus faced with the constant need for new capital, it is urged by Mr. Sullivan that the company should take advantage of the opportunity to obtain common stock money, which it now has, and to reserve its borrowing capacity for times when money cannot otherwise be procured. It appears to be the opinion of the witness that if the company now reduces its borrowing capacity, presumably through the issue of bonds or some other interest bearing security instead of common stock, it will be impossible for it to obtain new capital on reasonable terms at some future date when interest rates, in general, may be higher.

It is, of course, in the public interest for a utility, looking toward the future, to maintain a capital structure sufficiently flexible to enable it to raise funds when and as needed and to meet its requirements over a continuing period of time, under differing economic conditions. For this reason, in this particular case, I believe that upon the showing made, the Commission is warranted in making an order authorizing the issue of the shares of stock as requested.

I believe, however, that applicant should be placed upon notice that the Commission does not, and will not, regard the dividends on the common stock as determining or fixing the rate of return the company should be allowed to earn in the event the Commission is called upon or finds it desirable to review its rates.

I herewith submit the following form of order:

### ORDER

The Pacific Telephone and Telegraph Company having applied to the Railroad Commission of the State of California for an order authorizing the issue of \$65,625,000 par value of common stock, 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 through the issue of said stock is reasonably required for the purpose specified herein, and that the expenditures for such purpose are not, in whole or in part, reasonably chargeable to operating expenses or to income,

IT IS HEREBY ORDERED that The Pacific Telephone and Telegraph Company be, and it hereby is, authorized to issue and sell, on or before December 31, 1941, at not less than \$100 a share, 656,250 shares of its common capital stock of the aggregate par value of \$65,625,000, and to use the proceeds for the reimbursement of moneys actually expended, from income, and from other moneys in its treasury not secured by or obtained from the issue of securities, for the acquisition

of properties, the investment in securities of and advances to subsidiaries and the retirement of bonds prior to August 1, 1941, provided, said proceeds be used to pay indebtedness due The American Telephone and Telegraph Company or for such other purposes as the Railroad Commission will hereafter authorize.

IT IS HEREBY FURTHER ORDERED that The Pacific Telephone and Telegraph Company may offer said 656,250 shares of common capital stock to the holders of its outstanding preferred and common shares, for subscription, at the rate of \$100 a share, in the proportion of one share for each four shares of preferred and/or common shares standing in the name of each shareholder of record.

The authority herein granted is subject to the following conditions:

1. The Pacific Telephone and Telegraph Company shall keep such record of the issue and sale of the stock herein authorized, and of the disposition of the proceeds, as will enable it to file, on or before the 25th day of each month, a verified report as required by the Railroad Commission's General Order No. 24-A, which order, insofar as applicable, is made a part of this order.

2. The authority herein granted will become effective upon the date hereof.

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 7<sup>th</sup> day  
of October, 1941.

W. Baker  
Ray L. Cheney  
Justus J. Calmer  
Frank C. Stevenson  
Robert W. Hulse  
Commissioners.