rural population, was far from the peak of agricultural development.

At the close of the period agricultural, forest, and mine products provided 72% of the tonnage and 51% of the freight revenue; manufactured articles 23% of the tonnage and 38% of the revenue; animals and animal products 5% of the tonnage and 11% of the revenue. At the close of the period the company was receiving from other lines considerably more tonnage than it was delivering.

Because of the foregoing conditions the engineers felt that any attempt to build up estimates of the future by detailed studies of particular districts or particular lines of business would involve too many assumptions of uncertain elements. Changes in particular lines of business might in some years offset changes in other lines. Favorable weather conditions might result in large crops in certain parts of the territory at the same time that crop failures occur in other sections of the territory, and favorable business conditions in the manufacturing centers of the Eastern District might occur simultaneously with crop failures in the Western District and vice versa.

In reviewing the growth of the territory over the past 25 years the engineers saw that consideration must be given to the fact that during the first ten years of the present century occurred the major growth of the Western District, and that developments in that district after 1934 were more likely to correspond with those which began to appear in the Eastern District

at least 25 years ago. The influence of post-war conditions had also been reflected over a large portion of the company's territory in abnormal agricultural and banking conditions during the last few years, as has been pointed out previously in this chapter. Yet general business conditions had been fairly good even in sections which suffered most severely from the agricultural deflation of 1921 as could be seen at the close of 1924 from the increasing number of automobiles in states such as Minnesota, North Dakota, South Dakota, and Montana, by building permits, and by similar indices.

With the continued improvement in the economic position of the farmer and consequent improvement in business as a whole through the resulting enhancement in the farmer's purchasing power, with further diversification and intensification of agriculture, and with the freeing of credit which had occurred during 1923 and 1924 even in the most depressed sections of the Northwest, the engineers concluded that there should be a steady increase in the business of the territory.

The engineers in their investigation, studied the volume of freight movement on the lines of the company over the past 25 years and compared it with the corresponding figures of other roads operating in the same territory, and found that the rate of growth in freight traffic density had been on the whole even not only on the company's lines but on competitive lines in the territory. In considering the future possibilities of the territory from the standpoint of freight revenue the engineers came to

the conclusion early in 1925 that during the next ten years the growth in traffic density would continue on the average at the same rate as over the preceding 25 years, since it was evident that the diversification of the business of the territory and the wide extent of the territory had in the past resulted in averages which reduced the apparent peaks of prosperity and leveled the valleys of depression which appeared so striking in the consideration of particular localities or individual lines of activity whether with respect to agriculture, forestry, manufacturing, or mining. This rate of growth projected ahead into the immediate future would result in an average increase of 35% over the next ten years in freight traffic revenues at present rates and with the mileage as now constituted(1924).

As pointed out previously, the engineers looked upon 1920 and 1924 as a return or nearly a return to normal as far as the road was concerned. Rapid expansion from depression had already taken place. In the forecast above no immediate rapid short time expansion in business was promised. Long time factors were forecasted to produce an increase of 25% in freight traffic revenues under certain assumptions (present rates and present mileage). Under these assumptions and others including the adoption of their recommended increased rates of depreciation, the carrying out of their recommended program for future additions and betterments, and the increase in freight revenues of 25% as predicted, the amount available for interest on the company's bonds, notes, equipment trusts, unfunded debt, and the Terre Haute obligations would be $17,250,000 in 1925, $30,150,000 in 1930, and $39,100,000

in 1934. By the way, each figure for these three years represented an estimated average for a period of years. In 1923 and 1924 the amounts available for interest on these obligations, after the figures from the company's records were adjusted to the views of the engineers as to depreciation on equipment and other things, were $18,816,000 and $17,529,000, the actual interest on these obligations amounted to $20,950,000 and $21,751,000, and therefore the net income deficit amounted to $2,134,000 and $4,222,000 respectively. Another deficit of over $3,000,000 was predicted in 1925 if the interest charges remained about the same as in 1923 and 1924. But the engineers' future program of additions and betterments which they recommended as necessary for the future efficient operation of the lines called for proposed new equipment trusts and new money requirements which would increase future interest charges at the then present rates, $2,143,000 in 1925, $5,618,000 in 1930 and $7,545,000 in 1934. In other words it would be a number of years before the present (1924) interest charges, which would be paid when due to avoid receivership, would be covered assuming no maturities or the ability to refund on the same basis, neither of which could be assumed. Obligations in the hands of the public aggregating $48,336,000 were to mature in 1925. This amount consisted of equipment obligations, $2,207,000; European Loan of 1910, $11,532,000; gold 4's of 1925, $35,100,000; and a Terre Haute note, $167,000. There were also heavy maturities in the next nine years. The obligations in the hands of the public maturing in the next ten years from 1925 to 1934 inclusive aggregated

at the close of 1934, $236,358,000. In addition the company held $1,405,181 of the bonds maturing in this period in its insurance fund. Incidently, the figures in this paragraph are accurate only in thousands.

In short, the real problem of the St. Paul at the close of 1934 was not merely how it was to meet the 1935 maturities of nearly 50 millions, but that, in the face of the past earnings, it had also to meet the heavy maturities of the 10 year period 1935 to 1934 inclusive as well as finance much needed additions and betterments.

The company needed an impossible and even inconceivable lucky break in an economic sense to successfully meet its 1935 financial problems and still carry on its operations as it had been doing. Then after that it needed a series of lucky breaks to meet its financial problems over the ten year period in addition to all that which was promised by the engineers.

The outlook for the future as predicted by the engineers was a bright one but not sufficiently bright for a railroad system with a financial structure like that of the St. Paul.

CHAPTER X

THE FORMULATION OF THE NEW FINANCIAL PLAN.

During the closing period from 1925 to 1928 to be reviewed in this and the three subsequent chapters the inevitable happened. The company had built up a huge and complex financial structure and the subsequent failure of traffic to bring in sufficient earnings to support that financial structure could have only one result. The St. Paul went into receivership in March, 1925, and remained under the receivers' control until early in 1928. The background of the receivership has been brought out in previous chapters but more especially in the two preceding chapters. This need not be repeated in this chapter although it was the subject of much investigation, speculation, and discussion during the years now under review. During the receivership the financial structure of the road was reorganized. Also during this period some much-needed important physical changes in the way of additions and betterments took place in properties. Many of these were made possible by the receivership. The reorganization and the events connected therewith and these changes in the property are the important characteristics of this period. This chapter will be concerned primarily with a discussion of these two characteristics - especially the former.

A change in the order in which the material is taken up in this chapter from the order followed in the previous chapters will be noted. The financial events connected with the reorganization stand out so prominently as against other matters having to do with physical changes in the property that the writer has seen fit to take up the purely financial matters first and the physical changes brought about in the property second.

The events immediately connected with and leading up to the receivership are interesting.[1]

As early as 1923 Mr. Charles E. Mitchell, president of the National City Bank and the National City Company, the latter one of the reorganization managers, became skeptical of the future of the St. Paul. He took the junior bonds (subsequent to the General Mortgage) off the daily lists which went to the salesmen. He had previously even recommended that the junior bonds held by the bank be sold. However, due to William Rockefeller's stand they were not sold until after the latter's death in 1922. In 1923 several of the large insurance companies which had been watching the situation closely sold as many of the junior bonds as the market would absorb at prices satisfactory

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1. Unless otherwise stated, the sources of material for this discussion of the events prior to the receivership are Statement of H.E.Byram, President of the C.M.& St.P.Ry.Co., before the Interstate Commerce Commission, Dec.1,1925, p.28 and 131 I.C.C., p.653.

to these companies.

As pointed out in the previous chapter, the road's 1933 requirements were met by temporary loans from the banks. These loans were liquidated in 1934 by the sale of $14,000,000 of 10 year 6% bonds secured by $30,000,000 of first mortgage bonds. At the time of this financing the company furnished the bankers with a statement of the expected earnings for 1934. As the year went on this statement proved to be far too optimistic. The year, as pointed out previously, ended with a large deficit with inadequate rates of depreciation being charged.

In June, 1934 Byrne requested four of the directors to cooperate with him as a special committee for the purpose of developing, if possible, some practical plan to meet the bonds maturing in 1935 (nearly $50,000,000). Many meetings were held during that summer. The committee formulated some plans and met the bankers in August, 1934 and again in December, 1934, when the unfavorable results for the year were apparent. Several of the plans considered involved an effort to secure a voluntary exchange of securities on the part of the holders of the 1935 bonds. This would amount to an extension. The bankers stated that there would have to be a down payment, and finally 10% of the bonds would have to be paid in cash. The bankers doubted whether the government loans could be extended and additional loans secured. They questioned whether additional collateral could properly be given. The bankers apparently had in mind the experience of the New Haven in securing a short extension of 4% bonds maturing in 1932. Of

the matured bonds 10% were paid in cash and the interest on the balance was raised to 7%. About 10% of the holders of the New Haven bonds refused to extend and were paid in full with money borrowed from the government. A thorough canvass was made here and abroad to ascertain the holders of the 1925 maturities of the St. Paul. About 70% of the holders were located. To secure any extension of this kind, it would be necessary to assure the extended bondholders that he would get his interest during the extension and his principal at the extended maturity. The value of the company's securities which could be offered in exchange for the 1925 maturities had by this time (December, 1924) become so depreciated that it seemed unreasonable to expect that enough of the 1925 security holders could be persuaded to take new securities for their holdings to warrant the belief that such an exchange could be made effective. There would, as usual, be some holders who would not agree to make the exchange, and there were not sufficient assets in the company's treasury to produce the cash that might be necessary to satisfy any considerable percentage of these dissenters. Therefore the bankers and management doubted the possibility of a voluntary exchange. Some critics of the whole reorganization and the procedure connected therewith seemed to have doubted the wisdom of this view. They stubbornly, at this time and subsequently, insisted that the receivership could have been avoided by a voluntary exchange which, they claim, would have been successful.

But, as was pointed out in the previous chapter, there were heavy maturities coming in the next nine years to 1934. Over $27,000,000 in funded debt was due in 1927; over $32,000,000, in 1930; over $53,000,000, in 1932; and over $57,000,000, in 1934.[1] The maturities for the other years were smaller in amount.[2] Unless provision could be made for these maturities, taking care of the 1925 maturities would afford only temporary relief.

Consideration seems to have been given during these months to the possibility of issuing new securities to meet the refunding of these maturities. The commission was asked whether they would approve of the release of the $18,000,000 General Mortgage 5% Bonds pledged as collateral for a loan from the government through a substitution of the equivalent value of the company's General and Refunding Bonds. The commission promised approval if the consent of the Secretary of the Treasury were obtained. The board however decided that since the company was not even earning its fixed charges, and had no marketable assets other than these General Mortgage Bonds, a request for the release which would only postpone and not permanently solve the financial difficulties would not be justified.

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1. 131 I.C.C., p. 628.
2. The indebtedness of the company maturing from January 1, 1925 to December 31, 1934 consisted of $28,259,500 equipment obligations (out of a total of $32,700,000) $200,935,315 bonds (out of a total of $433,338,115) and $187,400 notes (out of a total of $187,400) or a total of $238,382,315 (out of a total of $466,103,515). These were the amounts in the hands of the public exclusive of the issues in the insurance fund - Coverdale & Colpitts, p. 212.

The board could not see the possibility of refunding on a large scale. Even if refunding were possible the rate of interest on the new securities would have to be higher than on the old ones, thus increasing instead of decreasing the company's financial load. With the liquid assets used up in refinancing proceedings there would be no reserve funds left with which to meet the deficiencies which might accrue in poor years between the net income and fixed charges. Receivership would result later to the company after the exhaustion of its liquid assets.

At the conference with the commission on October 17, 1924 in which the commission promised its approval of the release of the $18,000,000 General Mortgage Bonds, Byram was given assurance that the government loan due in 1927 could be renewed for five years in order to get it out of the way of the short term financing to meet the 1925 maturities. Byram also brought up the question of a possible loan from the fund created under the "recapture" (of excess earnings) clause in the Transportation Act of 1920. Since a comparatively small sum had been paid into this fund on account of the excess earnings and this paid only under protest, the commission said no funds were available from this source.[1]

Byrne also had a conference with the Secretary of the Treasury. The latter advised him that although the government was desirous of being helpful in avoiding a receivership, there was no authority under the law whereby any financial aid could be given

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1. Chronicle, vol.120, p. 2397.

by the government.

In a further effort to improve the credit of the St. Paul an effort was made to reduce the interest rate on loans made by the government to railroads from 6% as fixed by law to 4 1/2%. The St. Paul was then carrying loans with the government aggregating $55,000,000 at 6%. Congress was asked to pass legislation reducing the rate on these loans from 6% to an amount not exceeding the cost of such money to the government, approximately 4 1/4%. Byram appeared before the Senate Interstate Commerce Committee in January, 1925 in behalf of the bill proposed by Senator Gooding of Idaho, and pointed out the difficulties of the St. Paul and reduction of approximately $1,000,000 per year in the road's interest charges if the legislation were passed. This amount really represented that much profit to the government above the cost of government borrowing at that time. However, Congress adjourned without passing the desired legislation.

Therefore, Byram was satisfied in his own mind that every possible way of meeting the situation and avoiding a receivership was considered by the company's bankers and its board of directors.

At the December meeting of the special committee and the bankers, referred to above, the latter suggested that an independent study of the property be made by independent engineers. Coverdale & Colpitts were recommended by the bankers. The appointment of Coverdale & Colpitts was authorized at a special meeting of the directors on January 7, 1925.[1] The resolution recites that

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1. Ibid., p. 328. Railway Review, January 24, 1925, p. 207.

the action was taken at the request of the company's bankers. The bankers prepared for the engineers a questionnaire of problems for them to answer in their investigation. Their report covered more ground than that called for by this questionnaire. Their examination of the road was a thorough one. Their report went into the history of the road's difficulties, brought out the physical condition of the property, recommended an increased schedule of rates of depreciation as well as a future program of betterments and additions to 1934, contained an estimate of earnings up to 1934 on the assumption that the recommendations were adopted by the company, contained a digest of the various mortgages in detail existing on the property, brought out the fact that future earnings were to be inadequate to support the existing financial structure on the assumptions, and concluded with the statement that "a readjustment of the financial structure of the company is necessary."[1] This of course was a virtual recommendation for receivership. In January, 1935 Mitchell definitely reached the conclusion that a receivership was inevitable. About the end of February the bankers, some of the large bondholders like the Metropolitan Life Insurance Company, and certain directors of the company were aware of the nature of the adverse report which Coverdale & Colpitts were to make soon. On March 3 a preliminary oral report was made to the special committee by Colpitts. It seems as though by this time others besides Mitchell now had decided that a receivership was inevitable. The report of the engineers was

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1. Coverdale & Colpitts, p. 531.

finally submitted in completed and printed form to Byrne on March 18, 1935. This report has been referred to a number of times previously in this history. Ostensibly Coverdale & Colpitts were retained by the railroad; as an actual fact they were working for the bankers, who prepared the questionnaire for them, as previously pointed out. The board called on the company's executive and financial officers for a forecast of the company's probable earnings and expenses for a ten year period into the future. Their estimates indicated results similar to those reached by Coverdale & Colpitts.

Now according to the findings of the commission, most of the directors and the board itself had virtually ceased to function in January, 1935. The executive management, of course, was helpless. The bankers informally assumed control it seemed. Only a few knew the real situation - a few of the directors, the bankers, and some of the large bondholders. The idea seemed to be that the financial situation made further progress hopeless and that there was no use of informing the security holders or inviting them to determine for themselves what action, if any, should be taken or attempted. The counsel for the bankers prepared as early as January the pleadings necessary to institute receivership proceedings. Mr. F. S. Jameson, president of the Globe & Rutgers Fire Insurance Company, representing a large amount of junior bonds, still tried to interest Mr. Jerome J. Hanover of Kuhn, Loeb & Company in forming a protective committee to facilitate the extension of the maturing bonds. His efforts were discouraged. Later in the

receivership proceedings, he claimed that the receivership which followed was unnecessary and could have been avoided by short term financing and a voluntary extension of the maturing bonds.[1] Toward the end of February, Hanover definitely took charge of the situation. He began to organize security holders committees to represent the different classes of securities. These committees were to ultimately represent the majority of the securities to be disturbed in the coming reorganization. He first asked the president of the Mutual Life Insurance Company to serve as chairman of the bondholders' committee. The latter declined and suggested Mr. F. H. Ecker, vice president of the Metropolitan Life Insurance Company. The latter was appointed. Hanover then asked Mr. Mortimer N. Buckner and Mr. Donald C. Geddes to become chairman of the preferred stock and common stockholder committees respectively. They accepted. Both were at the time directors of the road. Hanover and Mitchell were made members of the bondholders' committee.

With the exception of these two, the members of this committee represented large bondholders. Outside the chairmen of the two stockholding committees, the members of these two committees represented no substantial stock interest. The two chairmen represented the Harkness holdings, the large single stock interest to be mentioned shortly. The others were selected for their prestige in person and position to assure the success of what was to follow. Hanover inquired of Mr. Potter, who had retired on

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1. Chronicle, vol. 123, p. 1110.

February 20, 1925 from the Interstate Commerce Commission, as to his availability to act as receiver. Counsel for the bankers conferred with New York counsel for the railroad and revised and perfected the drafts of receivership papers. The bankers' counsel communicated with associate counsel in Chicago so that the latter might ascertain if a district judge would be available on a certain date and to advise him as to the wishes of the company and the bankers as to the personnel of the receivers. The protective committees had been completely organized on March 16 and 17. The railroad people in Chicago secured as a friendly creditor a coal operator with whom it had had large dealings. On March 17 the road's board of directors approved formally the institution of the receivership proceedings. On March 18 the friendly creditor filed a bill in equity.

The Binkley Coal Company, this friendly creditor, requested a receivership before Judge James H. Wilkerson of the United States District Court for the Northern District of Illinois at Chicago. There was $125,000 owing the coal company for supplies for which payment was demanded and refused. At the time, the huge indebtedness and the recent inadequate earnings of the company were pointed out. It was pointed out also that on June 1 the company would be unable to meet the $11,831,515 four percent 15 year European loan bonds of 1910 and the $35,100,000 four percent gold bonds due on that date.[1] Furthermore, on April 1 semi-annual

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1. These amounts were in the hands of the public, exclusive of the insurance fund.

interest charges aggregating $989,503 on $43,088,000 General and Refunding 4 1/2's, Series A, was payable. The company would be unable to meet these April and June obligations. It was also pointed out that the company had outstanding floating indebtedness for materials and supplies which were overdue with creditors pressing for payment. The company was unable to provide for these. It was also pointed out that the company's inability to comply with the rules of the commission would subject it to heavy fines and that its failure to pay its regular obligations in respect to traffic balances, hire of equipment, rentals, etc. would still further reduce its revenues.[1]

The directors then made a frank statement of these difficulties to the public going into the history of these difficulties and pointing out the heavy maturities facing the road in the next ten years.[2]

On the same day as the bill was filed, March 18, 1935, Judge Wilkerson appointed Messrs. H. F. Byram, Mark W. Potter, and F. J. Bruntage as receivers. Byram was the president of the road; Potter was a member of the Interstate Commerce Commission for four and a half years. He had resigned recently from that body. He was familiar with railroad conditions in the east. Bruntage was a lawyer in Chicago. Previously he had been attorney general of the state. He was familiar with conditions in the west.[3]

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1. Chronicle, vol.130, p.1410. Railway Review, March 31, 1935, p.585.
2. Chronicle, vol.130, p.1410.
3. Ibid., p. 1455.

Now the commission claimed, as pointed out, that the bankers informally assumed the actual control of the road. It found that the directors lost control of the property. For months prior to the receivership they appeared to the commission to be impotent. It was an ideal situation for the bankers to control. This, the commission found, they promptly did, arranged all the details, fixed up the committees favorably to themselves, put themselves on the bondholders' protective committee, and constituted themselves reorganization managers, as will be pointed out shortly.

Why was it an ideal situation to control? Why did the directors lose control? Surely this situation was startling. The commission found that for many years there were four large stockholding interests in the St. Paul which undoubtedly, for all practical purposes, controlled it. Three out of the four had been sold out by the time the receivership materialized. Nevertheless the representatives of these four interests remained on the board. The late Mr. William Rockefeller held at one time 150,000 shares. His interests were disposed of partly in 1888 and partly in 1884. The second large holding was that of Mr. J. Ogden Armour who held at one time 125,000 shares. The Armour holding had been liquidated three or four years prior to the receivership. The third large block was held by the George Smith interests in England. The Smith holdings consisted of approximately $20,000,000 in bonds and stocks. These had been liquidated several years before, principally during the war. The fourth large holding was that of the Harkness family. At the time of the receivership Mr. E. S. Harkness held

over 100,000 shares of stock. This was the only large holding which was not liquidated before the receivership. Messrs. E. S. Harkness, Samuel Fisher, his attorney, and M. W. Buckner, chairman of the board of the New York Trust Company in which Harkness was substantially interested, represented the Harkness holdings on the board. The commission found that Buckner and Fisher, representing a real interest in the property, were the most active of the directors during the months prior to receivership in trying to find some way out of the difficulty. Harkness was the only one really pressing for a plan. He offered to stand back of a voluntary exchange of securities in a large way by putting up cash to pay dissenting bondholders. Some members of the board had been selected not on the basis of their holdings but with the idea that their position and knowledge would strengthen the board. Byrne, in presenting to the board his version of the events leading up to the receivership as related above, stated that the directors would have been derelict in their duty if they had failed to do as they did (seek aid from different sources, consider various plans, engage the engineers, etc.). The commission in commenting in their report stated that as a matter of fact outside of the Harkness representatives they did nothing except to formally approve the institution of receivership proceedings on March 17, as indicated previously. They had no substantial interest in the property and did not represent any such interest except that of Harkness.[1] They were impotent.

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1. 131 I.C.C., p. 638.

It was clear that the St. Paul did not have a single dominating financial interest in control like the Harriman interest with the Union Pacific and the Hill interest with the Great Northern. The control was divided among several large interests, all but one of which had "cleared out" by the time the receivership materialized. No doubt the severe criticisms the commission had occasion to make concerning the management of the road in the past, as brought out in its report on its investigation during the receivership, were the outcome in part at least of this apparent lack of a single dominant interest. Probably the direction of the road under a single interest would have been such as to have occasioned no such severe criticism on later investigation.

The Jameson committee representing a group of bondholders dissenting from the plan of reorganization put forward by the bankers claimed that the receivership was "conveniently" arranged by the banks to bring about the foreclosure of mortgages securing the junior bonds. It pointed out how the bankers assumed control and arranged things quietly as early as January without in some cases the direct authority of the board. It claimed that the receivership was hurried. Byram before Judge Wilkerson at Chicago where these charges were brought hotly denied the charges. He claimed that the directors were in control of the property up to the receivership, considered on their own initiative various plans to avoid the difficulty, engaged the engineers, and then frankly stated that the condition was hopeless on March 17. Of course

Byram claimed that the directors were constantly in touch with the bankers but only for purposes of advice.[1] The findings of the commission seem to agree with the facts as presented by the Jameson committee except that the receivership was hurried. The commission did not claim this in its report.

The company defaulted on the interest due on the General and Refunding 4 1/2's on April 1, 1935, $669,509.50; on the principal and interest due on the 15 year European loan of 1910 bonds on June 1, 1935, 21,386,500 French francs (at the rate of exchange on June 1, 1935, equivalent to $11,807,276.03) and $235,722.59 respectively; on the principal and interest due on the 4% gold bonds of 1933 on June 1, 1935, $35,100,000 and $702,000 respectively; on the interest due on the 4 1/2% convertible gold bonds on June 1, 1935, $1,124,568; on the interest due on the 4% gold bonds of 1909 on July 1, 1935, $865,720; on the interest due on the Chicago, Milwaukee & Puget Sound 4's on July 1, 1935, $3,413,300; and on the interest due on the General and Refunding 5's on August 1, 1935, $728,245.[2] In short, the company defaulted on the General and Refunding and Puget Sound Mortgages, for all these bonds with the exception of the Puget Sound 4's were secured by the General and Refunding Mortgage. These junior securities were represented by the bondholders' protective committee mentioned above. There were also a protective committee for each class of

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1. Railway Review, May 3, 1935, p. 664. Chronicle, vol. 132, p. 1451.
2. These figures represent amounts of the principal or the interest on the principal of bonds in the hands of the public exclusive of the insurance fund. 131 I.C.C., p. 877.

stock, as mentioned previously. These three committees were organized by the bankers.

Kuhn, Loeb & Company and the National City Company were the banking houses through which were distributed to the public the bonds at this time in default. It was represented that because of such relationship they undertook the responsibility of acting as reorganization managers in the formation of a plan for the St. Paul's reorganization.

Leaving the bankers at this point working out a plan of reorganization it may be well to point out how Coverdale & Colpitts ranked the different layers of securities in their report advising a reorganization. The engineers ranked the liens for reasons given below as follows:[1]

A. Obligations of the leased lines which included the obligations of the Terre Haute assumed and guaranteed by the St. Paul. As long as the lease was in effect the accounting rules of the commission required that the interest payment on guaranteed bonds should be carried as rental payment, and as such, from an accounting standpoint, it was a charge ahead of interest on the funded debt. Furthermore, as long as the lease was in effect all

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1. Coverdale & Colpitts, p.201. For the principal amount of these bonds in the hands of the public, see the statement of the funded debt as of Dec.31,1924 in the Appendix.

the obligations of the Terre Haute, whether first mortgage bonds or income bonds, should be of equal rank.

B. Equipment trust notes. Payment of interest and of maturing installments of the principal on these obligations was in the nature of rental payments for the use of equipment and was to be viewed as a charge against earnings intermediate between rental for the use of the road and interest on the public debt.

C. The General Mortgage was a first lien on substantially all the most important lines east of the Missouri River. The Chicago & Missouri River Mortgage maturing in 1926 underlied it on a short stretch of transcontinental line and some other lines of less importance, but the engineers believed that the General Mortgage should rank ahead. In this class the engineers not only put the Generals in the hands of the public, $99,788,000, but also the Generals pledged on the assumption that they could be reduced to possession. With the security gold loan of 1924 of course where the liability was $14,000,000 and the pledge was $20,000,000 Generals, only a liability of $14,000,000 was placed in the same rank as the Generals in this class.

D. In this class the engineers placed the divisional mortgage bonds. The engineers found that the traffic covered by the Chicago & Missouri Division 5's was very light. However, the line from Roscoe to Bowdle, which was part of the main transcontinental line, was supporting comparatively heavy traffic. This line, the engineers found, could no doubt be replaced at a cost considerably below the amount of outstanding bonds, but other conditions such as its value as a bridge line, the probable inter-

ruption to traffic in the course of replacement, and its relationship to the General Mortgage were relevant in determining the position of this mortgage.[1]

The two Milwaukee & Northern liens were put in this class. The traffic on the lines of the old Milwaukee & Northern were found to be heavy, approximating the average of the system. The engineers had no doubt but that the direct earnings of these lines plus the contribution of traffic to the rest of the system enabled them to support their interest charges. The traffic on the Bellingham Division under another mortgage was found to be light, but the engineers were of the same opinion concerning this division as of the lines of the old Milwaukee & Northern. The engineers did not believe that these should be ranked ahead of the General Mortgage. The latter covered the most important lines in the system and the mileage on which the Chicago & Division 5's were prior legally was relatively unimportant.

E. Liens junior to the General and divisional mortgages. In this class the engineers put the General and Refunding Mortgage bonds and other issues (originally issued as debentures) which ranked "pari passu" on account of the covenants providing that they should share in the lien of any later mortgage. The United States Government notes in excess of the principal amount of Generals pledged behind them and the interest on this excess amount were placed in this class. This excess was secured by $78,939,000

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1. The Chicago & Missouri River mortgage was the last of approximately 40 mortgages on the property formerly existing on the old lines ahead of the General Mortgage.

General and Refunding Bonds. The other portions of the principal and interest of these obligations were placed in Class C. In this Class E were placed also the Puget Sound 4's even though they were a first lien on the extension from Mobridge to Seattle and Tacoma. $28,175,000 was in the hands of the public and $1,000,000 was in the insurance fund. $154,489,500 was pledged under the General and Refunding Mortgage. If these pledged bonds were to be considered as outstanding there had been issued $181,664,500 with interest requirements of $7,266,580 per annum. But the engineers, as was pointed out in the previous chapter, found on analysis that the lines west of the Missouri River showed earnings available for interest in 1924 of only $1,478,000. This was available for interest on the Puget Sound 4's, the Bellingham Bay & British Columbia 4's, and the General and Refunding Bonds which were a first lien on some of the branch lines in the west. Therefore, it appeared that the interest requirements of the extension were so far in excess of the earning power of the lines on which these bonds were a first lien that as a practical matter the Puget Sound 4's should be grouped with the General and Refunding Mortgage and with the bonds originally issued as debentures but now secured by the General and Refunding Mortgage.

F. Guaranties of bonds issued by controlled companies and operated separately. This group included only the funded debt of the Gary which consisted of $3,000,000 first mortgage 5's in the hands of the public and $2,700,000 of the same bonds held by the St. Paul. The engineers considered this guaranty as an

obligation ranking after the obligations of the leased lines or those issued by the St. Paul.

The engineers report with this ranking was submitted prior to the receivership. It is interesting to note that the securities in which the company subsequently defaulted were in Class E which was next to the lowest rank as ranked by the engineers. No doubt the value of the Gary as a connecting link between the Illinois divisions of the system and the Terre Haute was an influence in the bonds of this line not being defaulted. They were considered to be of the lowest rank by the engineers.[1]

On March 29, shortly after the receivership, Mr. F. J. Lisman of F. J. Lisman & Company, New York, in an interview outlined the probable plan of reorganization of the capital structure of the St. Paul. His views at that time were of interest as they contained the first ideas published as to what would probably be done. The views of other authorities as to what should be done or what would probably be done were given publicity at the time. Lisman claimed that a plan must provide (1) means of raising funds for certain immediate purposes and future purposes at the lowest possible market rates, (2) a substantial amount of cash at once without increasing fixed charges, and (3) the removal of certain equities of securities which were to be disturbed. To accomplish this, he pointed out, it would be necessary to foreclose the General and Refunding and Puget

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1. An analysis of the junior bonds (in Class E) from the investors' point of view just prior to the receivership was clearly presented in a confidential pamphlet prepared by the statistical department of Brook, Stackes & Co., Philadelphia, entitled "Position of the Junior Mortgage Bonds of the C.M.& St.P. Ry. Co.", Feb.18,1925. For the Generals (in Class C) a similar analysis was made by Roosevelt & Sons, New York.

Sound Mortgages and exchange the bonds on these mortgages for junior bonds, and it would also be necessary to permit a mortgage which would be a first mortgage on the lines west of the Missouri River and a junior one on the lines east of the river for future needs. These new bonds to be exchanged might be income bonds. The company could not give stock as a good share of the General and Refunding Bonds were being held by insurance companies, banks, etc., which are restricted as to stock holdings. A new 5% income bond cumulative in from two to five years was desirable. The holders of General and Refunding Bonds might, he reasoned, receive these new income bonds. The holders of the Puget Sound bonds might receive the same or else 75% to 80% in new income bonds and the balance in preferred stock. The engineers report should aid in determining a fair exchange. The stock, Lieman thought, would have to pay an assessment of not less than $20 per share, probably more. Some security would have to be given. Probably an underwriting syndicate would underwrite the assessment. Legally the junior bondholders, when not receiving the interest and principal when due, should get the entire equity. If the stockholders were to retain an equity, it was only fair that they should get first preferred stock for the new money, something that would bring them a return after the junior bond holders got their return. He thought probably a compromise would give the stockholders half income bonds and half first preferred stock for their assessment. The loans from the government he thought were interesting. The St. Paul was paying 4% on money costing the government 4 1/4%.

netting 1 3/4% or $968,500 profit per annum. This was unfair to a company not on its feet and to the rest of the public with their funds tied up. A bill introduced in the previous session of Congress which would have reduced the rate to 4 1/2% saving the St. Paul $875,000 a year failed to pass. The commission had no power to reduce the rate. The treasury could compromise the claim but no doubt was afraid of Congress. The reorganization managers would probably decide that what the $18,000,000 General 5's pledged as collateral would bring should be paid at least.[1]

Early in June the reorganization managers announced their plan which was worked out in cooperation with their committees representing the bondholders and stockholders.[2] This plan will be presented in detail as it was the plan with some modifications to be brought out shortly which was finally adopted.

The plan called for the organization of a new company to acquire all the properties belonging to the St. Paul and to issue for that purpose its securities against the transfer to it of such properties and certain other assets.

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1. Chronicle, vol.130, p.1744.
2. The sources of material for this plan as of June 1, 1935 are "Reorganization of C.M.& St.P.Ry.Co., Plan and Agreement dated June 1, 1935 with Modifications of Plan dated November 19, 1935" published by the managers, hereafter referred to as the Plan, and 131 I.C.C.,p.880. For summary of the plan as of June 1, 1935, see Chronicle, vol.130,p.2935 and Railway Review, June 8,1935, p.1039.

Obligations aggregating $181,370,400 were to remain undisturbed. This amount consisted of the various divisional issues, the Generals, the obligations of the Terre Haute and Gary, and the several issues of equipment trusts.[1]

A new mortgage was to be made upon all of the St. Paul's road and assets subject to the undisturbed obligations. It was to be called the First and Refunding Mortgage. The purpose of the mortgage was to provide for future capital needs and also for the refunding of all of the underlying bonds, including those on the leased and controlled lines. Bonds necessary for refunding these prior liens were to be reserved. The details as to the series of these bonds to be issued, the rates, the maturities, sinking fund provisions, conversion privileges, etc. was to be left with the board. The total amount of bonds that could be issued under this mortgage was not to exceed twice the value of the outstanding capital stock of the company at any time. No First and Refunding Bonds were to be issued in the reorganization. February 2, 1925 was subsequently selected as the date of the mortgage, and the United States Mortgage & Trust Company and Calvert Brewer were selected as the trustees.

The reorganization managers and the committees concluded after careful study and conference with Coverdale & Colpitts that the equities of the situation required that all the various issues of bonds secured under the General and Refunding and Puget Sound

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1. . figures given here in the presentation of the plan of the managers represent the amounts of obligations in the hands of the public and in the insurance fund but not those in the treasury as of June 1, 1925. The defaulted bonds in the treasury were to be cancelled.

Mortgages outstanding in the hands of the public should be treated alike in the allotment of new securities. The security of all the bonds secured directly or indirectly (the several issues put out as debentures originally) under the General and Refunding Mortgage was identical. The Puget Sound bonds constituted a first lien on the lines west of Mobridge. But over 95% of these bonds were pledged under the General and Refunding Mortgage. The lines west of the Missouri River in earnings compared unfavorably with the lines east of the Missouri River. The General and Refunding Mortgage was preceded by several mortgages on the lines east. Therefore the managers and committees decided to treat all the bonds in default alike. $230,950,795 of junior bonds was in default.[1] For each $1,000 bond deposited with all coupons maturing after February 1, 1935, the depositor was to receive a new $1000, 5% adjustment mortgage gold bond. No bonds were to be issued in respect of the unpaid interest as the new bonds were to bear interest from February 1, 1935, and there was to be paid in cash all interest due and unpaid prior to the dates of default in interest.

The 5% adjustment mortgage was to secure an authorized issue of bonds not exceeding $230,950,800 (necessary to refund the

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4% bonds, due 1935	$38,144,991
European loan bonds	11,831,515
4 1/2% bonds, due 1932	50,000,000
4% bonds, due 1934.	33,369,000
General & Refunting Bonds, Series A & B	72,230,300
Puget Sound bonds	27,175,000
Total	$230,950,795

All these defaulted securities with the exception of the Puget Sound bonds will hereafter be referred to frequently as the various General and Refunding issues.

existing bonds in default) plus any amount necessary in liquidating the $30,000,000 note to the Government if it should select one of the two alternative methods of settlement offered to it in the plan. These alternatives will be brought out shortly. The bonds in connection with this alternative were never issued as the government selected the other alternative. The bonds were to mature on January 1, 1900 and bear interest at 5% per annum, payable annually or semi-annually. The interest was to be non-cumulative prior to January 1, 1930 and cumulative from and after that date. Accumulations of interest were not to bear interest. At the maturity of the principal all arrears of cumulative interest were to be payable. Interest on the bonds issued in exchange for deposited defaulted bonds was to be computed to February 1, 1925. On or before April 1, 1938 and yearly thereafter, there was to be paid to the trustee for a sinking fund from the net income for the preceding year, after payment of full cumulative interest on the adjustment bonds, an amount equal to one 1/2% of the authorized principal amount of adjustment bonds. Such sinking fund payments were to be cumulative. No dividends were to be paid on any class of stock until all interest and sinking fund payments and cumulations on the adjustment bonds were paid or set apart for payment. All the available net income for each year beginning January 1 might be applied and half of it had to be applied until this available net income should equal $10,000,000 and all the available net income each year in excess of $10,000,000 had to be applied to the payment of interest on the adjustment bonds and

thereafter, beginning April 1, 1936, to the sinking fund of this mortgage, including all accumulations of both interest and sinking fund during the cumulative period. Interest prior to the maturity of the bonds was to be paid only in multiples of 1%, smaller fractional amounts to be carried forward and added to that portion of the net income for the ensuing interest period required to be applied to the payment of interest and sinking fund on the adjustment bonds. Any remaining net income of any year until January 1, 1930, for which interest on the adjustment bonds at the full rate of 5% per annum had not been paid or set apart for payment, and any remaining available net income in every year after January 1, 1930, for which the full cumulative interest, and beginning with the year 1935, for which the sinking fund payments also shall not have been paid or set apart for payment, had to be carried into a separate account available only for expenditures chargeable to capital account, for providing for discount on securities sold, or for cumulative interest on the adjustment bonds, and if such interest had been paid, then for the sinking fund payments in respect of this mortgage. These adjustment bonds were to be redeemable, otherwise than for the sinking fund, at the option of the company in whole or in part on any interest payment date on or after October 1, 1930 at 105 and full cumulative interest. These bonds were all to be offered in connection with the reorganization. The mortgage in short was to rank after the 50 year 5% mortgage which was to secure bonds to be offered to the stockholders as will be explained below.

As finally arranged subsequent to the publishing of the plan as here presented the new adjustment mortgage was dated February 1, 1925 and made to the National City Bank of New York and William E. Hoffman, as trustees. Interest at 5% per annum was made payable from February 1, 1925 to December 1, 1926, on April 1, 1927, and thereafter semi-annually on October 1 and April 1 in each year to October 1, 1999. The last installment of interest of course was payable on January 1, 2000, the maturity date provided in the mortgage. It was also finally arranged as these bonds could be issued as series A, B, and C. Series A bonds were to be payable in dollars and might be issued in the denominations of $100, $500, and $1,000 for the coupon bonds and in the denominations of $500, $1,000, and multiples of $1,000 for the registered bonds. Series B bonds were to be payable in French francs and might be issued in the denominations of 400 and 2,000 francs. Series C bonds were to be payable in sterling money of Great Britain and might be issued in denominations of £15:16:5 and £79:2.

The management and managers' security holders' committees carefully considered the handling of the debt to the government. There was a note for $35,000,000 and another for $10,000,000 which were given for loans under section 210 of the Transportation Act of 1920 as amended. There was another for $30,000,000 given to the Director General of Railroads, as agent, in respect of matters pertaining to the federal control period. These all bore 6% and were collaterally secured by the pledge of bonds. These bonds were Generals and General and Refunding Bonds. Were the

government to foreclose upon the collateral and exchange it for new securities under this plan the funded debt would be increased at least $35,000,000; and the interest charges, at least $1,750,000. Besides $18,000,000 of this collateral were General 5's. These would be left outstanding and the company would be deprived of their use for future purposes. All this would dilute the security of the bondholders and increase the burden ahead of the stockholders' equity. Were the notes extended and the collateral left or exchanged for new securities the unsettled but ultimate necessary refunding would be a drag on the new company's credit. Bonds would have to be reserved under the new First and Refunding Mortgage thus weakening that mortgage as a source of funds for future capital requirements. Were the debt reduced to an amount which could remain upon the security of the $18,000,000 Generals, which were a part of the collateral, say $13,000,000, the new company would be deprived of the use of its best bonds for sources of necessary new funds during the first few years of its existence. New First and Refunding Bonds would have to be issued at higher rates than that at which these Generals could be sold. Therefore the managers and committees in the plan provided for the payment of the $35,000,000 and $10,000,000 notes, which were secured in part by the $18,000,000 in Generals, in cash. The $20,000,000 note was secured entirely by General and Refunding Bonds. At prices which prevailed since the receivership the collateral did not fully secure that note. Therefore the plan provided two alternative offers: (1) $17,000,000 in cash and $3,000,000 par value of new preferred stock with full interest on

the note to the date of settlement in cash or (2) $32,000,000 principal of new 5% adjustment mortgage gold bonds issuable under the plan. The same amount of General and Refunding bonds note use the collateral behind the note. After negotiations with Secretary of the Treasury and the Director General of Railroads arrangements were made to pay the note as provided in the first alternative.

New money aggregating $70,032,548 was deemed necessary to effect the reorganization. This comprised estimates of $52,000,000 for the government notes, $1,544,535 for interest in respect of bonds deposited under the plan, and $16,488,383 for additions and betterments, equipment, working capital, and expenses of receivership and reorganization. The foregoing cash requirements were to be met by payments of $28 per share by the holders of the $115,931,000 existing preferred stock and of $38 per share by the holders of $117,411,300 common stock. For such payments the stockholders were to receive new 50 year 5% mortgage gold bonds to the principal amount of $34 for each share of preferred stock and $38 for each share of common stock, and there was to be issued to them one share of new stock of the class on which the assessment was paid. Half the assessment was to be payable on a date to be fixed by the managers; and half, on or before February 15, 1927 with interest at 5% per annum from the date of the first payment to the date of the final payment. The stockholder depositing his stock with the proper committee was to be given the option of paying his full assessment on the date fixed for the first installment. To the extent of $4 a share payment

no new securities were to be issued. According to the reorganization agreement with the managers, $1.50 of this $4 was to be set aside for the compensation of the reorganization managers, various protective committees, and the fees of their counsel, depositaries, and expenses in connection therewith. Any balance remaining after such payments was to be paid, at the option of the reorganization managers, to the new company for additional working capital or returned to the holders of certificates of deposit for stock. Such provision would produce approximately $3,500,000 for reorganization expenses. Out of this amount there was to be appropriated for the compensation of the reorganization managers a sum equal to 1/4% upon $250,950,796 of bonds (disturbed bonds or bonds to be exchanged for new securities) and 30¢ a share upon 2,333,432 shares of stock outstanding or a total of about $1,044,000. Incidently, this charge of 25¢ on each $100 of bonds and 30¢ on each share of stock was not much more than the average fee charged for stock brokerage services, as Hanover pointed out before the Senate Interstate Commerce Committee, which in the course of the receivership delved into the road's affairs, under the chairmanship of Senator Watson of Indiana.[1] However it seems that the services of the managers were not comparable to that of the stock broker. The proposed payment to the managers appeared to be a "rake-off" for the bankers. Furthermore in many cases nothing is paid to the members of the security holders' protective

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1. Railway Review, April 3, 1933, p. 651.

committees. As will be pointed out later, the commission placed restrictions on the expenditure of this $4 collected from each stockholder. In short $20,032,548 was to be raised by assessing the stockholders for which $40,066,830 new 50 year 5% mortgage gold bonds were to be issued. Over $9,000,000 new money was needed and was to be raised for purposes which the managers and their committees did not wish to finally appear in the capital structure. These purposes were matters connected with the reorganization. The unpaid claims of general creditors, estimated to be about $1,000,000, were to be settled by the issue of new preferred stock.

The new 50 year 5% mortgage which was to secure the bonds to be issued to the stockholders for their assessments was to mature in 1975. The bonds were to bear interest payable semi-annually at of course 5% per annum. The bonds were to be redeemable, at the option of the new company, on any semi-annual interest payment date up to and including five years from the date of maturity at 105 and accrued interest and thereafter at a premium of 1/2% for each six months from the date of redemption to the date of maturity. This mortgage was to cover the entire road and assets and was to follow the new first and refunding mortgage. The total amount of bonds were to be limited to the $40,066,830 necessary for issuance in connection with the assessment of the stockholders. In other words the entire authorized issue was to be offered to the stockholders in connection with the reorganization. At the time the plan was first published the managers announced

that the exact form of this mortgage was to be subject finally to the approval of the two stockholders' protective committees formed by the managers. The mortgage was subsequently dated February 2, 1925 with the interest payable on February 1 and August 1 and the maturity date on February 1, 1975. The Guaranty Trust Company of New York and Merrel P. Callaway were made the trustees. It was also finally arranged so the bonds might be issued in series. Series A bonds were to be payable in dollars and might be issued in denominations of $100, $500, and $1,000 for the coupon bonds and $500, $1,000, and multiples of $1,000 for the registered bonds. Series B bonds were to be payable in French francs and were to be issued in denominations of 100 and 500 francs. Series C bonds were to be payable in sterling money of Great Britain and were to be issued in denominations of £3:19:3 and £19:15:6. Script certificates for Series A bonds for fractions of bonds less than $100 might also be issued.

2,000,000 shares of preferred stock with a par value of $100 each and 1,174,113 shares of common stock without par value or of such par value as the managers should determine (no par common was finally decided upon) were to be authorized. The preferred stock was to be entitled to yearly dividends at the rate of $5 a share before any dividends were paid on the common stock. The dividends on the preferred were to be non-cumulative. After the preferred stock received its full dividend of $5 per share the common stock was to be entitled to receive all other dividends in that year up to $6. All dividends in excess of $6 a share upon

both the preferred and common stock were to be paid or set apart for payment in equal amounts per share upon the preferred and common stock. In case of dissolution or liquidation the holders of preferred stock were to be entitled to receive out of the assets the par value of their shares before any distribution was made to the holders of common stock. Both classes of stock were to have equal voting power. $115,931,800 of the preferred was to be offered to the holders of the existing preferred stock deposited under the plan, $3,000,000 was to be issued to the government should it decide to select one of the two alternative methods of settlement offered on one of its notes, and about $1,000,000 was to be issued to general creditors for their claims. The remainder was to be reserved for future issue for corporate purposes of the new company. The entire authorised issue of new common stock was to be offered to the holders of the existing common stock deposited under the plan. The new preferred and common stock was to be deposited under a trust agreement. The voting power was to be vested in five trustees selected by the managers. Of these trustees three were to be approved by the bondholders' committee, one by the preferred stockholders' committee, and one by the common stockholders' committee. The trust agreement was to be made to extend for a period not less than five years. Extensions of the agreement were to be possible with the consent of the majority of each class of trust certificates. The exact details of this voting trust were to be left with the managers and

committees. The reader will note that the stockholders were to receive trust certificates and not stock and that the control of the new company was to be invested with the junior bondholders for five years at least.

A timber loan of $2,800,000 was to be liquidated by the sale of the obligations of third parties held as collateral to the loan which obligations might be guaranteed by the new company, or the loan was to be dealt with in any other manner as the managers might determine.

The managers were to declare the plan operative at their discretion when in their opinion sufficient securities had been deposited under the plan.

Such was the plan of the managers as put out on June 1, 1925. The Generals, divisional issues, the obligations of the Terre Haute and Gary, and the St. Paul equipment trusts were to remain undisturbed. A new first and refunding mortgage was to provide for future financing. The junior bonds in default were to be exchanged for new 75 year 5% adjustment mortgage bonds. These new bonds were to be income bonds really. The debt to the government was to be liquidated mostly with cash. The timber loan was to be liquidated. The general creditors were to be paid off in new preferred stock. The stockholders were to pay the necessary new money and receive new stock and also new 50 year 5% mortgage bonds. The plan called in short for three new mortgages on the entire road and assets to be subject to the undisturbed liens, practically all of which were on the lines east of Mobridge. Of these three, the new first and refunding mortgage was to rank first;

the new 50 year mortgage, second; and the new 75 year adjustment mortgage, third. This new first and refunding mortgage to secure bonds to be issued in the future for future needs was to be the fifth general and refunding mortgage in the road's history. The stockholders were to receive a lien superior to that of the junior bondholders in return for the contribution of new money. Table XXVII in the Appendix shows the existing capitalization and interest charges on June 1, 1925 and the approximate capitalization and interest charges if this plan were to go into effect. The reader will note that the capitalization would be increased from $708,884,396 to $708,383,216 if the new no par common stock is given a value of $100 per share; and the fixed charges reduced from $21,836,793 to $11,468,845, not counting the contingent interest charges on the new adjustment mortgage bonds which were cumulative after 1930. The managers and their committees representing the security holders thought that the plan brought the fixed charges safely within the available earnings of the company in the light of past earnings and probable future earnings as predicted by the engineers. The predicted future increase in business would, they decided, take care of the contingent liability in connection with the income bonds which would become cumulative within five years.

The managers and committees claimed that they framed this plan with four requisites constantly kept in view. These were:

1. That all debts of early maturity should be funded at not over 5% with securities junior in lien to the new financing mortgage.

2. That the new company should have moderate fixed charges and a capital structure permitting the raising of new money from time to time at the lowest cost and should be able to withstand the effects of future bad years without the danger of receivership.

3. With the foregoing requirements met, the earnings reasonably available to the interest on the bonds representing the bonds participating in the receivership should be paid thereon.

4. The relative position of the bondholders in respect to earnings as compared with the stockholders should be maintained and the latter should be given an opportunity to participate in the plan on such a basis that their participation could, if need be, be underwritten at a moderate expense.

As the various security holders' protective committees, which had been organized by the managers to protect the interests of the security holders and to represent them in the consideration of any readjustment plan, had approved of this plan, the security holders were urged to deposit their securities at designated depositaries in order to make the plan effective and bring the receivership to a close as quickly as possible.

Of course there was criticism from all quarters. It would certainly be a wonderful plan that would not excite some criticism. F. J. Lisman, who in a statement in March gave his views as to what form the capital structure of the St. Paul would probably be reorganized (referred to previously) now commented on the objections. He pointed out two objections which appeared to

be more or less general. The government loans should be refunded at lower rates making necessary the raising of less new money immediately. The road should not be reorganized until the commission had acted on the increase in rates being requested at that time by the carriers in the western district. There were objections from the security holders involved. The junior bondholders objected to the stockholders getting bonds prior to those to be given to the holders of junior bonds. The stockholders should also get income bonds for the assessment. The stockholders objected to the size of the assessment and the fact that for $4 of this assessment they were not to receive any security. Lisman thought that the purposes for which the $4 was to be expended should not appear in the financial structure. The preferred holders objected to the fact that their preference over common stock was to be reduced from 7% to 5%. The common stockholders objected to paying a higher assessment than the preferred and to be left with stock very remote from earnings, probably ten years. Lisman thought that all these objections had some force, but, unless the bondholders were in a position to underwrite the assessment on the stock and give the stockholders say 60% in the new adjustment bonds (income bonds) and the rest in stock for the new money, then the junior bondholders should not object. The objections of the stockholders were not unusual. Stockholders have always complained when they are assessed, Lisman pointed out.[1]

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1. Chronicle, vol. 130, p. 3062.

The two general criticisms above brought replies from the managers and their committees. The bondholders' committee in a letter to the bondholders pointed out why the managers and committees decided against the refunding of the government loans.[1] This point was brought out previously in this chapter. In July, 1935 the reorganization managers made a statement answering the other general objection. They objected to the delay until the western rate case was settled because there was no assurance that rates would be increased, delaying the reorganization would not hasten a rate increase, and any increase in rates permitted, in their opinion, should not cause any alterations in the plan which was devised so the road could withstand all possible future conditions. If the rates were increased then the security holders would benefit. They pointed out that the receivership should be lifted as quickly as possible to avoid damage to the good will due to a receivership, to avoid the heavy current expenses of a receivership, to avoid the higher financial costs than those of a road established as to credit, to avoid the loss due to the continuance of the government debt at 6%, to avoid the reduction in earnings available for interest caused by these factors, and to hasten the time when the earnings would be available for the present security holders.[2]

The securities affected by the reorganization plan began to pour into the designated depositaries. About the middle of July

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1. Ibid., p. 3308.
2. Ibid., vol.121, p.454.

the managers announced that a total par value of $44,000,000 in bonds and $23,000,000 in stock had been deposited under the plan.[1] On August 19 the Wall Street Journal announced that $47,400,000 or 21% of the bonds effected had been deposited.[2] On October 8, 1925, the reorganization managers declared the plan operative. A total of $111,500,000 or 49% of the junior bonds had been deposited. This included $19,000,000 or 73% of the Puget Sound bonds out and $92,500,000 or 45% of the bonds secured by the General and Refunding Mortgage. In addition $80,800,000 stock had been deposited. The total securities assenting amounted to $192,300,000. The reorganization managers at this time announced that the holders of the remaining securities would be given until November 30, 1925 to deposit their securities without penalties.[3] However, later the time limit to deposit securities was extended a number of times and no time limit or penalties were ever enforced.

A dissenting stockholders' committee was organized with Earnest Iselin of New York as chairman. This committee asked the court at Chicago to permit them to intervene on behalf of the stockholders in the receivership and foreclosure proceedings at that time pending in the federal court at Chicago. These proceedings were the result of the default in the various issues secured by the General and Refunding Mortgage and the first mortgage bonds secured by the Puget Sound mortgage. The trustees were seeking to foreclose the mortgages and bring about the sale of the property. The petition

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1. Ibid., p. 326.
2. Ibid., p. 874.
3. Ibid., p.1786. Railway Review, Oct.17,1925, p.807.

of this committee, known as the Iselin committee, was denied by Judge Wilkerson. The committee at that time represented stock of $19,200,000 par value. $14,400,000 of this was common.[1]

A dissenting bondholders' committee appeared on the scene in October, 1935. This committee was headed by George S. Roosevelt (Roosevelt & Sons, New York) "to secure a reorganization more equitable to the junior bondholders" and to oppose the consummation of the plan proposed by Kuhn, Loeb & Company and the National City Company. Informal efforts of the Roosevelt firm to secure certain modifications on the managers' plan had failed. It now called for the deposit of junior bonds.[2] This was known as the Roosevelt committee. At one time it represented $18,638,500 par value in bonds.

Later in October, 1935, the Roosevelt committee came forward with a plan. $5,000,000 of the government debt was to be paid in cash. The remaining $50,000,000 of this debt was to be paid in equal serial annual installments between the fourth year and fifteenth year inclusive after the consummation of the plan. This $50,000,000 was to bear 4 1/2% interest and be secured by $75,000,000 of 5%, 50 year mortgage bonds of a special series. The $230,050,794 of bonds in default were to be exchanged for 25% in fixed interest bonds on a 50 year mortgage bearing 4% for five years and 5% thereafter, and 75% in participating adjustment mortgage bonds paying 5% and receiving an additional 1% if the

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1. Chronicle, vol.121, p.2518.
2. Ibid., p.1785. Chronicle, Railway and Industrial Section, vol. 125, p. 38.

earnings warranted. This 50 year fixed interest mortgage besides securing the bonds to be issued to the junior bondholders for 25% of their holdings was also to secure the $75,000,000 bonds to be pledged with the government. The new adjustment bonds were to be cumulative in three years. The holders of the preferred stock were to receive for each share of existing preferred stock one share of new non-cumulative preferred stock entitled to 5% dividends before any dividends on the common. After 5% on the preferred, the common stock was to be entitled to 5% dividends. All dividends in excess were to go equally to the preferred and common. However, after the preferred received 4%, the new participating adjustment bonds were to receive the additional 1% before the preferred was to get its full 5%. The holders of the existing common stock were to receive an equal number of shares of new no par value common stock. No compensation was to be paid the Roosevelt firm to conduct the reorganization. The reorganization managers were to receive 1/4% of the par value of the disturbed bonds and 20¢ a share, as pointed out previously. The Roosevelt plan called for an assessment of $10 per share or $33,334,320 from the stockholders, $46,698,848 less than that called for by the managers' plan due to the plans to pay only $5,000,000 of the government debt at once instead of $53,000,000 as called for in the managers' plan. The stockholders were to receive the new adjustment bonds for the assessment - dollar for dollar. The Roosevelt plan in short called for three new mortgages like the plan of the managers, a special refunding and future financing mortgage to follow the undisturbed liens,

a new 50 year fixed interest mortgage, and a new adjustment mortgage. They were to rank in the order given.[1]

The three assenting protective committees (bonds, preferred stock, and common stock) criticized the new plan.[2]

The bondholders' committee opposed. It claimed that the future earnings as predicted by the engineers would not support the future installments on $50,000,000 of the government debt. The installments due from the fourth to the fifteenth year would be a burden injurious to the company's credit. Besides the possibility of refunding the government debt at 4 1/2% was not a certainty at that time. The fixed interest charges in the Roosevelt plan would be $1,584,567 a year for the first five years and $2,101,944 a year thereafter in excess of the fixed charges as called for under the managers' plan. The Roosevelt plan did not contain the provision making it compulsory for the new company to set aside one half of the first $10,000,000 available net income and all the rest in excess of that amount to pay the interest on the new adjustment bonds as contained in the managers' plan. Besides the voting trust in the managers' plan provided for a majority of the directors to represent the bondholders during the non-cumulative period. After that the cumulative feature would protect them regardless of the directors. The bondholders' committee could see no advantages in the provision of the Roosevelt plan which would give them 25% of their present bonds in new 5%

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1. Chronicle, vol.121, p.1903.
2. Ibid., p. 2151.

fixed interest bonds and 75% in 5% adjustment bonds with an additional 1% contingent on earnings after 4% was paid on the preferred. Its opinion was the same in regard to the provisions which would assess the stockholders only $23,334,42[illegible] instead of $70,032,548 for which they were to receive an equal amount of 5% adjustment bonds (the same as the bondholders received for 75% of their existing junior bonds in default) instead of 86% of their assessment in fixed interest bonds ranking ahead of the adjustment bonds as called for by the managers' plan. The managers' plan was to give the bondholders adjustment income bonds. The Roosevelt plan would break the security the bondholders were to receive into two parts. The new adjustment income bonds in the Roosevelt plan were to be diluted by the amount to be given the stockholders and the larger amount to be given the government. The assenting bondholders' committee therefore decided that the split-up security they would receive would be poorer than the security to be received under the managers' plan. Besides the restrictions to be placed on the new company as regards the disposal of the net income available on the new adjustment bonds as provided for in the managers' plan was sufficient protection to the bondholders in the new company. The 1% contingent interest on the new adjustment bonds was illusory to the assenting bondholders' committee as most likely 4% could not be paid on the preferred for a number of years.

Both of the assenting stockholders' committees also criticized the Roosevelt plan. The Roosevelt plan increased the fixed charges prior to the stock. Besides the charges prior to the stock were increased still more as against the managers' plan because the Roosevelt plan would make the new adjustment bonds