26-9

Statement of

H. E. Byram
President

C. M. & St. P. Ry. Co.

Before

Interstate Commerce Commission

December 1, 1925

Numerous requests were made at the hearing in Washington for copies of this statement, to comply with which printed copies have been made and are now available

I. C. C. Docket 17021

Re: Investigation of

Chicago, Milwaukee & St. Paul Railway Company

Statement of Mr. H. E. Byram

My connection with the Chicago, Milwaukee & St. Paul Railway Company began October, 1917, as its President. During the period of Federal control I served as Federal Manager of the property and on March 1, 1920, resumed my duties as President of the Company, which position I still hold. On March 18th, of the present year, I was appointed one of the Receivers by the District Court of the United States for the Northern District of Illinois, Eastern Division.

Prior to my connection with the St. Paul Company, I had been in railroad service since 1881, having held the positions of Superintendent and General Superintendent, and from September, 1910, to October, 1917, Vice-President in Charge of Operation, Chicago, Burlington & Quincy Railroad.

The Interstate Commerce Commission, on its own motion, has ordered an investigation into the history and management of the St. Paul Company, its financial and other operations, accounts and practices, for the purpose of determining the manner and method in which the business of the company has been conducted.

While we have arranged to give the Commission all the assistance in our power to the end that there may be made available to it all of our records which will throw all light possible on each of the features under investigation, as specified in the Commission's Order, I desire in this statement to cover, as briefly and as concisely as possible, the history of the property during the past twenty-five years, and more particularly, the operations, finances and practices during the period of my connection with it as President.

I will now introduce as Exhibit 2 a map of the St. Paul System, including the lines of the Chicago, Terre Haute and Southeastern and the Chicago, Milwaukee & Gary Railway.

The Chicago, Milwaukee & St. Paul System includes the lines of the Terre Haute and Gary companies, comprising a total of approximately 11,000 miles. Chicago, Illinois, is the principal terminal on the east, and Seattle and Tacoma, Washington, are the principal terminals on the west. The St. Paul System operates through twelve states, having extensive trackage serving the territory extending from the Missouri River on the west to Lake Michigan on the east; Kansas City, Terre Haute and Chicago on the south, and Fargo, the Twin Cities and Duluth on the southern shore of Lake Superior on the north, the latter point being reached through trackage rights over the Northern Pacific. West of the Missouri River the line traverses the states of Montana, North and South Dakota, Idaho and Washington, with

branches serving the territory tributary thereto. This mileage is co-ordinated and effective in serving the territory traversed.

Through the lease of the Chicago, Terre Haute & Southeastern, its lines tap the large bituminous coal fields of Indiana, securing an adequate and effective supply of coal of excellent quality for its own use as well as for distribution throughout the northwest. This line also serves as a connecting link through which this company may deliver freight which it originates at Chicago and west to the important eastern and southern lines, saving the delay and expensive operation through the Chicago terminals, as well as securing for the St. Paul a larger division of the through rate.

It has a favorable line, both as to distance and grades, between Chicago and the Twin Cities, and extensive terminal facilities at Chicago, Milwaukee and Twin Cities. It also has terminals for the interchange of business by water at Milwaukee and other Lake Michigan ports, and also Lake Superior, through Duluth and Superior. By reason of its location and the network of branch lines, it handles a substantial portion of the manufactured commodities, agricultural products, live stock and the products of mines and mills in the states of Iowa, Wisconsin, South Dakota, Minnesota, Northern Illinois and the Peninsula of Michigan.

With its lines extending from Chicago to Kansas City and Omaha, it participates extensively in the movement of business to and from the west, southwest and Pacific Coast, through those gateways. Its lines in Montana reach practically all important cities of that state and also serve large agricultural and live stock districts. They are also situated so as to participate in the transportation of the products of mines, both coal and metal, of that state.

With a small amount of mileage in Idaho, it reaches the important lumber manufacturing plants, and in the state of Washington reaches Spokane on the east and Seattle, Tacoma, Everett, Bellingham and Port Angeles on Puget Sound, as well as Pacific Coast, harbors at Raymond, Aberdeen and Hoquiam. Its lines reach, under very favorable conditions, the great timber resources of that state, and have complete terminal facilities for the interchange of business with water lines, the handling of export and import traffic, and having the short line to Puget Sound points from Chicago, Twin Cities and Spokane, added to the advantages of electrical operation of 649 miles of transcontinental line, it is now in a position to handle efficiently and promptly the tonnage moving by rail in either direction.

I will now introduce Exhibit 3, showing the principal changes in the physical and financial characteristics of the St. Paul for the period 1900 to 1924.

This statement shows for the period 1900 to 1909 that the average miles of road increased from 6,462 to 7,512; the investment in road and equipment from $218,302,680 to $274,468,163; funded debt decreased from $121,154,000 to $114,732,500; interest on funded debt from $6,633,170 to $5,855,718; operating revenues had increased from $41,884,692 to $61,296,041; operating expenses increased from $27,162,829 to $39,950,134; net income available for interest and dividends increased from $13,608,610 to $18,967,918; and the balance available for dividends on common and preferred stock increased from $6,975,440 to $13,112,200. The preferred stock outstanding increased from $35,595,000 to $49,718,000 and the common stock from $46,924,000 to

$83,705,000, not including preferred stock amounting to $66,214,000 and common stock amounting to $32,241,000 issued in March, 1909.

During this decade the Company's revenues increased 46% and there was a satisfactory margin between revenues and cost of doing business, operating expenses being 64.85% of the revenues in 1900 and 65.18% of the revenues in 1909. It had been earning three times the interest on its funded debt, had paid 7% dividends on preferred stock and 7% on common stock in all but three years, in which it paid from 5% to 6% and after doing so, carried forward for the ten-year period a surplus of $39,957,000.

With the acquisition of control of the Burlington Railroad by the Hill interests in 1901, the management of the St. Paul was faced with the situation of being confined to the territory east of the Missouri River or building an extension of its own to the Pacific Coast. The question has often been raised as to whether the St. Paul would be in the financial condition it finds itself today if it had not incurred the financial burden attendant to the construction of this line. This is a matter of conjecture, as who can say what the St. Paul's development and revenues would have been if it had not crossed the Missouri River?

As throwing some light on this situation I will now introduce Exhibit 4 showing for the St. Paul, the Northern Pacific, Great Northern, Chicago & North Western, including the Omaha, and the Chicago, Burlington & Quincy R. R., a comparison of the increase in miles of road operated, investment in road and equipment, including material and supplies; the increase or decrease in net railway operating income and the decrease in the rate of return earned on investment for the average of the years 1923 and 1924 compared with 1916 and the average of the two years 1908 and 1909.

This comparison would indicate that the investment of the St. Paul in the Puget Sound Extension has proved no more unprofitable than the investment made by the Northern Pacific and the North Western since 1909. For the average of the years 1908-1909, which were prior to the operation of the Puget Sound Extension, the average investment in road and equipment and material and supplies of the St. Paul amounted to $275,891,116; its average net railway operating income for those two years amounted to $17,837,294; the rate of return 6.47%. For the average of the two years 1923 and 1924, the investment in road and equipment and material and supplies amounted to $733,336,553, an increase of $457,445,437 over the average of 1908-1909. The net railway operating income for the average of the two years 1923-1924 amounted to $19,569,909, or 2.67% on the investment. The years 1923-1924, therefore, show a loss in return on investment, as compared with 1908-1909, of 3.80%.

In the case of the Northern Pacific, the average investment in the years 1908-1909 was $391,067,276; the net railway operating income $27,585,934, or a return of 7.05% on the investment. For the two years 1923-1924 the investment was $576,582,530; the net railway operating income $18,480,817, or a return of 3.21% on the investment. This road, therefore, for the same period shows practically the same loss in return on investment as the St. Paul, *i. e.*, 3.84%.

In the case of the North Western and Omaha combined the average investment in 1908-1909 was $323,107,258; net railway operating income $23,030,607; or a return of 7.13%. For 1923-1924 the average investment was $593,649,557; net railway operating income $19,532,665, or a return of 3.29%

on the investment. In the case of this road the loss in return on investment for the period in question was 3.84% compared with 3.80% in the case of the St. Paul and 3.84% for the Northern Pacific.

I think there is in the minds of some the belief that as a result of the issuance of securities for the purpose of raising funds for the construction of the Puget Sound Line the interest rate of the St. Paul is higher than those of its neighbors. A comparison of the percent that the interest is of investment in road and equipment, and the average interest rate for 1924 of the St. Paul, North Western and Omaha, Great Northern and Northern Pacific does not bear this out. These figures are as follows:

	Percent Interest is of Investment in Road and Equipment	Average Interest Rate
St. Paul	2.96	4.69
North Western and Omaha combined	2.58	4.84
Great Northern	3.71	5.56
Northern Pacific	2.63	4.63

In looking back and considering the decision made at that time it must be remembered that in the early years of the twentieth century the increasing commerce of the Orient, the expansion of the lumber industry and the agricultural and industrial boom in the Pacific Northwest, gave promise to the railroads in that territory of considerable long-haul tonnage yielding attractive revenues. It must also be remembered that at that time the development and result of water competition through the Panama Canal was not foreseen.

It is true that due, at least in part, to low rates on water traffic through the Panama Canal, and the agricultural depression in the Northwest territory, which has retarded the development of that section of the country, the Puget Sound Extension has not earned the interest on its cost. Nevertheless, it is my belief that with adequate rates, and a removal of the present restrictions which will permit the railroads to compete with water rates via the Panama Canal, or protection by regulation of such water rates by the Interstate Commerce Commission, and with the development of the territory served by the St. Paul, west of the Missouri River, which is bound to take place, the Puget Sound Extension will, ultimately, show satisfactory returns.

The question of whether the Extension is justified, and those who were responsible for it, as well as those who invested their money in the enterprise, should be condemned for lack of judgment, is best measurd by whether the property values created as a result of its construction exceed its cost.

The freight density of the main line of the St. Paul west of the Twin Cities for 1923 was 2,260,000 net tons per mile of road, and for 1924, 2,060,000 in comparison with 2,840,000 for the Great Northern in 1923 and 2,420,000 in 1924, and 3,310,000 in 1923 and 3,030,000 in 1924 for the Northern Pacific.

There is a general impression that the business of the Puget Sound Extension has largely been drawn from the other transcontinental lines serving that territory. This is not so.

The Exhibit 5 which I now introduce shows the business originating or terminating at points west of the Missouri River, and what proportion of this business moved from or to non-competitive points served by the St. Paul lines only. From this exhibit it will be seen that for the year 1924 the revenue accruing to the lines west of the Missouri River amounted to $24,407,900, of which $15,384,825, or 63%, was derived from business originating or terminating at non-competitive stations. The ton miles producing this revenue amounted to 2,563,534,779, of which 1,777,124,646, or 69.3%, was from non-competitive business. These figures show clearly that at least two-thirds of the business originating or terminating on lines west of the Missouri River, is to or from points local to the St. Paul, and not served by other railroads.

As of December 31st, 1924, the investment in road and equipment of lines west of the Missouri River was $252,748,872. That the abandonment of a line with the business indicated by the above freight density figures would cause a loss in property values in the territory it serves considerably in excess of its cost will hardly be disputed. If this is so, and these lines are a public necessity and their abandonment would be destructive of large property values and inimical to public interests, then the conclusion must be that the enterprise was justified.

I now offer the following exhibits:

Exhibit 6 showing the cost of construction of the Puget Sound Extension, as of the date of operation, August 9, 1909, additions and betterments and extensions from that date to December 31, 1924.

Exhibit 7 showing for the same period, by lines and years, charges for extensions constructed and purchased.

Exhibit 8 being a map showing the lines west of the Missouri River as placed in operation August, 1909, and the additional mileage added since that date.

The construction of the Puget Sound Extension commenced in April, 1906, and the line was opened for through freight traffic in July, 1909, and for through passenger traffic in September of the same year. As of that date there had been expended on road and equipment $99,506,000 and the mileage constructed and in operation was 1,399.83, of which 1,249.42 miles were owned and the balance was jointly owned and operated under trackage rights.

As of December 31, 1912, the investment of the Puget Sound Company had increased to $177,425,086, and the miles of road operated to 2,081, of which 1,942 miles were owned, the balance being jointly owned and operated under trackage rights.

As of December 31, 1924, the investment west of the Missouri River had increased to $252,748,872 and the miles of line in operation to 3,057, of which 2,871 were owned, the balance being jointly owned and operated under trackage rights.

The cost of the additional mileage, together with the cost of additions and improvements made since December 31, 1912, has increased the investment to $252,748,872.

From June 30, 1909, to December 31, 1917, the system mileage in operation increased from 7,512 to 10,305; investment in road and equipment from $274,468,163 to $602,334,419; funded debt from $114,732,500 to $380,829,255;

interest on funded debt from $5,855,718 to $16,596,624; operating revenues from $61,296,041 to $113,739,202; operating expenses from $39,950,134 to $85,195,964; and net income available for interest and dividends from $18,-967,918 to $21,065,255. The balance available for dividends on preferred and common stock decreased from $13,112,200 to $4,468,631.

From earning its fixed charges three times over in the ten-year period June 30, 1900, to June 30, 1909, in 1917 its earnings were only one and one-quarter times the fixed charges. This was the situation as to capitalization and earnings when I became President of the Company.

I found the roadway and track and fixed property in general to be in good physical condition. As to equipment, the case was somewhat different. There were not enough cars, and a large number of them were of a design inadequate to meet the modern conditions of long and heavy trains. There were not enough locomotives, and they were of a tractive effort too low to permit of the economies in operation resulting from increased train loads.

No doubt the drain on the company's finances in the building of the Puget Sound Extension and equipping it, and also the unsatisfactory return from this investment, together with the desire to maintain dividends on what had long been a gilt-edged investment stock, accounts for the failure to maintain an adequate amount of equipment of modern design and capacity.

An adequate quantity of freight locomotives and cars is of first importance to a railroad in maintaining and increasing its business. Inability to supply the demand for cars is expensive to shippers, and consequently, damaging to a company's good will and revenues. When business is good, the lack of the necessary equipment to meet the demand of shippers can never be supplied from the ownership of other roads. I believe the St. Paul's revenues have been affected to some extent by a lack of equipment, and soon after becoming connected with the company I realized that it would be necessary to make heavy expenditures to overcome the situation. This has been done in the case of locomotives. The company now has an adequate supply of them, both as to number and tractive effort. In the case of freight cars, however, while the situation has been greatly improved through rebuilding existing equipment and purchasing new, heavy expenditures still remain to be made in order to meet retirements of existing equipment, the average age of which is between eleven and twelve years, and to provide additional equipment necessary to handle present and prospective business of the company.

I now introduce Exhibit 9 showing a comparison between the St. Paul, Northern Pacific, Great Northern, North Western and Omaha, and Chicago, Burlington & Quincy R. R. of owned and leased equipment as of December 31, 1924.

During the period December 31, 1917, to December 31, 1924, 317 locomotives, including 17 electric, have been purchased at a cost of $18,889,914 and 18,105 freight cars at a cost of $35,774,931. During the year 1925 a total of 6,500 freight cars were purchased at a cost of $12,359,530.

From January 1, 1918, to December 31, 1920, little need be said, as owing to war-time conditions and post-war readjustments, operating revenues and expenses were so affected as to afford little value for comparative purposes.

The Chicago, Milwaukee & St. Paul Railway was taken over by the Federal Government midnight December 31, 1917, and returned to its owners

midnight February 28, 1920. The property was operated at a great loss by the Director General, and when it was returned to its owners they were confronted with inadequate revenues, a high scale of wages and a troubled labor condition. This situation was relieved somewhat by congressional legislation creating the six months guaranty period which provided that the standard return paid as rental during the period of Federal control would be continued for the six months March 1, to August 31, 1920, inclusive, so as to enable the owners to readjust themselves to the conditions resulting from the war.

During this period the operating revenues aggregated $451,423,583, operating expenses $425,453,931, with a net loss before interest charges of $10,-009,029, leaving a deficit of $50,980,919 for the period. The miles of road operated increased from 10,305 on December 31, 1917, to 10,620 on December 31, 1920, and the funded debt from $380,829,255 to $409,769,088 respectively.

The first two years of the period January 1st, 1921, to December 31, 1924, were ones of struggle in meeting and overcoming the disturbed conditions resulting from the war which caused a severe business reaction in the territory of the Northwest served by the St. Paul. In the agricultural districts of the middle West and Northwest, due to the wartime prices of wheat and corn, land had greatly risen in value, and as a result of the deflation which took place with the close of the war and the falling off in prices, production decreased, unemployment increased, credits were frozen and interest rates were high; crops which had been sown at a high cost in 1920 and 1921 were sold on a falling market.

These conditions produced great financial difficulty resulting in the closing of many banks. In the four years 1921 to 1924, fifty-four banks closed in Iowa, forty-two in Minnesota, ninety-nine in South Dakota and forty in Montana. The situation became so serious that in February, 1924, a conference was called at Washington by President Coolidge at which were present Secretary Hoover and other representatives of the Administration, together with representatives from the larger financial and business interests of the country. As a result of this meeting the Agricultural Credits Corporation was organized with an authorized capitalization of $10,000,000 for the purpose of giving financial aid to the farming interests in the so-called Pacific Northwest, comprising in part Minnesota and North and South Dakota and Montana.

In 1922 the production of the bituminous coal fields ceased, owing to a strike which began April 22nd and lasted until September 1st of the same year. This not only entailed a loss in revenue to the St. Paul—as well as other railroad companies—but increased the operating cost by reason of the higher prices it was necessary to pay for coal, which were felt for a long time after the strike ended.

On account of the troubled labor conditions resulting from the war, as already referred to, the railroad was confronted with further difficulties in the form of the shopmen's strike, which lasted from July 1, 1922, to September 15, 1922. This strike caused both an increase in the cost of maintenance of equipment and a shortage of locomotives and cars with a consequent loss of traffic. The effects of this strike were not overcome until many months after it terminated.

For the roads in the Western District and the Northwestern Region the period 1916 to 1924, inclusive, has been marked by rising costs and reduced

revenues. Any comparison of these roads with the roads in other parts of the country will show that they have had poorer net earnings.

The stock market over a period of time accurately reflects the value of a business based upon its earning power. If the earnings are good the stock will sell at a figure which will reflect that condition. If the earnings are poor the price will reflect that condition likewise. I now introduce Exhibit 10 showing for the St. Paul, the North Western and Omaha combined, Northern Pacific, Great Northern and Soo Line the market value of the common and preferred stocks of those companies as reflected by sales on the New York Stock Exchange during the year 1916 and the first eight months of 1925. It will be seen that the shrinkage in the market value of those stocks during the past nine years totals the figure of $625,000,000, or 55.8% of the market value in 1916. Excluding the St. Paul, the shrinkage in whose securities amounted to $231,000,000, or 87.8% the loss in sales of the securities of the other four roads amounted to $394,000,000, or 46%.

This condition must be due to one or more of the following circumstances, or a combination of all:

That these roads are not as efficiently operated and managed as the roads in the Eastern and Southern Districts.

That they have not enjoyed the same growth in business, or

That the rates on the commodities they handle do not yield the same margin of profit as the rates on the commodities handled by the roads in other sections of the country.

I now introduce Exhibit 11 which is a graphical analysis for the period 1916 to 1924, inclusive, showing for the St. Paul, Class 1 roads in the Northwestern Region and Western District, exclusive of the St. Paul, and for the Eastern and Southern Districts combined, certain comparisons as to rise in transportation service costs, the rise in transportation service rates, changes in volume of traffic, return on investment in road and equipment, and other information.

In the case of the St. Paul there has been an increase in the cost of labor between 1916 and 1924, as a result of the orders of the Railroad Administration and the Railroad Labor Board, of 84.4%. The details of these wage adjustments are shown on Page 1 of the Exhibit. As these labor increases are outside the control of the railway managements the increase in the cost of labor, in the case of the St. Paul, is believed to be typical of the increase in the case of other roads in the same territory.

The cost of material, as reflected by St. Paul purchases, has increased in the same period 67.1% and taxes 64.5%.

On page 4 of this exhibit there are shown a series of graphs or diagrams showing separately for the St. Paul, the roads in the Northwestern Region and Western District, exclusive of the St. Paul, and the Eastern and Southern Districts combined, the increase since 1916 in the cost of transportation service and the charge made for such service. These charts have been reproduced to a large size wall map which, if it may now be hung in some suitable place, will enable you to follow more easily the testimony relating to them.

In these graphs the year 1916 has been referred to a base of 100. This year was the last before the entrance of this country into the war, and reflects a normal pre-war condition. Business was good, there had been little increase

in the cost of labor and material, and there was a normal and proper relationship between the cost and the charge for transportation service.

In the case of the St. Paul the margin was a safe, if not fully adequate, one. In that year the St. Paul's net railway operating income amounted to $29,607,212, or a return of 4.92% on its investment in road and equipment, including material and supplies. With other income it had available for fixed charges and dividends the sum of $31,663,571. The standard return of the St. Paul for the period of Federal control, which was based upon the average annual net railway operating income of the three years June 30, 1914, to June 30, 1917, was $27,844,327, or 4.64% on the investment.

For the Class 1 roads in the Northwestern Region, excluding the St. Paul, the net railway operating income for 1916 amounted to $135,375,618, or 6.08% on their aggregate investment, including material and supplies. The standard return of these roads amounted to $120,138,859, or 5.31% on their investment.

For the Class 1 roads in the Western District, excluding the St. Paul, the net railway operating income for 1916 amounted to $426,442,452, or 5.79% on their aggregate investment. The standard return amounted to $367,172,-277, a return of 4.99% on investment.

These graphs show for each of the years in the period 1916 to 1924 the relationship between revenues and expenses and the spread that has taken place since 1916 due to the greater increase in the cost of, than the charge for, the service.

The upper line shows the unit cost of doing business, including a 5-¾% return, the transportation unit being the combined ton and passenger mile. This line is developed by dividing each year's total operating expenses, taxes, equipment and joint facility rents, plus a 5-¾% return on investment, but excluding all interest charges, by the combined total revenue net ton and passenger miles, and then ascertaining the percentage of increase that each year's result is over 1916. The lower line shows the operating revenue in terms of the same unit, that is, the total freight and passenger revenues divided by the combined total revenue net ton and passenger miles. The upper line represents the unit cost, including a 5-¾% return on the average production of the railroad, that is, the combined revenue ton and passenger mile, and the lower line shows the average selling price or charge levied for this same unit. The cost, plus a 5-¾% return, and the charge made, are, therefore, expressed in terms of the same unit. It necessarily follows that if a carrier is to earn a 5-¾% return over and above all costs, exclusive of interest, the lines in the graph representing the units charge and cost must coincide. The cross-hatched area between the two lines shows the spread between the unit charge and unit cost, and, consequently, the deficiency in revenues to meet cost plus a 5-¾% return.

From the diagram in the upper left-hand corner it will be seen that in 1916 the St. Paul's expenses, including a 5-¾% return, exceeded the gross revenue by 4.5%, the road earning 4.92% on investment in road and equipment, including material and supplies. In 1924 this excess of cost plus a return of 5-¾% over the revenues had increased to 15.1%. In that year the road earned 2.58% on its investment.

In the case of the roads in the Northwestern Region, excluding the St. Paul, as shown in the diagram in the upper right-hand corner, the expenses

in 1916 plus a 5¾% return, were 1.8% less than the gross revenues, the roads earning in that year 6.08% on their investment. In the year 1924 this situation was reversed; the expenses, plus a 5¾% return exceeded the gross revenues by 13.2%. The roads earned in that year 3.21% on their investment.

For the roads in the Western District, excluding the St. Paul, as shown in the diagram in the lower left-hand corner, the expenses in 1916, including a 5¾% return, for all practical purposes equalled the charge, the latter being only 0.2% greater than the cost. In that year the roads earned 5.79% on their investment. In 1924 the expenses, plus a 5¾% return, exceeded the gross revenues by 8.6%; the return in that year being 4.00%.

For the roads in the Eastern and Southern District, shown in the diagram in the lower right-hand corner, the expenses in 1916 plus a 5¾% return were 2.5% less than the revenues; the return on investment for these roads being 6.32%. In 1924 the situation reversed and expenses plus a 5¾% return were 2.0% in excess of the revenues; the return in that year being 4.83% on investment.

These diagrams have been introduced for the purpose of showing that the inadequacy of the net revenues of the St. Paul is not due to any cause of weakness inherent to it, but to conditions which it shares in common with its neighbors. It will be seen that the St. Paul's increase in the unit cost of doing business since 1916 has been less than that of the other roads in the Northwestern Region, this increase in 1923 and 1924 being for the St. Paul 56.7% and 61.6% as compared with 66.4% and 68.9% and that the increase in its unit revenue for the same years was 44.5% and 46.6% compared with 47.6% and 46.5%. I also think these diagrams will show that the unfavorable showing in respect to the net revenues of these Northwestern carriers is not due to a lack of efficiency in the management and operation of the properties, as their increase in unit cost since 1916 has been considerably less than in the case of the roads in the Eastern and Southern Districts. These increases in the case of the latter roads for 1923 and 1924 were 68.6% and 70.0% whereas their increases in the unit charge or rate for both years was 62.6%. The greater increase in rates for the Eastern and Southern roads is due to the 15% increase granted exclusively to those roads in 1917, to the larger increases granted under Ex Parte 74, and to the decreases made since Ex Parte 74 affecting commodities forming a much larger proportion of the business of the roads in the Northwestern Region than in the case of the roads in the Eastern and Southern Districts.

I now introduce Exhibit 12 showing the several rate reductions that have been made since Ex Parte 74, the commodities to which they applied and the effect on the revenues of the St. Paul as applied to the average of 1923 and 1924 volume of business.

The freight density of the St. Paul in 1923 was 2.7% in excess of what it was in 1916, and in 1924 the volume was 5% less than 1916. In the case of roads in the Northwestern Region, exclusive of the St. Paul, the increase in 1923 over 1916 was 1.2% and in 1924 there was a decrease of 6.8% over 1916. The roads in the Western District, exclusive of the St. Paul, showed an increase in 1923 over 1916 of 9.1% and in 1924, 8.5%. For the Eastern and Southern District roads the increase in 1923 over 1916 was 14.1% and in 1924, 4.5%.

These figures show that as a group the St. Paul and the other roads in

the Northwestern Region are the only ones whose volume of business in 1924 was less than it was in 1916.

The Panama Canal was opened for traffic on August 15, 1914, but the European War, which commenced in the Fall of that year, created so great a demand for the shipping of food supplies and munitions to Europe that there was little water competition in the transportation of coast-wise business. With the close of the war, however, the Canal at once began to take its place as an important factor in transportation between the Atlantic and Pacific Coasts, and on account of the restrictions imposed on the transcontinental lines in meeting this water competition, the revenues of those lines have been seriously affected.

The traffic through the canal is increasing at a high rate, and I now introduce Exhibit 13 showing the cargo tonnages for the years 1915 to 1924, inclusive, as taken from the Annual Report of the Governor of the Panama Canal, together with the tonnage that might have been transported by rail had the canal not been constructed. This exhibit shows that the tonnage moving through the canal in 1923 was 19,567,875 tons, and in 1924, 26,994,710 tons, an increase in 1924 over 1923 of approximately 38%. Of this tonnage California oil comprised 3,689,049 tons in 1923 and 8,501,010 tons in 1924, showing an increase in 1924 over other business of 16.4%. Without the Panama Canal it is doubtful whether the California oil tonnage would have moved by rail. Eliminating this, the tonnage which moved through the canal in 1924, and which, without the canal, would have had to move by rail if it moved at all, is shown in the lower half of the exhibit I have just introduced. Had this tonnage moved by rail and been equally divided between all of the transcontinental lines, including the Canadian Pacific, we estimate the increase in gross revenues of the St. Paul would be in the neighborhood of $15,000,000 per annum.

The managements of the transcontinental lines considered the question of obtaining relief under the fourth section of the Interstate Commerce Act, and finally made application to the Interstate Commerce Commission for permission to reduce their transcontinental rates to meet the water competition without at the same time having to make a corresponding reduction in rates to intermediate points. It is difficult to make an estimate of what the additional net revenue would be to the St. Paul were this fourth section relief granted, but we believe it would be approximately $1,500,000 to $2,000,000 per annum.

As to passenger business: the number of passengers carried one mile in 1923 showed a loss over 1916 of 20.9% and 28.5% in 1924. For the roads in the Northwestern Region the decrease in 1923 was 20.8% and in 1924, 24.4% For the roads in the Western District, excluding the St. Paul, the decrease in 1923 over 1916 was 1.6% and in 1924, 8.6%; for the roads in the Eastern and Southern Districts there was an increase in 1923 over 1916 of 15.2% and in 1924, 10.8%.

Although there has been an increase in passenger rates since 1916, the passenger revenue of the St. Paul in 1924 amounted to $21,768,000 compared with $19,757,000 in 1916 and $31,034,000 in 1920, or a loss of almost $10,000,000 per annum between 1920 and 1924. This loss in passenger revenues is aggravated by the fact that a corresponding reduction cannot be made in expenses, although such passenger trains as could be dispensed with were taken off. The public service demands that passenger trains be operated for

the handling of mail, express, milk and the few passengers that may want to travel. Although the passenger business in 1924 showed a decrease in volume of 28.5% over 1916, our passenger train miles in 1924 were only 2.92% less than in 1916.

This loss in passenger revenue is not a matter of rates, as there has been no reduction in passenger rates since 1920. It is due wholly to the fact that, with the construction of hard roads, the general public has taken to the use of the automobile. A partial solution of this difficulty is to require bus lines to pay a reasonable sum for the use of the highways which were constructed at the expense of the taxpayers, of which the railroads are the largest.

The question may be asked as to what the management has accomplished in offsetting these rising costs by increased efficiency in operation. While we know there has been considerable advancement in the efficiency of railroad operation during the past eight years, it is difficult to establish or prove it by figures because any comparison in dollars is valueless due to the greatly decreased purchasing power of the dollar. To make such a comparison it is necessary to have an equation factor between the cost of all classes of labor and material, and due to the many changes in wages and working conditions it is almost impossible to ascertain this accurately. For this reason the only comparison than can be made is in units other than dollars.

Some of the gains in efficiency are as follows:

The net tons per train on the average have been increased from 511 in 1916 to 680 in 1924, or approximately 33%.

The gross tons per train on the average have increased from 1196 in 1916 to 1523 in 1924, or 27.3%.

The average load per car has been increased from 20.67 tons in 1916 to 25.36 tons in 1924, or 22.7%.

The consumption of fuel per thousand gross ton miles has been decreased from 204.2 pounds in 1916 to 171.6 pounds in 1924, a decrease of 16%.

Through the acquisition of the Chicago, Terre Haute & Southeastern Railway, making available by direct connection with our own lines the coal mines of Southern Indiana, there has been a direct saving in excess of $1,000,000 per annum in the cost of company fuel.

In respect to the loss and damage freight: In 1916, with a gross revenue of $82,476,004 there was paid out, on account of these claims, a sum of $1,083,634, or 1.31388 cents per dollar of revenue received. For the years 1919, 1920 and 1921, with an average gross revenue of $113,223,481, there was paid out annually on the average $3,195,969, or 2.82271 cents per dollar of revenue received. In 1924, with a gross revenue of $124,613,957, the payment on account of loss and damage freight amounted to $1,180,890, or 0.94764 cents per dollar of revenue received. This shows an increase in efficiency in respect to these claims of 27.87%.

Six hundred and forty-nine miles of first main line over the Rocky and Cascade Mountains have been electrified, and the savings resulting therefrom amount to approximately $12,400,000, on an additional investment attendant to the electrification of $15,625,739. A complete analysis of the comparative cost of our electrical and steam operation has been made and a copy of the report is now filed as Exhibit 14 in this case.

Mr. Dynes: Mr. Byram, you have referred to the acquisition of the Chicago, Terre Haute & Southeastern Railway. I would like you to state briefly for the record the corporate history of that company, the terms of the lease, and as completely as you can the advantages which have accrued to the St. Paul as a result of this lease.

Chicago, Terre Haute & Southeastern Railway Company

CORPORATE HISTORY

The Chicago, Terre Haute and Southeastern Railway Company was chartered November 26, 1910, under the laws of the State of Indiana, as successor to the Southern Indiana Railway Company, whose properties were sold under foreclosure proceedings November 3, 1910. On November 4, 1910, the properties owned by the Chicago Southern Railway Company were sold under foreclosure and were later acquired by the Chicago, Terre Haute & Southeastern Railway Company, of Illinois. The Chicago, Terre Haute & Southeastern Railway Company, of Indiana, subsequently took over the property which had been acquired by the Chicago, Terre Haute and Southeastern Railway Company, of Illinois. The new company commenced operations January 2, 1911, and acquired the property of the Bedford Indiana Railway Company. The Bedford Belt Railway Company, the Danville Belt Railroad Company, and the Southeastern Railway Company of Illinois still retain their corporate existence. The Chicago, Terre Haute & Southeastern Railway Company, of Indiana, owns respectively 99.45%, 100% and 99.54% of their capital stock, carried at a nominal value of $3.00 on the balance sheet of the latter company.

On August 1st, 1913, a 99-year lease was entered into with the Baltimore & Ohio Chicago Terminal Railroad through which lease the Terre Haute Company acquired the use of 12.47 miles of that line commencing at a point one mile south of Chicago Heights and extending north to Harvey Junction.

By indenture of lease dated July 1, 1921, the Chicago, Milwaukee & St. Paul Railway Company acquired the use of the property of the Chicago, Terre Haute & Southeastern Railway Company for a period of 999 years, with the minor exceptions as shown on page 6 of the lease which is now introduced as Exhibit 15. This lease was approved by the Interstate Commerce Commission June 28th, 1921, see Finance Docket 1383.

Under the terms of this lease the Chicago, Milwaukee & St. Paul Railway Company assumed the payment of the principal and interest of funded and unfunded debt, which as of the date of the lease, July 1st, 1921, was as follows:

FUNDED DEBT:

	Principal	Annual Interest
Southern Indiana Railway Company 4% First Mortgage Bonds, maturing February 1, 1951	$7,287,000	$291,480
Bedford Belt 5% First Mortgage Gold Bonds maturing July 1, 1938	250,000	12,500
Chicago, Terre Haute & Southeastern Railway 5% First and Refunding Mortgage Gold Bonds, maturing December 1, 1960	4,244,000	212,200
Chicago, Terre Haute & Southeastern Ry. Income Mortgage Bonds, 5% Maturing Dec. 1, 1960	6,336,000	316,800
Chicago, Terre Haute & Southeastern Ry. 5% Equipment Gold Bonds	200,000*	10,000
Note: *Paid July 1st, 1921, to July 1st, 1923.		
UNFUNDED DEBT:		
Chicago, Terre Haute & Southeastern Ry. Demand Notes given Chicago Banks	837,000*	50,220
Note: *To be paid in five installments commencing October 1, 1921.		
Total Principal and Interest	$19,154,000	$893,200

Under a further provision of the lease the St. Paul Company agreed to pay for all or any part of the 43,000 shares of capital stock of the Terre Haute Company outstanding on the basis of $10.00 per share. As of November 18, 1925, the St. Paul Company had purchased 39,545.75 shares at a cost of $395,457.50.

The Interstate Commerce Commission has found, as of June 30, 1916, for the property of the Terre Haute Company owned and used for common carrier purposes, a final value for rate making of $20,150,000. Between June 30, 1916, and June 30, 1921, the net additions to investment, on account of additions and betterments made by the Terre Haute Company, amounted to $108,098. Adding this to the final value found by the Commission, we have the Commission's value for rate-making purposes as of June 30, 1921, without making allowance for difference in costs between 1916 and 1921, the sum of $20,258,098. The funded and unfunded debt, the principal and interest of which the St. Paul assumed, together with the payment for the capital stock outstanding on the basis of $10.00 per share, amounts to $19,584,000, or $674,098 less than the final value as found by the Commission for rate-making purposes.

The investment in road and equipment as of June 30, 1921, amounted to $25,035,860.93.

I now introduce as Exhibit 16 balance sheets of the Terre Haute Company as of June 30, 1921, and September 30, 1925.

GENERAL DESCRIPTION OF THE PROPERTY AND CHARACTER OF BUSINESS:

I now introduce as Exhibit 17 a map showing the lines of the Chicago, Terre Haute & Southeastern Railway Company and the Chicago, Milwaukee & Gary Railway, and connections with the St. Paul and other foreign carriers.

The lines of the Terre Haute extend from a point one mile south of Chicago Heights, about twenty-seven miles south of Chicago, to Westport, Indiana, and comprise as of December 31, 1924, in comparison with December 31, 1921, the following owned mileage:

	December 31, 1924	December 31, 1921
First Main	361.31	361.41
Second Main	44.41	7.64
Connecting Tracks	6.33	5.44
Yards and Sidings	218.66	196.41
Total	630.71	570.90

Through an agreement entered into by the Chicago, Milwaukee & St. Paul Railway and the Indiana Harbor Belt Railway, dated July 1, 1921, trackage rights were secured over the lines of the latter from Harvey Junction, to a connection with the lines of the Chicago, Milwaukee & St. Paul Railway, at Franklin Park, Illinois, about one mile east of the easterly end of Bensenville Yards. These trackage rights, together with those of the Terre Haute over the B. & O. C. T., and .52 miles over the Pennsylvania R. R. at Terre Haute Union Station, comprise as of December 31, 1924, in comparison with December 31, 1921, the following mileage:

	December 31, 1924	December 31, 1921
First Main	48.03	47.81
Second Main	34.92	34.92
Total Trackage Rights	82.95	82.73

PRINCIPAL TERMINALS:

The principal terminals of the Terre Haute are located at Bedford, Terre Haute, West Clinton and Faithorn.

CONNECTIONS WITH FOREIGN LINES:

Connections with foreign lines at the following points enable the St. Paul to deliver car load and less than car load freight to eastern connections instead of at Chicago, thus obtaining a larger division of the through rate, and avoiding the expense and delay of handling through the Chicago Terminals.

These connections are: Pennsylvania R. R. at Webster; New York Central at Delmar; Nickel Plate at Cheneyville; Clover Leaf at Humrick; C. & I. W. at West Dana for interchange on shipments to Indianapolis and Cincinnati; Vandalia and Big Four at Terre Haute; B. & O. at Seymour.

During the year ended December 31, 1924, the business handled over the Terre Haute amounted to 1,166,181,840 net ton miles. The bulk of this traffic, or 56%, is coal and may be separated as follows:

Company coal to C. M. & St. P.	26%
Commercial coal to stations beyond Chicago on the St. Paul or points beyond	8%
Commercial coal to stations on the Terre Haute, including Chicago	10%
Commercial coal to foreign lines	12%

The lime stone traffic from the Bedford District comprises approximately 5% of the total business handled. The balance, or 39%, is made up of grain, 7%; lumber, 5%; manufactured articles, 16%; miscellaneous and merchandise 11%.

BENEFITS ACCRUING TO THE ST. PAUL FROM THE LEASE OF THE TERRE HAUTE:

Prior to the leasing of the Terre Haute line the St. Paul Railroad, a system of over ten thousand miles, extending to the Pacific Coast, was dependent upon mines located on the lines of foreign railroads for two-thirds of its fuel requirements. The disadvantages to such a large system as the St. Paul in being so situated are, interrupted and expensive operation due to inability to insure an adequate and continuous supply of coal. Where a system has an adequate coal supply located on its own lines of railway it can assure to its coal operators a continuous and sufficient supply of coal cars and is able to make direct movement of its own trains over its own rails and avoid the delay occurring through interference with interchange business in bad weather, or during other periods when the movement through the terminals or intermediate switching line may be restricted on account of congestion.

Prior to the acquisition of the Terre Haute Railroad it was necessary for the St. Paul, particularly during the winter months, to maintain on its rails a supply of from fifteen hundred to two thousand cars of coal beyond its normal requirements so that when the supply was cut off due to bad weather or other reasons it could move this reserve supply to points where the quantity of coal on hand was low. Even with the maintenance of this reserve there were many times when it was necessary, in order to maintain operation of its trains, to confiscate coal consigned to various industries, which was not only costly but naturally created ill-feeling against the railway company. Under these conditions the same economy and consumption cannot be obtained as when all of the locomotives are adjusted, and the firemen are accustomed, to burning one grade of coal.

Since the acquisition of the C. T. H. & S. E. Ry., these operating disadvantages have been entirely eliminated and the St. Paul has been assured of a uniform and adequate supply of a good quality of steam coal. Our General Superintendent of Motive Power advises me that the Indiana steam coal has the same heat units as the Central District of Illinois coal and slightly less than the Southern District of Illinois but that when the difference in price at the mine is taken into consideration this slightly lower efficiency in heat units is more than offset by the greater quantity of coal that can be purchased for the same amount of money.

From July 1, 1920, to July 1, 1921, the last twelve months prior to the leasing of the Terre Haute, the St. Paul purchased for its own consumption 4,021,309 tons of coal. Of this tonnage, 2,678,189 tons were purchased from mines off the St. Paul lines; 171,501 tons F. O. B. lake docks, leaving a balance of 2,506,688 tons, or approximately 67% of the total company requirements, purchased from mines located on foreign lines; 1,343,120 tons, or 33%, were purchased from mines located on St. Paul rails. Of this latter tonnage 432,222 tons were purchased from mines west of the Missouri River to supply the company requirements in that territory.

For the 2,506,688 tons purchased from mines off the St. Paul lines, it paid foreign railroads freight charges totaling $2,970,425. On the basis of the present rates the freight charges on this tonnage would have amounted to $2,594,422, or $1.035 per ton.

For the first six months of 1925, 1,327,995 tons of company coal were purchased from mines on the Terre Haute for use on the St. Paul lines exclusive of the Terre Haute. The cost to the St. Paul of moving this coal from the mines to point of connection of the Terre Haute with the St. Paul rails, including all operating expenses, interest and other costs resulting from the leasing of the Terre Haute Railroad, amounted to 17.4c per ton, as compared with $1.035 per ton that would have been paid to foreign lines assuming the purchases were made from the same source as prior to the acquisition of the Terre Haute. On the basis of the coal purchased in the first six months of 1925 this represents a saving in freight charges alone of $1,144,000, or at the rate of $2,288,000 per annum.

I now introduce Exhibit 18 showing for the period July 1st to December 31, 1921, the calendar years 1922, 1923, 1924 and the first six months of 1925 the total tons of company coal purchased from mines on the Terre Haute and the total cost including all interest charges and other costs as a result of the Terre Haute lease, of moving that coal from the mine to the point of connection of the Terre Haute with the St. Paul, together with the saving over what would have been paid had this coal been transported over the Terre Haute at tariff rates. This exhibit shows that the savings amount to:

July 1st to December 31, 1921	$259,780	gain
Year 1922	148,220	Loss—coal strike
Year 1923	787,794	gain
Year 1924	1,121,013	gain
Six months of 1925	1,054,787	gain
Total for four year period	$3,075,154	gain

From these charges it will be seen that the savings in freight charges on company coal are now running in excess of $2,000,000 per annum.

Another way of stating this is that the deficit or cost of the Terre Haute to the St. Paul for the six months of 1925, after the payment of all expenses, interest charges and other costs as provided for in the lease, and taking credit for the railway operating revenues which, of course, do not include company fuel which is hauled at cost, as shown by the exhibit, amounted to $230,420. If the St. Paul had not had this lease it would have paid freight charges to foreign railroads amounting to $1,285,207, for the coal which moved over the Terre Haute at cost, and which went to make up the deficit of $230,420. The difference, or $1,054,786, is the saving to the St. Paul for the six months of 1925, on its fuel bill, and for the four years period since the leasing of the Terre Haute this saving has amounted to $3,075,154.

NEW REVENUE FROM COMMERCIAL DEVELOPMENT:

In addition to the benefits of an adequate and continuous fuel supply, and the savings in operating expenses and freight charges paid foreign lines, resulting therefrom, the development of markets for Indiana coal in the States of Wisconsin, Iowa, Minnesota and South Dakota, served by the lines of the Chicago, Milwaukee & St. Paul Railway affords a field for greatly increasing its freight revenue.

For the twelve months ended December 31, 1924 the total tonnage of commercial coal originating on the Terre Haute and destined to points beyond Chicago on or beyond the rails of the St. Paul, amounted to 530,565 tons, with freight revenue to the St. Paul of $870,395 for the haul beyond Chicago and $502,743 to the Terre Haute Railroad for the haul from the mine to Chicago, or a total of $1,373,138. This does not include commercial coal shipped to Chicago or other points on the Terre Haute. I am advised by Mr. J. T. Averitt, our Coal Traffic Agent, formerly General Freight and Passenger Agent of the C. T. H. & S. E. Ry., that this is practically all additional revenue which probably could not have been obtained as long as the Terre Haute was operated as a separate company. Mr. Averitt advises me the policy of the Terre Haute management was not to market its coal beyond Chicago for the reason that its division of the through rate to points beyond Chicago was materially less favorable than the local rate to Chicago. The pressure of the Terre Haute management on its coal operators was, therefore, not to seek markets involving long hauls beyond its own line.

For the six months ended June 30, 1925, this tonnage amounted to 269,031 tons. The revenue to the St. Paul for the haul beyond Chicago was $448,991 and for the Terre Haute Division on the haul from the mine to Chicago, $244,393. This is an increase of $46,670 over the first six months of 1924.

The development of markets for Indiana coal in the States served by the St. Paul east of the Missouri River is slow and while the progress thus far has been all that was expected it is a small part of the tonnage which it is believed will be developed in the course of future years as the coal becomes better known and its quality in comparison with coal from the Illinois fields is established.

INDIANA FIELD AS A SOURCE OF COAL SUPPLY:

The coal area of the State of Indiana is confined to a narrow strip 120 miles long and 20 to 30 miles wide, lying East of the Wabash River except at the north end where the river cuts through it. The total production of the State for the last four years averaged 21,000,000 tons per annum. According to the report of the Indiana Bituminous Coal Operators Association, the present production of coal on the Terre Haute Division in Indiana is approximately 32% of the total production within the State.

The two principal coal producing districts on the Terre Haute Railroad are what are known as the Clinton District, comprising mines located north of Terre Haute, and the Linton District, comprising the mines located south of Terre Haute.

In the Clinton District there are seventeen mines having a potential daily output of 33,000 tons. At the present time there are eleven mines in operation, the average daily production of which during October, 1925, was 13,500 tons.

In the Linton District there are thirty-one mines having a potential daily output of 36,000 tons. At the present time there are seventeen mines in operation, the average daily production of which during October, 1925, was 13,000 tons.

The life of the Indiana coal fields at the present rate of production is estimated at one hundred years.

I now introduce Exhibit 19 showing by years the earnings of the Terre Haute for the period 1915 to 1924, inclusive, and the 9 months ending September 30, 1925, together with the total interest payable on all bonds outstanding, including income bonds, and the interest paid.

The revenues from July 1, 1921, when the St. Paul took over the operation of the Terre Haute, do not include company fuel which was transported over the line at cost.

Had the Terre Haute been allowed credit at tariff rates for company fuel the net railway operating income for the year 1921 would have been $721,500 instead of a deficit of $172,008; for 1922 it would have been $794,450 instead of a deficit of $1,036,510; for 1923 it would have been $1,815,763 instead of a deficit of $894,512; for 1924 it would have been $2,297,106 instead of a deficit of $289,458; for the nine months of 1925 it would have been $2,454,324 instead of $564,669; this being the saving to the St. Paul on its transportation of company fuel. During the entire period above mentioned the interest on funded debt was paid.

The average high and low sale price of C. T. H. & S. E. First and Refunding 5% mortgage gold bonds, as reported on the New York Stock Exchange and taken from the Commercial and Financial Chronicle for the years 1918 to 1925, was as follows:

1918	58	
1919	62¾	
1920	67½	
1921	66	(6 mos. ending July 1, 1921)
....	70¾	(6 mos. ending Dec. 31, 1921)
1922	80⅛	
1923	79¾	
1924	79⅛	
Ten mos. 1925	82½	

In the case of the income bonds no sales were reported for the period ending December 31, 1923. For the year 1924 the average was 61, for the ten months of 1925 it was 69¾, the low being 55 and the high 84½. At the present time these bonds are selling from 82 to 83.

SUMMARY OF ADVANTAGES OF LEASING THE TERRE HAUTE RAILROAD:

(1) The St. Paul has secured for many years to come an adequate and uninterrupted supply of good quality coal for its own use from a field 75 miles nearer Chicago than the Southern Illinois fields, thereby avoiding the expensive operation and delay due to lack of a continuous supply which previously existed, and at the same time a saving in freight charges amounting to $2,000,000 annually.

(2) There is made available an additional source of revenue through the development of markets for this coal in the states served by the St. Paul east of the Missouri River. In the few years since the acquisition of the Terre Haute this source of revenue has been developed to a point where it approximates $1,000,000 per annum. It is expected that as the market for this coal is widened this additional revenue will be very considerably increased.

(3) Interchange connections with Eastern lines have been effected giving, on the business it is able to interchange at these points, a larger division of the through rate. With the acquisition of the Gary Road and its development, as will be explained in dealing with that road, it is possible to move business to and from the east without incurring the expense and delay attendant to the handling through the Chicago Terminal District.

(4) That for the year 1925 the Chicago, Terre Haute & Southeastern Railway will, through additional revenue on commercial coal, better divisions on eastbound business, and a saving in freight charges to foreign lines on company fuel, show a net profit to the St. Paul in excess of $3,000,000.

Mr. Dynes: Will you now please outline in a similar way the acquisition of the Chicago, Milwaukee & Gary Railway.

Chicago, Milwaukee & Gary Railway Company

CORPORATE HISTORY

The Chicago, Milwaukee & Gary Railway Company was chartered March 3, 1908, under the general laws of the State of Illinois. On October 20, 1908, it acquired by warranty deed the property of the Illinois, Iowa & Minnesota Railway Company consisting of a line of railroad extending from Momence, Ill. to Joliet, Ill. and from Aurora, Ill. to Rockford, Ill. together with all rights, privileges, agreements and franchises pertaining thereto, including trackage rights over the Elgin, Joliet & Eastern Railway between Joliet and Aurora, a distance of 23.29 miles. The right of the Illinois, Iowa & Minnesota Railway Company to use the tracks of the Elgin, Joliet & Eastern Railway was granted by agreement between the two companies dated February 21, 1905, for a period of 25 years and is automatically extended beyond that period until canceled by either party upon six months notice. This agreement contains certain restrictions as to the kind of traffic which the Illinois, Iowa & Minnesota Railway may handle over the rails of the Elgin, Joliet & Eastern, details of which will be referred to hereafter.

Under date of October 20, 1908, the Chicago, Milwaukee & Gary Railway Company acquired by warranty deed the entire property of the Rockford Belt Railway Company, consisting of 3.16 miles of track serving industries located within the city of Rockford.

The mileage obtained by these two purchases was as follows:

	Main Line	Side Track
Illinois, Iowa & Minnesota Ry.	91.92	14.04
Rockford Belt Railway	3.16	....
	95.08	14.04

The Chicago, Milwaukee & Gary Railway during September, 1909, constructed a main line extension from Momence, Ill., to a connection with the Chicago, Terre Haute & Southeastern Railway at Delmar, Ill. a distance of 3.35 miles.

Trackage rights in the city of Momence connecting its tracks north and south of that point were obtained from the Chicago, Indiana & Southern

(succeeded by the New York Central R. R.) under agreements dated June 19, 1909, and July 22, 1909, which were later canceled and succeeded by agreement dated July 13, 1923, between the Chicago, Milwaukee & Gary and the New York Central Railroad for a period of 10 years, from the date thereof, and is automatically extended beyond that date until canceled by either party upon 90 days written notice.

As of January 1, 1922, the Chicago, Milwaukee & St. Paul Railway Company acquired control of the Chicago, Milwaukee & Gary Railway pursuant to the terms of agreement dated December 31, 1921, between the Chicago, Milwaukee & St. Paul Railway Company and the St. Louis Union Trust Company, Syndicate Manager, owner and holder of all the securities of the Chicago, Milwaukee & Gary Railway consisting of $1,000,000 capital stock and $5,798,000 First Mortgage 5% Gold Bonds due April 1, 1948. By the terms of that agreement the St. Louis Union Trust Company delivered to the Chicago, Milwaukee & St. Paul Railway Company all of said capital stock, $2,700,000 of said bonds and canceled $98,000 principal amount of said bonds, all in consideration of the Chicago, Milwaukee & St. Paul Railway Company guaranteeing the payment of $3,000,000 principal amount of said bonds and the interest accruing thereon after January 1, 1924. The terms of this agreement were approved by the Interstate Commerce Commission February 11, 1922, see Finance Docket No. 2141.

Owing to the physical condition of the property, interest on the $3,000,000 principal amount of bonds guaranteed by the Chicago, Milwaukee & St. Paul Railway Company was waived from January 1, 1922, to January 1, 1924, in recognition of the expenditures necessary to bring the property up to the standard of maintenance required for the operation of traffic such as the Chicago, Milwaukee & St. Paul Railway Company contemplated putting over this line. Interest which was thus waived amounted to $300,000 and during the year 1922 under the management of the Chicago, Milwaukee & St. Paul Railway Company there was spent for maintenance of way and structures $439,663; in 1923, $167,928; and in 1924, $157,588 as shown on the attached statement which I now introduce as Exhibit No. 20.

A copy of the indenture dated December 31, 1921, between the Chicago, Milwaukee & St. Paul Railway Company and the St. Louis Union Trust Company is introduced and filed as Exhibit No. 21.

The Interstate Commerce Commission has not as yet found a final value of the Chicago, Milwaukee & Gary Ry. It has, however, reported as of June 30, 1915, for property owned and used for common carrier purposes a tentative value for rate making purposes of $2,889,475. Between June 30, 1915, and January 1, 1922, the investment in road and equipment was reduced $183,027 as a result of retirements. Deducting this from the tentative value found by the Commission, we have as the Commission's tentative value for rate making purposes as of January 1, 1922, without making allowance for difference in costs between 1915 and 1922, the sum of $2,706,448 or $293,552 less than the principal amount of First Mortgage 5% Gold Bonds assumed by the St. Paul.

The investment in road and equipment as of December 31, 1921, amounted to $6,803,296.14.

I now introduce as Exhibits Nos. 22 and 22 balance sheets of the Chicago, Milwaukee & Gary Railway Company as of December 31, 1921, and Sept. 30, 1925.

GENERAL DESCRIPTION OF THE PROPERTY AND CHARACTER OF BUSINESS

Reference is made to map previously introduced as Exhibit No. 17 showing the lines of the Chicago, Terre Haute & Southeastern Railway Company and the Chicago, Milwaukee & Gary Railway Company and connections with the St. Paul and other foreign carriers. The line of the Gary extends from point of connection with the Chicago, Terre Haute & Southeastern Railway at Delmar, Ill. approximately 50 miles south of Chicago, in a northeasterly direction through Momence, Joliet, Aurora, DeKalb and Kirkland, crossing the tracks of the Chicago, Milwaukee & St. Paul Railway at Kirkland, Ill., and extending to another connection with the Chicago, Milwaukee & St. Paul Railway Company tracks at Rockford, Ill., and comprised as of December 31, 1924, in comparison with December 31, 1921, the following owned mileage:

	December 31, 1924	December 31, 1921
Main track	96.96	96.83
Yards and sidings	31.33	30.23
Total	128.29	127.06

Trackage rights acquired with the acquisition of the Chicago, Milwaukee & Gary Railway over the rails of the Elgin, Joliet & Eastern between Joliet and Aurora and over the New York Central at Momence comprised as of December 31, 1924, in comparison with December 31, 1921, the following mileage:

	December 31, 1924	December 31, 1921
Main track	24.24	24.24

PRINCIPAL TERMINALS

The principal terminals of the Gary are Delmar, Rockford and Joliet, Illinois.

CONNECTIONS WITH FOREIGN LINES

Connections with foreign lines are made at the following points: New York Central and Chicago & Eastern Illinois at Momence; Wabash at Manhattan; Chicago & Alton, Atchison, Topeka & Santa Fe and Elgin, Joliet & Eastern at Joliet; Chicago, Burlington & Quincy, Chicago & Northwestern and Elgin, Joliet & Eastern at Aurora and Chicago & Northwestern at DeKalb. The exchange of business with foreign connections at these points is not large. The volume of business via the Terre Haute and Gary destined to points west on foreign lines connecting with the Gary is still undeveloped. It is anticipated, however, that as business increases and the importance of the Gary develops as an outer Belt Line an increasingly large amount of traffic will be exchanged with foreign lines thereby avoiding the use of the Chicago Terminals as a transfer point between Eastern and Western Lines.

During the year ended December 31, 1924, the business handled over the Chicago, Milwaukee & Gary amounted to 148,912,351 net ton miles. The bulk of this traffic or approximately 82% is coal originating on the Terre Haute, the remainder of the traffic is as follows:

Manufactured Articles	8%
Products of Agriculture	4%
Stone	3%
Miscellaneous & Merchandise	3%

BENEFITS ACCRUING TO THE ST. PAUL FROM THE ACQUISITION OF THE GARY

In connection with the acquisition of the Chicago, Terre Haute & Southeastern Railway by the Chicago, Milwaukee & St. Paul Railway Company, the Chicago, Milwaukee & Gary Railway through its connection with the Terre Haute at Delmar and the St. Paul at Kirkland, forms an important connecting link between those two lines. It affords an uninterrupted route for the supply of coal for railroad use from mines on the Terre Haute to points south and west of Milwaukee, particularly during a peak business and during times of traffic congestion in the Chicago Terminals due to weather conditions. What is true of the movement of company coal is also true of commercial coal and other west bound business moving into the St. Paul's territory.

By means of the acquisition of the Gary, the St. Paul is enabled to enter into competition with other carriers in handling business originating in quarries at Bedford destined to or beyond the Kansas City gateway and similarly business originating at Terre Haute and destined to or beyond the Omaha-Kansas City gateway.

The full benefit of the Gary road will not be derived until it builds its own line of railroad from Joliet to Aurora.

Under the contract with the Elgin, Joliet & Eastern the Chicago, Milwaukee & Gary Railway cannot handle over the lines of the Elgin, Joliet & Eastern between Joliet and Aurora traffic destined east of the Illinois-Indiana State Line to points on the Elgin, Joliet & Eastern, Chicago, Lake Shore & Eastern or lines connecting with those roads. As the Elgin, Joliet & Eastern and the Chicago, Lake Shore & Eastern have connections with practically all of the principal eastern carriers, the restrictions thus imposed prevent the St. Paul from diverting east bound business at Kirkland over the Gary for delivery to Eastern Lines having connections with the Terre Haute and securing a larger division of the through rate.

The income account for the Chicago, Milwaukee & Gary since its acquisition by the Chicago, Milwaukee & St. Paul Railway shows a deficit after interest charges for the period to September 30, 1925, of $896,187.88, made up by periods as follows:

Year 1922	$629,291	Deficit
Year 1923	212,639	"
Year 1924	77,660	"
Nine Months ended Sept. 30, 1925	33,402	Surplus
Total Deficit	$896,188	

Since its acquisition by the St. Paul the deficit in the income account of the Gary has been reduced each year until now the first nine months of 1925 show a profit of $33,402 after paying all expenses, taxes and interest charges.

The Gary has terminals at Rockford serving a number of important and valuable industries. These industries are now served by the St. Paul as a result of its connections with and control of the Gary.

Since January 1, 1921, when the Gary was acquired, the St. Paul's proportion of freight earnings on traffic forwarded from and received at Rockford for the years 1918 to 1924 inclusive and the first nine months of 1925 are as follows:

1918	$445,288	Average per Annum $452,302
1919	443,279	
1920	511,659	
1921	408,982	
1922	751,724	Average per Annum $848,996
1923	937,241	
1924	772,061	
Nine Mos. of 1925	722,710	

This increase alone justifies the purchase of the Gary Road.

The St. Paul's proportion of freight earnings from business in and out of Rockford Station for the four years 1918 to 1921 inclusive, prior to the acquisition of the Gary averaged $452,302 per annum and for the three years nine months since its acquisition the average annual earnings have been $848,996 or an increase of $396,694 per annum which for the three years nine months amounts to $1,487,602. This increase, after making allowance for the cost of handling, about offsets the deficit of the Gary for the same period.

The full possibilities of the Gary and its value to the St. Paul System will only be realized in future years when, with its own line between Aurora and Joliet, it will afford to the St. Paul a through connection with the Terre Haute and Eastern Lines for the growth in business which will come with the expansion and development of the Western territory and enable it to avoid the increasingly difficult and expensive operations through the Chicago Terminals.

SUMMARY OF THE ADVANTAGES OF ACQUIRING THE CHICAGO, MILWAUKEE & GARY RAILWAY

(1) The St. Paul has secured an outlet for its company coal originating on the Terre Haute and destined to points south and west of Milwaukee thereby avoiding the expense and delay of movement through the Chicago Terminals.

(2) It has obtained a strategic position for the future handling of business both east and westbound and through foreign line connections with the Terre Haute, will with the construction of the line between Aurora and Joliet be provided with a channel for the interchange of business with Eastern roads without passing through the Chicago Terminals.

(3) The St. Paul enjoys a large and increasing business at its Rockford Station which amounts at the present time to over $500,000 a year more than prior to the acquisition of the Gary.

Mr. Dynes: Please state briefly what efforts were made to fund the obligations maturing in 1925 and whether you endeavored to obtain assistance from the United States Government.

It has been suggested that there was undue haste in calling for a Receivership of the property and that had sufficient effort been made by the Board of Directors a Receivership might have been avoided, and particularly, if the aid of the Government had been sought such a consequence might have been avoided. To show what was done in this direction I submit the following.

In June, 1924, I requested four of the Directors, Mr. Fisher, Mr. Geddes, Mr. McHugh and Mr. McRoberts to cooperate with me as a Special Committee for the purpose of developing, if possible, some practicable plan to meet the bonds maturing in 1925. This Committee had many meetings during the summer and fall and considered, I think, every possible means to provide for this maturity and avoid a Receivership. A number of different plans were considered, several of which included making an effort to secure a voluntary exchange of securities on the part of the holders of 1925 bonds, and a thorough canvass was made to ascertain the holders of these securities, both in this country and in Europe, and through this effort about 70% of the holders were located. But the value of the company securities which could have been offered in exchange for the 1925 securities was 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. In such cases there are always a certain percentage of holders who will not agree to make an 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 the holders of 1925 securities who might not be willing to go along with such a voluntary exchange.

Besides this, if it had only been a question of meeting the 1925 securities, even if it could have been accomplished, it seemed plain that unless provision could be made for the other obligations maturing the following nine years, taking care of the 1925 maturities would have afforded only temporary relief.

I now introduce Exhibit 23 showing the company's obligations maturing during the period 1925 to 1934, inclusive, totaling $209,925,315. Consequently, we came to the conclusion that any practical plan of refinancing the company's maturities would necessarily include provision for not only the 1925 maturities but also the other maturities falling due soon thereafter.

Consideration was given to the possibility of issuing new securities to meet the refunding of these maturities. Members of Division Four of the Interstate Commerce Commission were consulted for the purpose of ascertaining whether they would approve the release of the $18,000,000 of the company's General Mortgage 5% Bonds pledged as collateral for the company's loan through a substitution of the equivalent value of the company's General and Refunding Mortgage Bonds. The members of Division Four indicated that they desired to be helpful in every way and would approve with the consent of the Secretary of the Treasury such an arrangement if it was necessary to meet the securities maturing in 1925 and would at the same time solve the company's financial difficulties. However, as the company was not earning its fixed charges and had no marketable assets other than these General Mortgage bonds, the Board did not feel it would be justified in asking permission of the United States Treasury to make such substitution which would only postpone and not permanently solve the financial difficulties of the St. Paul Company.

Also for the reasons which have been covered in my testimony the credit of the company was such that no refunding on a large scale was possible, and even if it were the rate of interest on the new securities would necessarily be higher than on the old ones, thus increasing instead of decreasing the company's financial load. With its liquid assets used up in refinancing proceed-

ings there would be no reserve funds available to meet the deficiencies which might accrue in poor years between the net income and fixed charges, and it was the belief of the Board that an attempt to carry out such a program would in the end ultimately mean a default and Receivership proceedings after the exhaustion of all the company's liquid assets.

As to the question of whether the Interstate Commerce Commission could give aid by means of a loan from the fund created under the "recapture" clause in the Transportation Act, I had on Friday, Oct. 17, 1924, an informal conference with Messrs. Meyer, Potter and Eastman, members of Division Four of the Interstate Commerce Commission, at which Mr. Mahaffie, Director of Finance, was present. The general financial situation of the Milwaukee was discussed and I explained our difficulties, particularly as to the 1925 maturities. At this conference I was given definite assurance that if we required the release of the $18,000,000 General Mortgage Bonds pledged with the United States Treasury as collateral by the substitution of the equivalent market value of the General and Refunding Mortgage Bonds, it could probably be arranged and also that the Government loan due in 1927 could be renewed for five years in order to get it out of the way of short term financing to meet the 1925 maturities.

I brought up the question of a possible loan from the recapture earnings fund, but was given to understand that a comparatively small sum had been paid in on account of such excess earnings and that those amounts had been paid under protest by the carriers. Therefore, it was clear that under these conditions no funds could be made available from that source for loans to assist in meeting our difficulties.

I also had a meeting with Secretary of the Treasury and was advised by him that although the Government was desirous of being helpful to the St. Paul Company with a view of avoiding a Receivership, there was no authority under the law whereby any financial aid could be given by the Government.

In a further effort to improve the credit of the St. Paul Railway an effort was made to secure action of Congress toward the passage of legislation which would reduce the interest rate on loans made by the Government to the railroads during Federal Control, which rate of interest was fixed at 6% by the law and could only be changed by action of Congress. This Company was then carrying loans with the Government aggregating $55,000,000 on which a 6% rate of interest was being paid. Congress was asked to pass legislation reducing the rate of interest on these loans to an amount not exceeding the cost of such money to the Government, approximating 4¼%. I appeared before the Senate Interstate Commerce Committee in January, 1925, in behalf of the proposed bill and pointed out the serious financial situation of the St. Paul Company in regard to refinancing its June, 1925, maturities and the great benefit that would be derived by favorable action on legislation reducing the interest rate as proposed, and which would have the result of reducing our interest charges on these loans approximately $1,000,000 per year, and which amount really represented that much profit to the Government above the cost of Government borrowing at the present time. We were disappointed in our efforts in this direction as Congress adjourned without passing the desired legislation.

I am satisfied in my own mind that every possible way of meeting this maturity and avoiding a Receivership was considered by the company's

bankers and its Board of Directors. It seemed clear that on account of the fixed charges and large maturities falling due in the next few years and the unsatisfactory earnings of the company, the Board of Directors would have failed in its duty if it had attempted to carry on under the present capital structure of the company.

But before reaching a definite conclusion the Board decided to employ the well known firm of Consulting Engineers, Coverdale & Colpitts, to make an independent report on the financial and other prospects of the company. This firm made an exhaustive study of the physical and financial condition of the St. Paul Company and reported to the Board that in their opinion there was no possible way of solving it other than a reorganization. A copy of this report will be filed with the Commission as an exhibit in these proceedings. The Board also 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 in the future, which indicated results similar to those reached by Coverdale & Colpitts.

After reaching the conclusion that a reorganization of the company's finances was necessary and which entailed a receivership, the Board made a frank statement to the public and parties in interest, giving the reasons which governed their action in deciding that their course was necessary. A copy of the statement will be submitted for this record.