FINANCE DOCKET No. 12637

DELAWARE, LACKAWANNA & WESTERN RAILROAD COMPANY RECONSTRUCTION FINANCING

Submitted December 15, 1939. Decided January 8, 1940

1. Delaware, Lackawanna & Western Railroad Company, on the basis of present and prospective earnings, found reasonably to be expected to meet its fixed charges without reduction thereof through judicial reorganization.
2. Upon application, purchase for itself by the Reconstruction Finance Corporation, at a price not in excess of their principal amount and accrued interest of not to exceed $3,100,000 of 2½-percent, 10-year, serial equipment-trust certificates, series C, obligations of the Delaware, Lackawanna & Western Railroad Company, when issued as proposed, approved.

Douglas Swift for applicant.

REPORT OF THE COMMISSION

DIVISION 4, COMMISSIONERS PORTER, MAHAFFIE, AND MILLER

BY DIVISION 4:

The Delaware, Lackawanna and Western Railroad Company on November 10, 1939, filed an application requesting the purchase by the Reconstruction Finance Corporation, hereinafter called the Finance Corporation, under the provisions of section 5 of the Reconstruction Finance Corporation Act, and acts amendatory thereof and supplementary thereto, of not to exceed $3,100,000 of its proposed equipment-trust certificates. Under the provisions of the acts mentioned, the Finance Corporation, notwithstanding any limitation of law as to maturity, may, with our approval, including approval of the price to be paid, to aid in the financing of railroads engaged in interstate commerce, purchase for itself, or for account of a railroad obligated thereon, the obligations of such railroads, including equipment-trust certificates. We have made the required investigation.

We have previously approved a loan of $2,000,000 to the applicant by the Finance Corporation, due November 30, 1943. *Delaware, L. & W. R. Co. Reconstruction Loan*, 230 I. C. C. 361.

The application.—The Finance Corporation is to purchase the equipment-trust certificates so as to enable the applicant to acquire for its own use under lease, and eventually to own, additional equipment consisting of 500 all-steel boxcars, 500 all-steel hopper cars, and 100 all-steel gondola cars, estimated to cost approximately $3,100,000.

The equipment is to be financed by an equipment trust under the so-called Philadelphia plan for the entire cost, not to exceed $3,100,000, to be liquidated in 10 years and 1 month by 20 equal semiannual payments of $155,000 starting at the end of 7 months from the date of the trust. The certificates under the trust will be designated as series C and are to be noncallable. The terms of the trust, lease, and trust certificates are more fully stated in our report in *Delaware, L. & W. R. Co. Equipment Trust Certificates*, 236 I. C. C. 538, issued concurrently herewith, wherein we authorized the assumption of obligation and liability by the applicant in respect of the certificates and their sale as proposed.

It is proposed by the applicant that the Finance Corporation purchase at par all of the equipment-trust certificates necessary to cover the net cost of the above-described equipment but not to exceed $3,100,000. The certificates will bear interest at 2½ percent per annum. In consideration of such interest rate, the applicant agrees to expend for labor and material for construction in its shops and maintenance on its railroad of its equipment, during the 14 months commencing November 1, 1939, and ending December 31, 1940, $1,240,000 over and above $5,619,316, representing the average annual expenditure for maintenance of its equipment during the last 7 years. The applicant further requests that if the Finance Corporation, as an aid to any railroad in financing the acquisition of equipment, grants any more favorable interest basis than is here applied for the Finance Corporation will accord the applicant the benefit of the more favorable basis. In that connection our approval herein of the proposed financing should not be construed as approval of the acquisition by the Finance Corporation of certificates of the proposed issue calling for interest at a rate other than 2½ percent per annum. In our opinion, the price to be paid by the Finance Corporation should include interest accrued thereon from the date of issue of the certificates.

The Finance Corporation, under the proposed plan, is to deposit with the trustee of the equipment trust, contemporaneously with the actual delivery of the equipment in installments from time to time by the manufacturers or vendors of the equipment to the trustee, cash for the purchase of the certificates in an amount sufficient to pay the estimated net cost of the equipment. The applicant is to be obligated for interest only from the time that each deposit is made. The securities will be guaranteed by the applicant and secured by the equipment to be purchased under the trust agreement and lease.

The applicant avers that it is unable at this time to obtain additional funds for the purchase of equipment in whole or in part from any other source upon terms which are reasonable and acceptable to it; that its usual banking connection has refused a further loan and terms of other banks are unacceptable; and that it believes that it cannot secure additional funds by the sale of its bonds to the public in the present condition of the bond market, without unwarranted sacrifices. It likewise avers that no agreement has been made or will be made by it to pay any person, association, firm, or corporation, either directly or indirectly, any commission or fee for or in connection with the purchase by the Finance Corporation of the proposed equipment-trust certificates, and that no such payments have been or will be made by the applicant.

Necessities of the applicant.—The applicant states that in its judgment the present volume of its traffic and that which reasonably may be anticipated requires the procurement of the additional freight-train cars applied for.

The applicant's property, traffic, and valuation were discussed in *Delaware, L. & W. R. Co. Reconstruction Loan, supra.* For the year ended December 31, 1938, the five leading commodities and the tonnage handled were 6,621,598 tons of anthracite coal, 2,479,122 tons of bituminous coal, 1,860,979 tons of manufactures and miscellaneous, 1,036,529 tons of rough stone, and 821,743 tons of cement.

There are outstanding $2,681,000 of equipment-trust certificates, series A, due 1949, and $667,000 of series B, due 1944. There are no other obligations maturing in the near future.

Earnings and financial structure.—During the period from 1932 to 1938, inclusive, the applicant has incurred yearly deficits in net income as follows: $2,542,447, $2,993,862, $1,972,613, $2,932,305, $132,847, $936,772, and $3,954,954, respectively, totaling $15,465,800. However, during the same period the total depreciation charges of $18,000,938 exceeded total deficit by $2,535,137. The yearly depreciation charges for the foregoing period were, respectively, $2,552,991, $2,606,687, $2,517,368, $2,696,701, $2,655,514, $2,507,474, and $2,464,203. Thus only in 1933, 1935, and 1938 did the applicant's deficit exceed its depreciation charges during that 7-year period. For the first 9 months of 1939 railway operating revenues and expenses were $36,561,012 and $28,507,846, respectively. Income available for fixed charges during the same period amounted to $4,539,233, with a deficit of $1,291,534 after fixed charges. For September 1939 net income of $394,639 remained after fixed charges as contrasted with deficits of $480,028, $194,456, $299,518, $388,168, and $445,029 for February, March, June, July, and August, respectively. In January, April, and May net income amounted to $9,005, $45,637, and $66,384, respectively. For the entire year 1939, with 9 months actual and 3 months estimated, the applicant forecasts operating revenues of $50,559,512, operating expenses of $38,225,846, income available for fixed charges $7,657,782, and a deficit after fixed charges of $144,605, whereas, on the same basis, depreciation charges will be $2,434,260. The applicant stresses the fact that, in view of the present and prospective economic conditions, it believes that it will be able to earn all its fixed charges, and shows that for the last 4 months of 1939, on the basis of actual figures for September and estimates for the last 3 months, it will earn its fixed charges and have a surplus of $1,541,568.

The balance sheet of the applicant as of August 31, 1939, showed total current assets of $7,798,906, including cash $4,243,789, material and supplies $1,589,375, traffic and car-service balances receivable $761,988, and miscellaneous accounts receivable $732,868. Total current liabilities were $6,996,796 and included audited accounts and wages payable $2,974,443, traffic and car-service balances payable $741,293, loans and bills payable $950,000, and unmatured rents accrued $1,868,247. Tax liability amounted to $4,870,187, and total corporate surplus was $53,469,697. At the beginning of the current year the actual cash balance was $2,716,430. On the basis of the $6,010,058 cash balance on hand on October 31, 1939, the applicant forecasts a cash balance of $3,056,258 on January 1, 1940.

Conclusions.—We conclude:

1. That the applicant may reasonably be expected, on the basis of present and prospective earnings, to meet its fixed charges without reduction thereof through judicial reorganization.

2. That we should approve the purchase by the Finance Corporation, for itself, at a price not in excess of their principal amount and accrued interest, of not to exceed $3,100,000 of 2½-percent equipment-trust certificates, series C, obligations of the applicant, when issued substantially as proposed in the application.

An appropriate certificate of approval will be issued.