FINANCE DOCKET NO. 26522[1]

ERIE LACKAWANNA RAILWAY COMPANY BONDS MODIFICATION

Decided July 22, 1971

1. In F. D. No. 26522: (a) Upon application by Erie Lackawanna Railway Company, the requisite statutory findings made for approval and authorization of alteration and modification of the Erie Railroad Company Ohio Division First Mortgage 3 1/4-Percent Bonds due September 1, 1971, issued and outstanding under and secured by the Erie Railroad Company Ohio Division First Mortgage, dated as of September 1, 1941; and (b) Authorization granted applicant to submit, in specified manner, the proposed alterations or modifications, with terms and conditions determined to be just and reasonable, to the holders of said Bonds for acceptance or rejection.
2. In F. D. No. 26523, request by Erie Lackawanna Railway Company for authority under section 20a, dismissed.
3. In F. D. No. 21494: (1) Consent requested by Erie Lackawanna Railway Company for modification, under section 505 of part V, of outstanding loan guaranty by releasing certain of the pledged collateral, denied, and (2) Consent under said section 505 granted for modification of said loan guaranty in all other requested respects, subject to conditions.
4. In F. D. No. 21495, authority under section 20a granted to Erie Lackawanna Railway Company to annex and imprint notations on outstanding 5 1/4-percent collateral notes of Erie-Lackawanna Railroad Company reflecting the aforesaid approved modifications.

Richard Johnson for applicant.
Irving D. Friedman, intervenor in support, pro se.

REPORT OF THE COMMISSION

DIVISION 3, COMMISSIONERS TUGGLE, BUSH, AND GRESHAM

[1]This report also embraces F. D. No. 26523, Erie Lackawanna Railway Company Bonds; F. D. No. 21494, Erie-Lackawanna Railroad Company Loan Guaranty; and F. D. No. 21495, Erie-Lackawanna Railroad Company Securities.

BY DIVISION 3:

NATURE OF PROCEEDING

On February 10, 1971, the Erie Lackawanna Railway Company (EL or Applicant) filed an application seeking the requisite consent and statutory[2] authorizations to effect a proposal (hereafter sometimes called the Plan) which is designed primarily to postpone the impending maturity of the Erie Railroad Company Ohio Division First Mortgage 3 1/4-Percent Bonds (Bonds) from September 1, 1971, to May 1, 1980. Pursuant to the requested authority under section 20b of the act, the Plan would also alter and modify accordingly the Erie Railroad Company Ohio Division First Mortgage, dated as of September 1, 1941 (Mortgage), pursuant to which the Bonds were issued as well as other substantive provisions of both instruments. In aid of these alterations and modifications, the Plan would additionally modify certain provisions of an outstanding loan guaranty[3] and of the notes[4] thereby guaranteed, viz the modifications would primarily postpone certain sinking fund payments. The application also seeks the requisite consent under section 505 and authorization under section 20a for this aspect of the Plan.

As indicated, the Plan is designed to accomplish two major objectives: (1) extension of the maturity of the Bonds, and (2) deferral of certain sinking fund payments with respect to the Notes. The Bonds mature on September 1, 1971, and the sinking fund payments to be deferred are contractually required to be made on June 1, 1971. In view of the urgency of time and other reasons therein stated, our order entered February 25, 1971, assigned for hearing only that portion of the application which relates to extending the maturity of the Bonds[5] and in addition found that due and timely execution of the Commission's functions imperatively and unavoidably requires omitting issuance of a report and recommended order by the presiding hearing examiner. Accordingly, this report will dispose of all matters embraced by the application.

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[2]Unless otherwise indicated, all references to statutory provisions are to the Interstate Commerce Act, as amended.

[3]The guaranty was authorized and approved by order dated June 8, 1961, in F. D. No. 21494, *Erie-Lackawanna Railroad Company Loan Guaranty*.

[4]Known as the Applicant's 5 1/4-Percent Collateral Notes (hereafter called Notes), they were issued under a Collateral Trust Indenture dated as of May 1, 1961 (Indenture).

[5]The request under section 20b (designated as F. D. No. 26522) and the related section 20a portion of the application (designated as F. D. No. 26523).

At the hearing which was held on April 5, 1971, in Washington, D.C., Irving Friedman, who holds other obligations of EL, was permitted to intervene in support of the application. No representation with respect to the application was made at any time by any State authority.

THE APPLICATION

More specifically, the application (as supplemented and amended)[6] seeks an order or orders:

1. Authorizing and approving the modification of: (a) the loan guaranty evidence by the Guaranty Agreement, dated as of May 1, 1961 (Guaranty Agreement),[7] (b) the pertinent Loan Agreements, which are dated as of May 1, 1961, (c) the Indenture,[8] and (d) the Notes. Authorization and approval in these respects is sought (i) in accordance with paragraph 5(a) of the Guaranty Agreement in order to obtain the Commission's written consent to such modifications under section 505 of part V of the act, and (ii) under section 20a of the act to obtain authorization for stamping, on the face of the Notes and of the Consolidated Note, a Notation reflecting such modification.

2. Authorizing and approving under section 505 and under section 20a of the act, the modification of certain provisions of the guaranty, the Indenture and the Notes in order to provide that: (a) three sinking fund payments[9] will be deferred until June 1, 1976; (b) in substitution for the deferred sinking fund payments, there shall be (so long as any Notes are outstanding) contingent sinking fund payments payable on June 1 of each year beginning with 1973 in accordance with a specified formula; (c) the rate of interest payable on the Notes will be increased from 5 1/4 percent to 6 3/8 percent effective June 1, 1971; (d) interest on overdue amounts of principal on the Notes will be payable at the rate of 7 percent per annum; (e) specified securities whose aggregate principal amount is $1,017,500 will be released from the pledge of collateral under the Indenture; (f) the Notes will be registered notes and will not carry the privilege of being exchanged for coupon notes, or of coupon notes being registered as to principal;

[6]The initial application was amended by Supplemental Applications Nos. 1, 2, and 3, respectively filed on March 15, 1971, May 17, 1971, and June 24, 1971. Subsequent amendments were effected by filing on July 2, 1971, the most recent revisions of: (a) exhibit 2 (the Plan), and (b) exhibit 6D (the proposed Supplemental Indenture to the Mortgage).

[7]The Guaranty Agreement is between the United States of America, acting by and through the Interstate Commerce Commission, and First National City Bank of New York (the predecessor of First National City Bank), as trustee.

[8]The Indenture is between the Erie-Lackawanna Railroad Company (the predecessor of EL) and the First National City Bank of New York (the predecessor of First National City Bank), trustee.

Erie-Lackawanna Railroad Company was created October 1960 through the merger of two railroads pursuant to authorization given in *Erie R. Co. Merger*, 312 I.C.C. 185. Effective April 1, 1968, that company was merged into EL and since that date EL has operated as a wholly owned subsidiary of Dereco, which in turn is controlled by N&W pursuant to an order dated June 24, 1964, authorizing the so-called N&W-Nickel Plate-Wabash unification.

[9]Due on June 1 of each of the years 1971, 1972, and 1973. The payment which was due on June 1, 1971, was temporarily deferred until December 1, 1971, pursuant to authorization granted by our order dated May 26, 1971, in F. D. Nos. 21494 and 21495 *(Erie-Lackawanna Railroad Company Loan Guaranty* and *Erie-Lackawanna Railroad Company Securities*, respectively).

and (g) the above-described modifications will be set forth in a Modification Agreement to be attached to each of the Notes, and a Notation with respect thereto will be stamped on the Notes.

3. Authorizing giving the Commission's written consent (pursuant to paragraph 5(a) of the Guaranty Agreement) (a) to the modification of the Indenture and the Notes; and (b) to the extension of the pledge of collateral under the Indenture (which secures the Notes).

4. Authorizing giving an opinion of the General Counsel for the Commission on or before the date of the lenders' consent in compliance with the requirements of section 5.5 of the First Amendatory Loan Agreement.

5. Authorizing and approving the alteration and modification of: (a) certain provisions of the Mortgage, pursuant to which the Bonds were issued, and (b) the outstanding Bonds accordingly, such modification to be evidenced by annexing a prescribed form of Extension Agreement and by stamping or imprinting a prescribed form of endorsement. Authorization and approval in these respects is sought under section 20b of the act in order to provide that: (a) the maturity date of the Bonds will be extended from September 1, 1971, to May 1, 1980; (b) the interest on the Bonds will be increased from 3 1/4 percent to 7 percent effective September 1, 1971, and will be payable in semiannual installments on May 1 and November 1 in each year until maturity, the first payment at the increased rate to be made November 1, 1971; (c) interest on overdue amounts of principal on the Bonds and, to the extent enforceable under applicable law on overdue amounts of interest, will be payable at the rate of 7 3/4 percent per annum; (d) the sinking fund provision for the Bonds will be changed from semiannual payments of $90,000 to a payment of $1,250,000 on May 1, 1972, and thereafter quarterly payments of $313,000 and $312,000, alternately payable on February 1, May 1, August 1, and November 1 of each year, the first such quarterly payment to be made on August 1, 1972, in the amount of $313,000; (e) so long as any Bonds are outstanding, there shall be contingent sinking fund payments in accordance with a prescribed formula dependent upon the amount of EL's working capital; and (f) the Bonds will be all registered Bonds and there will no longer be a privilege of exchanging such Bonds for coupon bonds registered as to principal.

The application also makes certain other requests which the urgency of time makes it advisable to consider subsequent to the issuance of our order herein since the requests relate to matters such as approval of certain forms of documents, appointment of a depositary and authority to consummate the Plan. As amended, the application contemplates appending an Extension Agreement to the Bonds and omits the alternative request initially made in F. D. No. 26523 for authorization under section 20a of the act pertaining to modification of the Bonds and the Mortgage pursuant to section 20b. At the hearing the examiner questioned the necessity or propriety of seeking authority under section 20a with respect to the section 20b aspects of the application. Upon further consideration of this matter, El's counsel concluded that this particular request is not necessary or proper and by letter dated May 11, 1971, this request was withdrawn. In the circumstances the portion of the application embraced by F. D. No. 26523 will be dismissed.

DETAILS OF NOTES AND BONDS

The Notes.—The Notes are fully guaranteed as to the payment of principal and interest by the United States of America under part V of the act. Of the $15 million principal amount originally issued, $12 million are presently outstanding in denominations of multiples of $1,000, all of which are held by five insurance or banking institutions. The Notes mature on June 1, 1976, bear interest at the rate of 5 1/4 percent per annum payable semiannually and are entitled to the benefit of a sinking fund requiring annual payments which are applied pro rata to the outstanding Notes. Article 4 of the Indenture provides for issuance of a Consolidated Note by EL to the trustee, such note to be completed by the trustee and delivered to the Commission if and when the trustee, having become entitled so to do under the Guaranty Agreement, shall make a demand upon the Commission, calling for the purchase by the United States of America from the trustee of the rights and remedies of the holders of the Notes. Upon the trustee's receipt of the purchase price, the Consolidated Note would become effective and supersede the Notes.

The Bonds.—Of an original issue in the aggregate principal amount of $18 million, there are now outstanding Bonds in the principal amount of $12,245,000. The Bonds bear interest at the rate of 3 1/4 percent per year payable semiannually on March 1 and September 1 and are entitled to sinking fund payments of $90,000 on March 1 and September 1 of each year. They mature on September 1, 1971. They were issued under the Erie Railroad Company Ohio Division First Mortgage dated as of September 1, 1941, and upon the merger of The Delaware, Lackawanna and Western Railroad Company into Erie Railroad Company on October 17, 1960, the obligation of the Mortgage continued to be carried by Erie-Lackawanna Railroad Company. Upon the merger of that company into EL on April 1, 1968, EL assumed the obligation of the Mortgage by supplemental indenture dated as of April 1, 1968. The Bonds are secured by a first lien on 303 miles of EL's main line,[10] by a first lien on certain branch lines,[11] and also by a third lien on another of EL's lines.[12]

More than 75 percent of the aggregate principal amount of the Bonds is held by fewer than 25 holders. $11.7 million principal

[10] Between Salamanca, N.Y., and Marion, Ohio.

[11] To Dayton, Cleveland, and Lisbon, Ohio, and to Sharon and Oil City, Pa.

[12] The line between Pymatuning and New Castle, Pa.

amount of the Bonds, or about 95 percent of the total outstanding principal amount, are owned by banking and insurance companies. The holders of $572,000 principal amount, or about 5 percent of the total, are unknown.

LONG-TERM DEBT

As of December 31, 1970, EL's long-term debt totaled $326,148,235, consisting of $171,702,050 mortgage bonds, $21,567,850 collateral trust bonds, $47,143,250 income bonds, $26,576,200 miscellaneous obligations, $57,100,977 equipment obligations, and $2,057,908 amounts payable to affiliated companies. As of March 31, 1971, the total long-term debt declined to $322,461,788 of which $22,651,080 is due within 1 year.

SYNOPSIS OF PLAN

Applicant's Plan[13] is designed to achieve two major objectives: (1) deferral of certain sinking fund payments on the Notes, and (2) an extension of the maturity of the Bonds for approximately 9 years. While both involve modification of existing contractual obligations, achievement of the first requires—from a regulatory standpoint—authorization under section 20a for the changes which are mutually agreeable to the contracting parties. On the other hand, the proposed modifications affecting the Bonds require authorization under section 20b. Because the primary objectives are interdependent, the Plan consists of two parts, one relating to the Notes and the other to the Bonds.

With respect to the Notes, the Plan provides that:

(1) Three sinking fund payments[14] will be deferred and will become payable at maturity of the Notes on June 1, 1976.

[13]The Plan sets forth the modifications and alterations proposed to be made in both the Bonds and the Notes. Initially it was filed as exhibit 2 attached to Supplemental Application No. 1. As amended at the hearing, it was received in evidence as exhibit H-3 (these amendments are set forth in a letter dated April 13, 1971, which was received in evidence as exhibit H-10 pursuant to rule 86 of our General Rules of Practice). In accordance with the understanding at the hearing, paragraph 3 of the Plan was made definite by counsel's letter dated May 5, 1971, and subsequently a revised version was filed as exhibit 2 attached to Supplemental Application No. 2. Another revision was filed as exhibit 2 attached to Supplemental Application No. 3 and the most recent version appears as exhibit No. 2 filed on July 2, 1971.

[14]$750,000 due on June 1, 1971, and the other two, each in the amount of $2,250,000 due June 1 of 1972 and 1973. Since consummation of the Plan could not be achieved prior to June 1, 1971, the interim deferral of the $750,000 payment until December 1, 1971, is provided for in a proposed Deferral Agreement (see exhibit 6X).

(2) The rate of interest on the Notes will be increased from 5 1/4 percent to 6 3/8 percent effective June 1, 1971. Interest on any overdue principal and on any amounts advanced by the trustee under section 7.02(H) of the Indenture will be at the rate of 7 percent.

(3) If, however, the alterations and modifications of the Bonds and Notes, as described in the Plan, do not become effective by December 1, 1971, (a) the sinking fund payment which (prior to the recent amendment[15]) was due on June 1, 1971, will be payable on December 1, 1971, with interest for that 6-month period at the rate of 6 percent; and (b) except in respect of the deferral of that one sinking fund payment and of the other amendments effected by the Second Indenture, the Notes and instruments relating to their issuance will continue in being as originally drawn and the obligations of the parties will be deemed unchanged.

(4) Of the collateral pledged under the Indenture, securities[16] aggregating $1,017,500 in principal amount will be released.

(5) The Notes will also be entitled to a contingent sinking fund in each year beginning with the year 1973 in a principal amount equal to 20 percent of the amount by which EL's working capital (as at the end of its fiscal year immediately preceding the sinking fund payment date of June 1) exceeds the sum of the working capital (as at the beginning of such immediately preceding year) and $5 million. However, no such contingent sinking fund payment shall be required in any year when EL's working capital (as at the end of the immediately preceding fiscal year) is less than $10 million and no such contingent sinking fund payment shall exceed $2,250,000 in any year.

(6) All Notes will be registered Notes without coupons and will not have the privilege of exchange for coupon notes or registered notes with coupons.

With respect to the Bonds, the Plan proposes the following alterations and modifications:

(1) The maturity date will be extended from September 1, 1971, to May 1, 1980.

(2) The semiannual sinking fund payments of $90,000 will be changed to a sinking fund payment of $1,250,000 payable on May 1, 1972, and thereafter quarterly sinking fund payments of $313,000 and $312,000 alternately payable on February 1, May 1, August 1, and November 1 of each year, the first such quarterly payment to be made on August 1, 1972, in the amount of $313,000. Upon receipt, sinking fund payments will be applied to the redemption of Bonds in accordance with a specified procedure.

[15]That is prior to execution of the Second Supplemental Indenture, dated as of June 1, 1971 (Second Indenture).

[16]The securities are:

The New York, Lackawanna & Western Railway Company First and Refunding Mortgage Bonds

Series A—4 percent, 1973 -----	$559,000
Series B—4 percent, 1973 -----	308,000

The Delaware, Lackawanna & Western Railroad Company First and Refunding Mortgage Bonds (New York, Lackawanna & Western Division)

Series C—5 percent, 1973 -----	150,500
Total ---------------------------	1,017,500

(3) The interest rate will be increased from 3 1/4 percent to 7 percent effective September 1, 1971, and will be payable semiannually on May 1 and November 1 in each year until maturity in 1980. The first payment of interest at the increased rate will be made on November 1, 1971. Interest on any overdue principal and, to the extent enforceable under applicable law, on any overdue interest will be at the rate of 7 3/4 percent.

(4) Beginning with 1973, the Bonds will also be entitled to a contingent sinking fund payment in each year in a principal amount equal to 10 percent of the amount by which EL's working capital (as at the end of its fiscal year immediately preceding the sinking fund payment date of May 1) exceeds the sum of the working capital (as at the beginning of such immediately preceding year) and $5 million. No such contingent sinking fund payment, however, shall be required in any year when EL's working capital (as at the end of the immediately preceding fiscal year) is less than $10 million. The contingent payment, if any, is to be made once in each year and no such annual payment shall exceed $1,250,000.

(5) After the Plan becomes effective, all Bonds will be issued in the form of registered bonds without coupons. Bonds shall be redeemable by application of sinking fund payments in the manner specified in the proposed supplemental indenture to be dated as of September 1, 1971 (Proposed Indenture),[17] between EL and the trustee under the Mortgage. All of the respects in which the provisions of the Mortgage and the rights of the holders of the Bonds will be altered and modified upon effectiveness of the Plan are set forth in the Proposed Indenture.

The Proposed Indenture provides for the annexation to the Bonds of so-called Extension Agreements and the stamping or imprinting on the Bonds of Notations for the purpose of evidencing the alterations and modifications as well as the rights of the bondholders in accordance with the Plan. The Proposed Indenture declares that on and after September 1, 1971, the Mortgage and each Bond and the rights of the bondholders shall be deemed modified and altered accordingly, regardless of whether or not an Extension Agreement shall be annexed and whether or not a Notation shall be imprinted. After the effective date of the Proposed Indenture, outstanding Coupon Bonds will be exchanged for registered bonds. The Proposed Indenture includes an appropriate form of Extension Agreement and Notation and in addition to provisions extending the maturity of and interest on the Bonds, amending the sinking fund provisions as described above, and requiring appropriate modification and alteration of each Bond delivered for that purpose, there are also other customary and appropriate provisions (*e.g.*, governing transfer, exchange, and redemption of the Bonds, continuing the lien of the Mortgage, et cetera).

[17]Proposed Indenture refers to the version filed on July 2, 1971.

DEVELOPMENT OF PLAN

In July 1970 EL retained, as financial advisor in connection with the approaching maturity of the Bonds, the largest underwriter of fixed income securities in the United States, a firm which is also regarded as outstanding in the field of railroad obligations. After examination of EL's financial structure and of the overall market for rail securities (which was very unfavorable for nonequipment obligations) the financial consultant concluded that a new issue of EL securities secured by the Ohio Division Line even with a substantially improved sinking fund would be difficult if not impossible to place. Hence, the consultant recommended that the only feasible means of handling the maturity of these Bonds is to obtain an extension of maturity under the provisions of section 20b and over a period of 8 months the above-described Plan was developed in consultation with EL's management and individually with major holders of the Bonds.

FINANCIAL POSITION

Its financial advisor and its senior vice president both expressed the opinion that EL has neither the cash nor the credit to obtain the cash needed to pay the Bonds at maturity. The carrier's poor cash position is confirmed by its financial statements[18] for the calendar years 1969 and 1970. Particularly noteworthy is the loss of $10.9 million sustained in 1970. EL's inability to refinance the Bonds through borrowing or other conventional methods appears from the financial advisor's detailed testimony describing present and foreseeable conditions in the railroad securities market. Suffice it to note the evidence showing that: (a) in the short period[19] between May 1 and August 1, 1970, the market for railroad securities disintegrated; (b) subsequently the market for railroad equipment obligations recovered to a large degree; but (c) the recovery of market position has not proceeded as promptly for nonequipment obligations; and (d) in the existing and foreseeable market conditions, it would be difficult if not impossible to effect a refunding of the outstanding Bonds.

[18] The general balance sheets and the income statements for both years are attached. See appendixes A and B, respectively.

[19] On June 21, 1970, Penn Central Transportation Co. filed a petition for reorganization under section 77 of the Bankruptcy Act.

According to its senior vice president, the loss of $10.9 million in 1970 foreclosed any prospects which EL had for paying the Bonds in cash. Indicative of EL's inability to pay is the fact that in both years its current liabilities ($45,784,189 in 1969 and $56,666,557 in 1970) exceeded its current assets ($42,947,600 in 1969 and $41,235,549 in 1970). Indeed these figures also reflect a substantial deterioration in EL's financial position, its deficit in working capital having increased almost sixfold in 1 year (from $2.8 million to $15.4 million)—a deficit which increased another $1.4 million during the first 3 months of 1971. Also indicative of the deterioration in its financial position is the fact that its total assets show a decline of almost $10 million in this 15-month period (from $468.3 million on December 31, 1969, to $458.4 million on March 31, 1971). Its cash and temporary investments also reflect the decline, from $7.6 million in 1969 to $6.3 million in 1970 but rose slightly to $6.5 million[20] as of March 31, 1971.

EL attributes its present financial difficulties to a series of unanticipated reverses[21] which began in 1969. The carrier emphasizes that these reverses blunted the substantial progress which EL had made in recent years in increasing the efficiency of its operations and improving its physical facilities, and particularly so following its affiliation with Norfolk & Western Railway Company. Such progress, EL believes, enabled it to pay off at maturity on October 1, 1969, $11,006,000 of its First Consolidated Series E Bonds. However, as a result of the unanticipated reverses its cash is at a low level and there is no prospect of an improvement sufficient to meet the maturity of the Bonds on September 1, 1971.

[20]EL's balance sheet as of the date so indicates and apparently the $5.3 million figure given by EL's vice president is erroneous.

[21]In 1969 EL allegedly suffered a decline of 34,000 carloads of traffic (representing an estimated loss of $9.5 million in revenues) as a result of disruptions by the Penn Central Transportation Company of the interchange at Maybrook. In July of that year severe flooding in the Midwest caused loss of traffic, detours, and an expenditure of $297,000 to restore three main-line bridges which were destroyed or badly damaged. Unusually severe weather conditions during the winter of 1969-70 substantially increased operating and per diem expenses and reduced revenues and as a result applicant sustained a loss of over $5 million in the first quarter of 1970 instead of the profit which had been anticipated. The General Motors strike in 1970 cost EL about $1.2 million in revenues and the bankruptcy of the Penn Central suspended payment to EL of approximately $1 million in cash which was owed primarily for interline balances and per diem for the period preceding the bankruptcy. EL's difficulties were compounded by the slackening of business which began in the second half of 1969 and continued through 1970 and also by the serious inflation which has continued since 1967. A combination of these two factors resulted in higher costs while business was declining and, as a consequence of a recently enacted statute (PL 91-541) signed on December 10, 1970, applicant owes $5.1 million in back wages to members of four labor organizations.

Despite the severe squeeze on EL's cash, its president is optimistic concerning the railroad's future prospects, emphasizing that the carrier has devoted even greater vigor to its program of cost control while at the same time aggressively pursuing steps to improve its business prospects, to increase its operating efficiencies, to keep abreast of its equipment needs, and to maintain its property in the best possible physical condition. A substantial reduction in personnel has been effected, from a level of 17,024 in 1964 to 13,684 in 1970. Nevertheless, there has been a substantial increase in gross ton-miles, from 30,064,639 in 1964 to 34,166,754 in 1970. Gross revenues increased from $212.5 million in 1964 to $262.2 million in 1970. Substantial sums have also been expended for maintenance of way and equipment and for increasing the efficiency of its equipment fleets. Also, the problem of passenger train losses has been substantially resolved and EL has also effected a number of coordinations with its sister company, Delaware & Hudson Railway Company, to improve the efficiency of operation of properties of both railroads.[22] Other activities have also been coordinated, including purchases and stores and motor power and rolling stock repairs. The resulting savings are being shared. If EL is given the opportunity to exhibit its true potential in earning power, he believes, sufficient funds will be generated internally to meet the new maturity date of the Bonds.

THE ISSUES

Since the Plan contemplates that the proposed modifications relating to the guaranty aspects of the application would be effected by consent of all holders of the Notes, section 20b of the act is not applicable to this portion of the Plan. In this regard the threshold question is whether consent should be given to the requested modifications of the existing contractual provisions of the loan guaranty. Section 505 of part V of the act expressly empowers us to grant such consent if we deem it equitable to do so.[23] Hence, the primary issue with respect to the guaranty aspects of the application

[22]These coordinations include the establishment in Cleveland of a locomotive power control center which controls the distribution and use of locomotives on both railroads. Also, EL's and D&H's data processing systems are being integrated.

[23]Section 505 reads: "The Commission may consent to the modification of the provisions as to rate of interest, time of payment of interest or principal, security, if any, or other terms and conditions of any guaranty which it shall have entered into pursuant to this part, or the renewal or extension of any such guaranty, whenever the Commission shall determine it to be equitable to do so."

is whether the requested modifications are equitable. A negative determination with respect to any request would, of course, require denial of the particular request. An affirmative determination, on the other hand, with respect to any request involving altering the terms of the outstanding Notes would invoke the provisions of section 20a of the act. So would any modification of the Guaranty Agreement if the modification would result in altering the Notes; for it is now well established that section 20a requires "Commission authorization of agreements to alter those securities over which Congress did give the Commission jurisdiction." *United States* v. *New York, N. H. & H. R. Co.* (1959), 276 F. 2d 525, 532, certiorari denied 262 U.S. 959; *Boston Term. Co. Reorganization,* 312 I.C.C. 373, 384. Hence, to the extent that our consent under section 505 involves modifications of that nature, our approval for their effectuation must be based upon making the two findings specified in paragraph (2) of section 20a. That is, we must find that the proposed modifications (a) are for some lawful object within Applicant's corporate purposes and compatible with the public interest, which is necessary or appropriate for or consistent with the proper performance by EL of service to the public as a common carrier, and which will not impair its ability to perform that service, and (b) are reasonably necessary and appropriate for such purpose.

The remainder of the application pertains to modification of the Bonds with the consent of less than all of the bondholders. Hence its disposition is governed by the provisions of section 20b of the act, which prescribes that, before causing a plan of alteration or modification to be submitted to affected security holders for acceptance or rejection, we must make four findings whose essence is that the proposed plan for modifying outstanding securities (a) is within the scope of paragraph (1) of section 20b; (b) will be in the public interest; (c) will be in the best interests of the carrier, of each class of its stockholders, and of the holders of each class of its obligations affected by such modification or alteration; and (d) will not be adverse to the interests of any creditor of the carrier not affected by such modification or alteration. Where, as here, the proposal involves the issuance of securities within the meaning of section 20a,[24] section 20b additionally requires that we also make

[24]It is well established that attachment of the Extension Agreement to the outstanding Bonds constitutes an issuance of securities within the meaning of section 20a. Indeed, the provisions of section 20a are invoked even where no physical alteration is involved and, notwithstanding the absence of any provision either for changing the text of the Bonds or for attaching thereto a supplementary or amendatory instrument, an issuance of securities is involved if the proposed modifications would operate to alter a substantive provision or characteristic of the outstanding Bonds. See *Boston Term. Co. Reorganization,* 312 I.C.C. 373, 385.

the two previously described findings specified in paragraph (2) of section 20a. Hence, with respect to the section 20b aspects of the application the requested approval may be given only if we make all six of the above-described findings.

Since the proposal to modify the Bonds is the heart of the Plan, that aspect will be considered first.

SECTION 20b ASPECTS

Necessity and reasonableness of Bonds modification.—This record permits only one conclusion: the proposed modification of the Bonds is both necessary and reasonable. The Bonds, now outstanding in the aggregate principal amount of $12,245,000, mature September 1, 1971. Its financial condition leaves no room for doubting that EL will not have the cash to discharge the Bonds at maturity and the evidence supports the opinion of EL's financial advisor that under present and foreseeable conditions in the railroad securities market the carrier will not be able to refund or refinance the Bonds by conventional methods and that the only feasible means of avoiding default when these bonds mature is to obtain an extension under the provisions of section 20b. This appraisal of the situation is shared by EL's management and apparently also by major holders of the Bonds who were consulted in developing the proposed Plan. The evidence is unequivocal that, unless the impending maturity of the Bonds can be deferred, reorganization proceedings under the Bankruptcy Act are virtually inevitable. With such a short time remaining before maturity, this record compels the conclusion that modification of the Bonds as set forth in the Plan represents the sole prospect of avoiding such reorganization proceedings.

It is equally apparent from the evidence that, in the light of EL's circumstances, the proposal is also reasonable. Applicant's present plight is the result of a net working capital deficit of $15 million and the loss of approximately $11 million in 1970. In the opinion of the supporting intervenor, who is a registered representative and bond specialist employed by a member of the New York Stock Exchange, these deficits are temporary and the railroad's operations should become profitable[25] in 1972 and 1973. In his opinion EL "has a good

[25] EL's controller was more conservative. In his opinion, the present deficit and working capital of $15 million will be reduced at the end of 1971 to approximately $13 million and, with the recent freight rate increase, the carrier will be able to generate a net income which will continue to reduce the working capital deficit.

going business and in spite of its poor financial record, it can even be called a growth company," as is apparent from the fact that its total railway operating revenues rose from $243 million in 1968 to $251 million in 1969 and $262 million in 1970. This view harmonizes with the rationale underlying development of the Plan. EL's financial advisor explained that May 1, 1980, was selected as the new maturity date because the additional time thus afforded is the shortest period over which projected cash flows indicate that it will be possible to provide for the regular amortization[26] of the extended Bonds without impairing the financial structure of EL or restricting the company's flexibility to meet its other continuing borrowing requirements. In brief, regardless of the differing opinions concerning the time when EL is expected to become profitable, the evidence indicates that this Plan is needed in order to afford the company the opportunity and the time to work its way out of its present financial difficulties.

The evidence also indicates the reasonableness and necessity of the new interest rate. In its initial form, the Plan provided for increasing the interest on the Bonds from 3 1/4 percent to 6 percent. This increase was determined as the culmination of negotiations with the largest bondholder, Metropolitan Life Insurance Company, concerning the terms of the extension. Subsequently the Plan was amended to increase the rate to 7 percent because certain large bondholders with holdings sufficient to defeat the Plan demanded 7 1/2 percent and indicated that they would not support the Plan at the 6-percent rate. EL estimates that over the entire extended period, the additional 1-percent increase will cost about $308,000. Its officials consider this to be a substantial sum but they regard the obligation as necessary in order to assure approval of the Plan and are confident of EL's ability to pay this additional interest. The evidence indicates that the new rate would reasonably compensate the holders for their reinvestment of moneys and at the same time would not prove unduly burdensome to EL in its efforts to become financially viable pursuant to the Plan.

At present EL does not have sufficient cash flow to increase its sinking fund payments on the Bonds as well as to satisfy the proposed interest rate increase. Indeed, because existing provisions[27] relating to the Notes would intensify its critical cash

[26]The almost sevenfold increase in sinking fund payments, which the Plan provides, will retire 80 percent of the Bonds by their maturity in 1980. The orderly retirement of indebtedness thus made possible will permit EL to begin a systematic reduction in its burdensome debt.

[27]Under existing contractual arrangements, the sinking fund payments on the Notes are scheduled to increase from an annual rate of $750,000 in 1971 to an annual rate of $2,250,000 in 1972 and thereafter to maturity.

squeeze, the Plan also provides for deferring three sinking fund payments until maturity of the Notes in 1976—a deferral which, in addition to enabling EL to make the annual sinking fund payment of $1,250,000 on the Bonds, is expected to permit improving EL's working capital by over $2 million during 1972 and 1973. Also helpful is the provision for the additional sinking fund payments (which are contingent upon specified improvements in EL's working capital). It will give EL the opportunity to rebuild its financial strength while at the same time allocating a share of any substantial future prosperity to the holders of the Bonds as well as holders of the Notes.

Interests of public, EL, creditors, and stockholders.—EL's financial advisor believes that the Plan represents a fair accommodation of the interests of all involved or affected parties and the record shows the specific reasons why the witness considers it fair to EL, to the holders of the Bonds, to the holders of the Notes, and to the holders of other EL securities. Insofar as EL is concerned, the Plan would enable the railroad to meet a maturing mortgage obligation in an orderly manner and to begin to make some reduction in its bonded indebtedness. For the holders of the Bonds the new 7-percent interest rate not only would be a substantial increase but would also provide reasonable compensation for their reinvestment of moneys. The Plan would also benefit the bondholders by providing an increase of nearly 700 percent in the fixed annual sinking fund payments and also by affording the opportunity of receiving even greater sinking fund payments and accelerated retirement of their obligations whenever the carrier's working capital position attains the specified level of improvement.

The Plan is also fair to other creditors. Insofar as the holders of the Notes are concerned, the Plan would not change the Government-guaranteed status of the Notes and the new higher interest rate represent a rate on the deferred sinking fund payments which is comparable to the holders' reinvestment opportunities. Holders of other EL securities would also be benefited because the Plan provides a means of avoiding the burden, expense, and risk of a reorganization proceeding under the Bankruptcy Act.

EL's president expressed great concern about the impact of bankruptcy proceedings on a carrier's ability to operate and serve the public efficiently. The institution of such a proceeding, he emphasized, immediately places certain restrictions which are legally required on the ability to manage the railroad during the pendency of such proceedings. These restrictions not only delay effecting decisions pertaining to the management and operation of the company but also greatly increase the difficulties of retaining and holding good management. Also, the legal ramifications of the reorganization proceedings require substantial amounts of time.

EL's financial circumstances as disclosed by this record confirm the foregoing views concerning both the Plan and the threat of bankruptcy. As for the adverse consequences of a reorganization proceeding under the Bankruptcy Act, suffice it to observe that a usual result of bankruptcy is deterioration of the service afforded to the public; for a trustee in bankruptcy is as much concerned with the conservation of assets for the benefit of creditors as with the maintenance of a service required by the public. *Boston & Maine Corp. Bonds Modification,* 328 I.C.C. 150, 175. Interruption of employment also usually attends bankruptcy and, should EL collapse because of inability to meet the muturity of the Bonds on September 1, 1971, it is likely that deterioration of service combined with unemployment would create hardship within the area served by the railroad.

The impact of bankruptcy upon creditors and the sole stockholder would also be adverse. Although holders of the Notes could resort to the Government guaranty, the Federal Government would stand in their place and along with holders of the Bonds would suffer the immediate effects of delayed interest payments and a long wait in securing the return of their principal. Also, as in all bankruptcy proceedings, there is always the risk that even the first lien creditors may ultimately find themselves subordinated to legal and trusteeship fees and borrowings. *Boston & Maine Corp. Bonds Modification, supra,* at p. 176. And to state the obvious, stockholders come last in the order of priorities.

The preamble to section 20b declares it to be in the public interest to avoid consequences such as these. Indeed the congressional purpose in enacting the statute was to provide a means of assisting in preventing their occurrence. As its preamble specifically declares, section 20b was designed to avoid prospective financial difficulties, inability to meet debts as they mature, and insolvency. Accordingly we have pointed out that avoidance of proceedings under the Bankruptcy Act is ordinarily in the public interest, as well as in the interests of a carrier, its stockholders, and creditors. *Erie-Lackawanna R. Co. Bonds Modification,* 324 I.C.C. 152, 171. For the reasons previously stated, the evidence in this record compels the conclusion that the Plan is in the public interest and will benefit the public, EL, its creditors, and its sole stockholder.

Conclusion.—It appears, therefore, that the Plan provides reasonable treatment for the interests of all affected parties while at the same time serving EL's basic urgent need by affording the time and opportunity to work its way out of its present financial difficulties. The record indicates, and we find, that: (1) the impending debt maturity represented by the Bonds presents a problem squarely within the remedial intent of section 20b and, and more particularly, within the scope of paragraph (1) thereof; (2) the proposed alternations and modifications of the Mortgage and Bonds are necessary and in the public interest; (3) the terms and conditions are just and reasonable; (4) the proposals relating to the Mortgage and Bonds (a) will be in the best interests of EL, its sole stockholder, and of the holders of each class of its obligations affected by such modifications or alterations and (b) will not be adverse to the interests of any creditor of EL not affected by such modifications or alterations; and (5) such modifications and alterations are (a) for a lawful object within EL's corporate purposes, and compatible with the public interest, which is necessary or appropriate for or consistent with the proper performance by EL of service to the public as a common carrier, and which will not impair its ability to perform that service, and (b) reasonably necessary and appropriate for such purpose.

Expenses of the proceedings.—The statement of estimated expenses to be incurred in connection with the Plan shows a total of $172,500 consisting of the following items: printing and engraving $5,000, advertising $2,000, depository for assents $1,000, the Cleveland Trust Company trustee (of the Mortgage) $1,000, First National City Bank, trustee (under the Collateral Trust Indenture) $1,000, counsel for the mortgage trustee and for the indenture trustee $5,000, counsel for other parties $75,000, solicitation expense $1,000, fee of Salomon Bros., consultants, $75,000, New York Stock Exchange listing fee $1,500, and miscellaneous (postage and other out-of-pocket disbursements and contingencies) $5,000.

Submission of plan for acceptance or rejection.—As previously mentioned, the proposed modification and alteration of the Notes, although actually recited as part of the Plan, does not fall within the scope of section 20b. Hence, the only class of securities affected by the alterations and modifications which EL seeks to effect pursuant to the provisions of section 20b is the outstanding issue of Erie Railroad Company Ohio Division 3 1/4-Percent First Mortgage Bonds, which mature on September 1, 1971. None of the Bonds is held by any holder whose assent to the proposed Plan is within the control of EL or any person controlling EL. No carriers or other persons have assumed liability as guarantor, endorser, surety, or otherwise with respect to the securities proposed to be affected. Except for holders of the Bonds, the claims and equities of creditors[28] and the sole stockholder are not affected by the proposed alteration and modification of the Bonds. Subject to the terms of our order herein, EL proposes to submit the Plan to the holders of the Bonds for acceptance or rejection in the manner described in its application.

As prescribed in paragraphs (2) and (3) of section 20b our accompanying order will direct submission of the proposed alterations and modifications to the holders of the outstanding Bonds for acceptance or rejection. The procedure to be followed in connection with the submission of the Plan to the holders of the Bonds, the handling of assents and revocations of assents, and certification of the results of submission shall be as follows:

(1) The submission shall be made by mailing to each known holder of the Bonds as soon as practicable after the effective date of our order (a) a copy of such order, (b) a copy of this report, (c) a copy of the revised version of the plan filed July 2, 1971, (d) a form of letter of assent, and (e) a letter of transmittal explaining the foregoing and requesting the holder's assent.

(2) The approved plan of modification, forms of assent, and revocation of assent, all letters, circulars, advertisements, and other communications, including written or printed instructions to solicitors, as well as all financial and statistical statements or summaries thereof, to be used in soliciting acceptance or rejection of the Plan by persons entitled to vote thereon, before being so used, shall be submitted to this Commission for approval as to the form and substance thereof, and at the same time, any such material so submitted to the Commission shall be distributed to all parties of record by the party seeking its approval.

(3) Notice of submission shall be promptly given by publication in a form to be approved by this Commission, once a week for 2 successive weeks in two newspapers published and in general circulation, one in the city of New York, N.Y., and the other in Cleveland, Ohio, and by such further publication of such notice at such other times and places as EL in its discretion may determine.

(4) Solicitation of assents may be carried on by personal interview, mail, telephone, and telegraph by directors, officers, and regular employees of Applicant; and Applicant may retain the services of brokers, security dealers, firms of professional solicitors, or persons specializing in such work and provision may be made for the reasonable compensation of such persons or firms for services rendered in such solicitation.

(5) Any affected bondholder's assent to the plan of modification (as herein approved) shall be given by mailing or delivering a duly executed vote of assent,

[28]The holders of the Notes are affected directly by the proposal to modify the Notes—a proposal which is in aid of, but not a part of, the proposed alteration and modification of the Bonds.

within the time specified in the succeeding paragraph numbered (8), to a qualified bank or trust company (referred to as the depositary), satisfactory to the Commission, as Applicant may select, showing the identifying serial number or numbers and principal amount or amounts of the Bond or Bonds to which the assent relates. Failure of any bondholder to act shall constitute a vote of rejection, without execution of any ballot.

(6) An assent once given shall be binding upon all subsequent holders of the Bond or Bonds to which it relates, and such assent may be revoked only by execution and delivery to the depositary of a letter of revocation, in a form to be approved by this Commission prior to a declaration by Applicant of termination of the right of revocation, given in the manner hereinafter set forth.

(7) To be valid, an assent or a revocation executed by a person other than the owner or holder of record of the affected Bond or Bonds respecting which the assent or revocation is given must be accompanied by documentary evidence of the authority of such person to execute the assent or revocation on behalf of the owner; provided, however, that the foregoing shall not be construed as requiring such documentary evidence of authority for the execution of an assent or revocation by (a) a partner in behalf of the firm of which he is a member, or (b) an officer in behalf of a corporation when such execution is attested under the seal of such corporation.

(8) Assents may be made on and after the date of mailing hereinbefore provided in paragraph numbered (1), and on or before 20 days from the effective date of our order, or within such further time as may be designated by subsequent order in this proceeding; provided that if, at any time prior to the expiration of such period, or extension thereof, assent shall be received and remain unrevoked from the holders of at least 75 percent of the aggregate principal amount of the Bonds then publicly held, EL by written instrument delivered to the depositary may declare the submission period closed and the right to revoke assents terminated, in which event EL shall forthwith give notice thereof by telegraph to this Commission and by at least one advertisement in the same newspapers in which the notice of submission shall have been published.

(9) In performing its task, the depositary shall act as agent solely for the Commission in the discharge of the Commission's responsibility under the statute to assure a valid vote. The depositary will be expected, on its own initiative, to set up an efficient, effective and reliable procedure for processing and recording the votes for acceptance or rejection. However the following specific rules shall be observed:

(a) No assent, or revocation of an assent, nor rescission of a revocation shall be treated as valid unless and until it or reliable evidence thereof is received and recorded by the depositary. Assents, revocations, and rescissions shall be countable when received.

(b) The depositary shall cause the actual date or receipt to be timely endorsed, imprinted, or inscribed (by pen, rubber stamp, or other appropriate means which will ensure permanency of record) upon both the letter (or ballot) and the accompanying envelope (both of which shall be preserved as a unit until the Commission's final consummation order has been issued) in which each assent, revocation, or rescission is transmitted to the depositary. Such recorded date of receipt shall govern in determining any question relating to the counting and certification of the results of submission, and also the validity of any ballot from the standpoint of its receipt in relation to the termination of the submission period.

(c) At all times during the submission period, the depositary shall keep on hand a supply of letters of revocation adequate to enable it to comply promptly with any reasonable number of requests therefor from signers of letters of assent.

(10) As soon as possible after the closing of the submission period, EL shall submit to this Commission, in connection with a supplemental application, a certificate as to the aggregate principal amount of Bonds outstanding, the aggregate principal amount thereof with respect to which valid unrevoked assents have been received and recorded, and the percentage thereof to the aggregate principal amount outstanding. Such certificates shall be supported and accompanied by a certificate of a responsible officer of the depositary as to the aggregate principal amount of the affected Bonds with respect to which valid unrevoked assents were received by the depositary. For the purposes of this provision, any affected Bonds held in the treasury of EL unpledged shall not be deemed to be outstanding.

(11) If assents are received from holders of the requisite percentage of the aggregate principal amount of affected Bonds outstanding, copies of the effectuation documents reflecting the plan of modification shall be furnished to each intervenor and shall be filed with this Commission for review and approval, in connection with a supplemental application seeking our final order approving such plan.

(12) Upon request EL shall supply to any holder of the Bonds, or to a duly authorized representative of such holder, or make available to such holder or representative under conditions reasonably convenient to their use, the most current available list of names and addresses of the holders (so far as known to EL) of this class of bonds, or, in the alternative, if it so elects, EL shall mail, at the request and expense of such holder, copies of any documents or material approved by this Commission, which such holder wishes to be used in connection with the solicitation of assents or dissents to the plan of modification.

THE LOAN GUARANTY ASPECTS

The loan guaranty in F. D. No. 21494, *Erie-Lackawanna Railway Company Loan Guaranty,* which EL now seeks to modify was approved by order dated June 8, 1961. The same order also granted the requisite related authority under section 20a of the act in F. D. No. 21495, *Erie-Lackawanna Railroad Company Securities.* By that order as last modified by supplemental order dated May 26, 1971, the Commission, division 3, authorized and approved, among other things:

(1) In F. D. No. 21494 the guaranty against loss of principal and interest under part V of the Interstate Commerce Act of a proposed loan to Erie-Lackawanna Railroad Company, in the principal amount of $15 million, in the form of 5 1/4-percent collateral notes (i.e., the Notes). The loan was to mature in the principal amount of $750,000 on each June 1, from June 1, 1967, to June 1, 1970, both dates inclusive, and December 1, 1971, and in the principal amount of $2,250,000 on each June 1 from June 1, 1972, to June 1, 1976, both dates inclusive. The loan was to be secured by:

(a) A group of bonds (E-L's securities) consisting of (i) $8,026,000 principal amount of Erie-Lackawanna Railroad Company Pennsylvania Division first mortgage 6-percent bonds, Series B, due May 1, 1980; (ii) $6,476,300 principal amount of Erie-Lackawanna Railroad Company Pennsylvania Division refunding mortgage and collateral trust 6-percent bonds, Series C, due May 1, 1985; (iii) $12,000 principal amount of Erie Railroad Company first consolidated mortgage 3 1/8-percent bonds, Series F, due January 1, 1990; (iv) $4,217,500 principal amount of Erie Railroad Company first consolidated mortgage 4-percent bonds, Series I, due January 1, 1995; (v) $559,000 principal amount of The New York, Lackawanna and Western Railway Company first and refunding mortgage 4-percent bonds, Series A, due May 1, 1973; (vi) $308,000 principal amount of The New York, Lackawanna and Western Railway Company first and refunding mortgage 4 1/2-percent bonds, Series B, due May 1, 1973; (vii) $150,500 principal amount of The Delaware, Lackawanna and Western Railroad Company first and refunding mortgage 5-percent bonds, Series C, due May 1, 1973 (New York, Lackawanna and Western Division); (viii) $327,875 principal amount of The Delaware, Lackawanna and Western Railroad Company Lackawanna of New Jersey Division first mortgage bonds, Series A, bearing 4 percent fixed interest, due May 1, 1993; (ix) $26,600 principal amount of The Delaware, Lackawanna and Western Railroad Company Pennsylvania Division refunding mortgage and collateral trust 5-percent bonds, Series A, due May 1, 1985; (x) $190,000 principal amount of The Delaware, Lackawanna and Western Railroad Company Pennsylvania Division refunding mortgage and collateral trust 4 1/2-percent bonds, Series B, due May 1, 1985; (xi) $191,000 principal amount of The Delaware, Lackawanna and Western Railroad Company Warren Division mortgage bonds, bearing 4 percent fixed interest and 2 percent contingent interest, due May 1, 1992; (xii) $154,000 principal amount of The Delaware, Lackawanna and Western Railroad Company Oswego and Syracuse Division mortgage bonds, bearing 4 percent fixed interest and 2 percent contingent interest, due May 1, 1993; (xiii) $538,000 principal amount of The Delaware, Lackawanna and Western Railroad Company UC&SV Division mortgage bonds, bearing 3 percent fixed interest and 2 percent contingent interest, due May 1, 1992; (xiv) and $1,386,000 principal amount of Erie Railroad Company general mortgage income 4 1/2-percent bonds, Series A, due January 1, 2015, herein collectively, called E-L's securities; and

(b) 9,641 shares of capital stock of Lehigh & Hudson River Railway Company and $794,750 principal amount of Lackawanna & Wyoming Valley Railway Company general mortgage 4-percent income bonds, due January 1, 2010; and

(2) In F. D. No. 21495, under section 20a of the act:

(a) The issue by Erie of not exceeding $15 million of its above-described 5 1/4-percent collateral notes (i.e., the Notes) pursuant to a collateral trust indenture dated as of May 1, 1961 (i.e., the Indenture), between Erie and The First National City Bank of New York, now the First National City Bank (Bank), as trustee for the lenders (the Indenture was subsequently modified by the supplemental indenture dated April 1, 1968, and by the second supplemental indenture dated June 1, 1971);

(b) The issue of a consolidated note not exceeding $15 million; and

(c) As collateral security for the Notes the pledge of the above-described bonds hereinabove collectively called EL's Securities.

Pursuant to the aforesaid order of June 8, 1961, the United States of America, acting by and through the Commission, entered into a guaranty agreement dated May 1, 1961, with the Bank (i.e., the Guaranty Agreement), the load has been fully disbursed, and a balance of $12 million remains outstanding.

In the application now under consideration EL requests:

(1) The consent of the Commission under part V of the act to the modification of the loan in Finance Docket No. 21494 by:

(a) Extending the sinking fund and required payments on said loan of $750,000 now due December 1, 1971, and $2,250,000 due June 1, 1972, and June 1, 1973, respectively, or total payments of $5,250,000 until the maturity of the loan on June 1, 1976,

(b) Increasing the interest on the loan to 6 3/8 percent per annum, effective June 1, 1971, or 7 percent on any overdue payments,

(c) Releasing of the following collateral as security for said loan: (i) $559,000 principal amount of The New York, Lackawanna and Western Railway Company first and refunding mortgage 4-percent bonds, Series A, due May 1, 1973; (ii) $308,000 principal amount of The New York, Lackawanna and Western Railway Company first and refunding mortgage 4 1/2-percent bonds, Series B, due May 1, 1973; and (iii) $150,500 principal amount of The Delaware, Lackawanna and Western Railroad Company first and refunding mortgage 5-percent bonds, Series C, due May 1, 1973 (New York, Lackawanna and Western Division), and

(d) Providing that the loan will be entitled to an additional sinking fund payment in any 1 year (beginning with the year 1973) in which EL's working capital exceeds $10 million at the end of the immediately preceding year, such sinking fund payment to be equal to 20 percent of the difference between its working capital at the end of such immediately preceding year and the sum of its working capital at the beginning of the immediately preceding year and $5 million, provided, however, that the additional sinking fund payment will not exceed $2,250,000, and

(2) In Finance Docket No. 21495, authority under section 20a to:

(a) Attach annexations and imprint notations to its outstanding 5 1/4-percent collateral notes and consolidated note reflecting the above-described part V loan modification, and

(b) Extend the pledge, as collateral security for such modified notes, of the above mentioned EL's Securities, less the bonds proposed to be released.

The requested modifications of the loan guaranty and the documents evidencing that transaction require only brief additional discussion. The facts which establish the need for extending the maturity of the outstanding Bonds in the manner contemplated by the Plan also establish that, with one exception, the requested modifications of the loan guaranty as provided in the Plan would be equitable. In other words, avoidance of bankruptcy proceedings (especially, the consequential adverse impact upon service to the public, upon the railroad's creditors, and upon its operational management) and affording EL the opportunity to work its way out of the existing financial squeeze amply demonstrate that it would be equitable to consent to all but one of the requested modifications of the loan guaranty under section 505. Since the matters to which these consents pertain are in aid of the proposal to alter and modify the Bonds, our findings will reflect that such consents and the related authority under section 20a will become null and void in the event that the Bonds modification proposal fails to become effective on or before September 1, 1971.

The request which should be denied pertains to the release of collateral. The pledged securities whose release is sought all mature on May 1, 1973, whereas the Notes do not mature until June 1, 1976. In support of the request for release, the application argues that denial of this request will necessitate either payment in cash equal to the par value of such securities upon their maturity or negotiations (with the holders of the Notes as well as with the holders of such bonds) to extend the term of the pledged securities. A cash payment, it is further argued, would be inconsistent with and tend to negate the deferral of the sinking fund payments being effected in this proceeding and negotiations for extension of the term of the Bonds would be complicated so long as the pledge is outstanding. In our opinion the request for release of these pleadged securities is based on convenience rather than necessity. At any rate, it is premature and at this time unwarranted, particularly in view of the deferral of the sinking fund payments. Accordingly, good cause therefor not having been shown, the request for release of the specified pledged securities should be denied at this time.

STATUTORY AND ULTIMATE FINDINGS

Accordingly, we find that:

I. In F. D. No. 26522:

A. The proposed alterations and modifications of the Mortgage and the Bonds are just and reasonable and the portion of the Plan relating thereto (i) is within the scope of paragraph (1) of section 20b of the Interstate Commerce Act, as amended, (ii) will be in the public interest, (iii) will be in the best interests of EL, of its sole stockholder, and of the holders of each class of its obligations affected by such modifications or alterations, and (iv) will not be adverse to the interests of any creditor of EL not affected by such modifications or alterations; and

B. The aforesaid alterations and modifications of the Mortgage and the Bonds (i) are for a lawful object within EL's corporate purposes, and compatible with the public interest, which is necessary or appropriate for or consistent with the proper performance by EL of service to the public as a common carrier, and which will not impair its ability to perform that service, and (ii) are reasonably necessary and appropriate for such purpose.

II. In F. D. No. 26523, the request for relief is superfluous and the portion of the application relating thereto should be dismissed.

III. In F. D. No. 21494:

A. Good cause therefor not having been shown, it would not be equitable to give consent to the request for release of certain specified collateral presently pledged as security for the outstanding guaranteed 5 1/4-percent collateral notes of Erie-Lackawanna Railroad Company. Such request should be denied.

B. In all other respects consent to the requested extension and modification of the loan guaranty on the terms stated would be equitable to the United States, Erie Lackawanna Railway Company and the lenders, subject to the following conditions:

(i) The parties will furnish to this Commission two executed or conformed copies of the third supplemental indenture and all other documents and instruments entered into by the parties in connection with the proposed modification of the guaranteed loan in Finance Docket No. 21494, which documents and instruments shall be in form and substance satisfactory to the Commission, and

(ii) The requisite number of lenders will consent to the proposed modification.

IV. In F. D. No. 21495:

(1) The proposed issue of annexations and imprint of notations to Erie-Lackawanna Railroad Company's outstanding 5 1/4-percent collateral notes and consolidated note reflecting the part V loan extension and modification referred to above, and (2) the extension of the pledge as part of the collateral security for said extended notes as set forth above (i) are for lawful objects within EL's corporate purposes and compatible with the public interest, which are necessary and appropriate for and consistent with the proper performance by it of service to the public as a common carrier and which will not impair its ability to perform that service, and (ii) are reasonably necessary and appropriate for such purposes.

V. The consent hereby given in F. D. No. 21494 and the related authority under section 20a hereby granted in F. D. No. 21495 shall become null and void in the event that the proposal in F. D. No. 26522 fails to become effective on or before September 1, 1971.

An appropriate order will be entered, including, in view of the urgency of time, a provision that the order shall become effective on the date of service.

COMMISSIONER BUSH did not participate.

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APPENDIX A

Erie Lackawanna Railway Company—general balance sheets

ASSETS

		December 31, 1969	December 31, 1970
	Current assets:		
(701)	Cash	$3,934,518	$2,602,737
(702)	Temporary cash investments	2,019,719	2,000,000
(703)	Special deposits	1,617,981	1,649,890
(704)	Loans and notes receivable	----------------	----------------
(705)	Traffic and car-service balances—dr.	346,770	----------------
(706)	Net balance receivable from agents and conductors	9,522,888	10,210,782
(707)	Miscellaneous accounts receivable	5,549,768	6,275,833
(708)	Interest and dividends receivable	2,670	53,499
(709)	Accrued accounts receivable	8,391,225	8,341,157
(710)	Working fund advances	88,002	88,319
(711)	Prepayments	381,844	390,008
(712)	Material and supplies	10,948,448	9,439,914
(713)	Other current assets	143,767	183,410
	Total current assets	42,947,600	41,235,549
	Special funds:		
(715)	Sinking funds	1,218	671
(716)	Capital and other reserve funds	2,686,924	1,611,277
(717)	Insurance and other funds	422,661	245,007
	Total special funds	3,110,803	1,856,955
	Investments:		
(721)	Investments in affiliated companies	29,722,471	29,713,996
(722)	Other investments	1,592,524	1,602,828
	Total investments	31,314,995	31,316,824
	Properties:		
(731)	Road and equipment property	548,450,928	540,637,221
(732)	Improvements on leased property—road	2,067,474	2,789,782
	Total transportation property	550,518,402	543,427,003
(735)	Accrued depreciation—road and equipment	(166,414,941)	(166,664,290)
(736)	Amortization of defense projects—road and equipment	(3,082,952)	(2,953,358)
	Recorded depreciation and amortization	(169,497,893)	(169,617,648)
	Total transportation property less recorded depreciation and amortization	381,020,509	373,809,355
(737)	Miscellaneous physical property	3,276,772	4,164,212
	Total properties less recorded depreciation and amortization	384,297,281	377,973,567

ASSETS

		December 31, 1969	December 31, 1970
	Other assets and deferred charges:		
(741)	Other assets	$2,368,653	$1,751,539
(743)	Other deferred charges	4,226,887	5,382,344
	Total other assets and deferred charges	6,595,540	7,133,883
	Total assets	468,266,219	459,516,778

LIABILITIES AND SHAREHOLDERS' EQUITY

		1969	1970
	Current liabilities:		
(751)	Loans and notes payable	940,500	----------------
(752)	Traffic and car-service balances—cr	----------------	370,279
(753)	Audited accounts and wages payable	10,486,774	13,891,393
(754)	Miscellaneous accounts payable	206,186	379,025
(755)	Interest matured unpaid	1,929,443	2,017,779
(756)	Dividends matured unpaid	10,041	10,041
(757)	Unmatured interest accrued	1,768,333	1,608,551
(759)	Accrued accounts payable	23,657,552	31,165,433
(760)	Federal income taxes accrued	----------------	----------------
(761)	Other taxes accrued	4,015,714	4,187,366
(763)	Other current liabilities	2,769,646	3,036,690
	Total current liabilities (exclusive of long-term debt due within 1 year)	45,784,189	56,666,557
	Long-term debt due within 1 year:		
(764)	Equipment obligations and other debt	11,120,524	22,683,147
	Long-term debt due after 1 year:		
(765)	Funded debt unmatured	267,882,650	253,964,350
(766)	Equipment obligations	55,178,607	47,442,831
(769)	Amounts payable to affiliated companies	----------------	2,057,908
	Total long-term debt due after 1 year	323,061,257	303,465,089
	Reserves:		
(771)	Pension and welfare reserves	2,725,548	2,160,651
(774)	Casualty and other reserves	5,129,781	4,437,272
	Total reserves	7,855,329	6,597,923
	Other liabilities and deferred credits:		
(782)	Other liabilities	16,960,511	16,706,670
(784)	Other deferred credits	2,443,036	2,605,482
(785)	Accrued depreciation—leased property	488,717	520,371
	Total other liabilities and deferred credits	19,892,264	19,832,523

Erie Lackawanna Railway Company—general balance sheets—Continued

LIABILITIES AND SHAREHOLDERS' EQUITY—*Continued*

Shareholders' equity:	Total issued (number of shares)	December 31, 1969	December 31, 1970
Capital stock:			
(791) Capital stock issued—			
Erie Lackawanna Railway Company—			
(A) Common—par value $1,000 per share	1,000	$1,000,000	$1,000,000
Capital surplus:			
(794) Premiums and assessment on capital stock		52,668,488	52,668,488
(796) Other capital surplus		1,092,271	1,701,406
Total capital surplus		53,760,759	54,369,894
Retained income:			
(798) Retained income—unappropriated		5,791,897	(5,098,355)
Total shareholders' equity		60,552,656	50,271,539
Total liabilities and shareholders' equity		468,266,219	459,516,778

( ) Denotes red figure.

APPENDIX B

Erie Lackawanna Railway Company—Income statements

	Year 1969	Year 1970
Railway operating revenues:		
Merchandise	$206,575,103	$217,803,633
Coal and coke	11,974,773	13,726,711
Total freight	218,549,876	231,530,344
Passenger	11,490,588	11,186,297
Mail	2,811,502	1,654,762
Express	3,116,949	1,978,438
Miscellaneous	15,292,332	15,800,446
Total railway operating revenues	251,261,247	262,150,287
Railway operating expenses:		
Maintenance of way and structures	28,290,101	29,651,888
Maintenance of equipment	41,016,575	42,822,028
Traffic	5,342,409	5,500,193
Transportation	113,722,683	122,886,106
Miscellaneous operations	532,785	475,697
General	10,756,790	10,833,581
Total railway operating expenses	199,661,343	212,169,493
Net revenue from railway operations	51,599,904	49,980,794

Erie Lackawanna Railway Company—Income statements—Continued

	Year 1969	Year 1970
Railway tax accruals:		
Property and miscellaneous taxes	$6,835,379	$7,669,222
Payroll	12,976,288	13,640,792
Total railway tax accruals	19,811,667	21,310,014
Railway operating income	31,788,237	28,670,780
Equipment rents—net	(22,394,462)	(28,799,457)
Joint-facility rents—net	(345,183)	(203,363)
Net equipment and joint-facility rents	(22,739,645)	(29,002,820)
Net railway operating income	9,048,592	(332,040)
Other income	5,688,043	3,901,969
Total income	14,736,635	3,569,929
Miscellaneous deductions from income	1,356,634	1,066,609
Income available for fixed charges	13,380,001	2,503,320
Fixed charges:		
Rent for leased roads and equipment	245,159	244,227
Interest on funded debt	11,381,258	11,112,581
Interest on unfunded debt	143,494	94,169
Amortization of discount on funded debt	1,860	794
Total fixed charges	11,771,771	11,451,771
Income after fixed charges	1,608,230	(8,948,451)
Other deductions:		
Interest on funded debt (contingent)	349,371	------------------
Ordinary income	1,258,859	(8,948,451)
Extraordinary and prior period items:		
Extraordinary items (net)	------------------	(1,941,801)
Net income transferred to retained income—unappropriated	1,258,859	(10,890,252)

Erie Lackawanna Railway Company—Statement of retained income—unappropriated

	Year 1969	Year 1970
Balance at beginning of year	4,533,038	5,791,897
Credit balance transferred from income	1,258,859	------------------
Total	5,791,897	5,791,897
Debit balance transferred from income	------------------	10,890,252
Appropriations for sinking and other reserve funds	180,000	180,000
Appropriations released	(180,000)	(180,000)
Balance carried to balance sheet	5,791,897	(5,098,355)
Total	5,791,897	5,791,897

( ) Denotes red figure.