# RAILROAD REORGANIZATION

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# CHAPTER VII

## UNION PACIFIC

Acts of 1862 and 1864 — High cost of construction — Forced combination with the Kansas Pacific and the Denver Pacific — Unprofitable branches — Adams's administration — Financial difficulties — Debt to the Government — Receivership and reorganization — Later history.

THE construction of the Union Pacific was made possible by direct grants of lands and government bonds by Congress. The motive for the project was military and political as well as economic; on the one hand California was to be cemented to the Union, and aggression on the part of England was to be forestalled; on the other a great and fertile territory was to be opened and an additional market provided for the products of the East.

In 1862 the first act "to aid in the construction of a Railroad and Telegraph Line from the Missouri River to the Pacific Ocean, and to secure to the Government the Use of the same for Postal, Military, and Other Purposes" was passed.[1] It created a corporation to be known as the Union Pacific Railroad Company, with a capital of 100,000 shares of $1000 each, and authorized it to construct a railroad from the one hundredth meridian of longitude west from Greenwich at a point within the territory of Nebraska westward to the western boundary of the territory of Nevada. It granted the right of way, and in addition five additional sections per mile on each side of the track, plus a varying amount of United States bonds per mile, the use and delivery of which was to constitute a first mortgage on the property of the company. All compensation for services rendered to the Government was to be applied to the payment of these bonds and interest thereon; and after the road was completed, until the bonds and interest should have been paid, at least 5 per cent of the net earnings of the road was to be annually applied to the payment thereof. The directors were to be not less than fifteen in number, of whom two were to be appointed by the President of the United States. It was hoped that the offer would be sufficient to attract private capital to the un-

[1] Statutes at Large, 37th Congress, 2d Session, chap. 120.

dertaking, and when it failed in this, the inducements were increased. The Act of 1864 amended that of 1862. It reduced the par value of the shares of stock from $1000 to $100, and increased their number from 100,000 to 1,000,000. It increased the land grant from five to ten alternate sections per mile, and subordinated the government lien to the rank of a second mortgage. Only one-half the compensation for services rendered for the Government was required to be applied to the payment of the bonds issued by the Government. The directors were to be twenty in number, of whom five were to be appointed by the Federal President.[1]

It was under these main provisions that the Union Pacific Railroad was constructed. In their final shape they were intended to provide for the greater part of the cost of construction, while allowing the company to supply deficiencies by the issue of its own first mortgage bonds. Capitalization under these conditions would not have been excessive; the Government's investment would have redounded unmistakably to its own benefit, as well as to that of the country, and the corporation would have looked forward to a long and prosperous career. Three things interfered to swell the cost of the construction of the road, and with that its capitalization: First, construction was carried on during a time of high prices, swollen not only by depreciation of the currency, but by artificial conditions occasioned by the war; second, the normal level of the prices paid was raised by the speed with which the road was completed; third, construction was entrusted to a construction company, the famous Crédit Mobilier.

In its comparison of the prices of the years 1864–9, with those of 1860, the Aldrich Committee arrived, in 1893, at the following result:

| *Year* | *Food* | *Bar Iron Rolled* | *Rails, Iron* | *Metals & Implements exc. Pocket Knives* | *All Articles* |
|---|---|---|---|---|---|
| 1864 | 165.8 | 249.3 | 262.5 | 198.0 | 190.5 |
| 1865 | 216.5 | 181.1 | 205.5 | 218.7 | 216.8 |
| 1866 | 173.8 | 167.0 | 180.7 | 192.7 | 191.0 |
| 1867 | 163.9 | 148.2 | 173.2 | 178.9 | 172.2 |
| 1868 | 164.2 | 145.8 | 164.3 | 167.1 | 160.5 |
| 1869 | 162.9 | 139.0 | 160.9 | 157.9 | 153.5 |

[1] Statutes at Large, 38th Congress, 1st Session, chap. 216.

These figures may be divided by the premium on gold, in order roughly to ascertain gold prices. The index numbers then become:

| *Year* | *Food* | *Bar Iron Rolled* | *Rails, Iron* | *Metals & Implements exc. Pocket Knives* | *All Articles* |
|---|---|---|---|---|---|
| 1864 | 106.6 | 160.3 | 168.8 | 127.3 | 122.5 |
| 1865 | 100.1 | 83.7 | 95.0 | 101.1 | 100.3 |
| 1866 | 124.1 | 119.2 | 128.9 | 137.5 | 136.3 |
| 1867 | 121.8 | 110.1 | 128.6 | 132.9 | 127.9 |
| 1868 | 118.6 | 105.2 | 118.6 | 120.6 | 115.9 |
| 1869 | 120.1 | 102.5 | 118.6 | 116.4 | 113.2 [1] |

The tables show that both currency and gold prices were much higher in 1866 than before the war, and that both remained high while the Union Pacific was being built. Wages were also above the normal, and for similar reasons. During the war the demand for men and goods of all kinds was great. After 1865 the country turned with tremendous energy to industry; and the upward swing, which was unchecked until the panic of 1873, and which was especially directed toward railroad building, maintained both wages and prices at an unusual height. Besides this, American rails were at the time in a period of transition from iron to steel; and much of the work carried through at such expense had completely to be done over within the next ten years.

The high prices were made higher by the speed of construction. The Union Pacific built west from the Missouri River, but at the same time the Central Pacific was building east from Sacramento, under similar conditions as to government aid. The two roads were expected to meet at the western boundary of Nevada; but to encourage their early completion, the Act of 1862 authorized the road which first reached the designated point to continue construction, east or west as the case might be, until junction with the second road should be made. Since the amount of land granted depended on the mileage completed, the haste of the companies was feverish. "The Union Pacific Company," says Davis,[2] "had its parties of graders working 200 miles in advance of its com-

[1] Aldrich Committee Report. The value of gold used is that given in the American Almanac for 1878, and varied from year to year as follows:

| | | | | | |
|---|---|---|---|---|---|
| 1864 | 155.5 | 1866 | 140.1 | 1868 | 138.5 |
| 1865 | 216.2 | 1867 | 134.6 | 1869 | 135.6 |

[2] John P. Davis, History of the Union Pacific Railroad, p. 151.

pleted line in places as far west as Humboldt Wells." The Central Pacific had completed 105 miles east of Sacramento by the autumn of 1867, hauling iron and supplies over the mountains without waiting for the piercing of its tunnels. No less than 1038 miles of the Union Pacific, including the difficult stretch over the Rocky Mountains, were completed by 1869, four years after construction was commenced. The prize of additional land was thereby secured, but this land was long unsalable, and the cost of construction was largely increased.

Finally, large sums were misapplied through a construction company. The story of the Crédit Mobilier has been so often told that only brief mention need be made of it here.[1] In 1864 T. C. Durant, vice-president of the Union Pacific, induced one H. M. Hoxie to bid for a contract to build from Omaha to the one hundredth meridian. Hoxie was financially irresponsible, and four days later assigned the contract to a company composed of Durant and other stockholders of the Union Pacific. Meanwhile Durant had purchased the charter of the Pennsylvania Fiscal Agency, a corporation which possessed convenient powers. Later in 1864 the members of Durant's construction company were given stock in the Fiscal Agency, now called the Crédit Mobilier of America, for the amounts they had paid in, and stockholders of the Union Pacific were allowed to receive Crédit Mobilier stock for the amounts they had paid in on their Union Pacific shares. Stockholders of the Union Pacific thus became also stockholders of the Crédit Mobilier, and in their former capacity were enabled to vote lucrative contracts to themselves as constructors of the railroad. Durant's company assigned its contract to the Crédit Mobilier. Subsequently it was found more convenient to assign contracts to certain individuals, who transferred them to seven trustees, who built the required road with funds furnished by the Crédit Mobilier, and turned over the profits to that organization, but the practical result was the same.[2] These various devices removed all incentive to economy on the

[1] Useful accounts of the Crédit Mobilier may be found in Davis, Union Pacific Railroad; Crawford, Crédit Mobilier of America; Hazard, The Crédit Mobilier of America; White, History of the Union Pacific Railroad; Poland Committee, Report and Testimony, 42d Congress, 3d Session, House Reports, No. 77.

[2] Davis, pp. 163–70.

part of the Union Pacific stockholders. Instead of gaining by cheap construction, they profited by dear; instead of aiming to reduce the cost in every possible way, they schemed at making the construction contracts as lucrative as possible to the persons to whom they were assigned. The advantages to them as stockholders of the Crédit Mobilier outweighed the disadvantages to them as stockholders of the Union Pacific. The profits realized by the Crédit Mobilier are still a subject of dispute. H. K. White figures them as 27½ per cent, or $16,700,000; Davis says that the profit was safely over $20,000,000; but whereas White calculates the percentage of profits to the total cost of construction, Davis insists that a large part of the capital invested was replaced on the completion of each section of twenty miles by the proceeds of the government bonds and railway bonds and stock, and that though from $50,000,000 to $70,000,000 were expended, in all probability not more than $10,000,000 were sunk at any one time; in which case a profit of $20,000,000, spread over four years, represents $5,000,000 per year, or 50 per cent annually on the capital employed. Finally, the Union Pacific Railway Commission estimated the actual cash profits at $23,366,320, and remarked that the obligations incurred by the railroad company represented a very much larger sum, being measured by the bonds and stock at their par values.[1]

The result of the three factors was a corporation bonded at an extremely high rate. The cost of road in 1870 was reported to be $106,245,978, or $102,951 per mile, against which was a capitalization of $107,907,300, or $104,561 per mile, of which $32,715 per mile was stock, $26,080 government bonds, and $45,765 first mortgage, land grant, and income bonds. In 1873 the net earnings were $4,092,032, and the interest on the funded debt, not including the government interest, was $3,403,660. In 1874 the figures were $5,291,243 and $3,431,720; in other words, the corporation started with a heavy handicap, which its monopoly of transcontinental business at first helped to overcome, but which grew heavier and

[1] Union Pacific Railway Commission Report, 1887, p. 52. The Government endeavored to force the cancellation of the above mentioned construction contracts and the restoration of unlawful profits, but was held by the Supreme Court to have no standing in the case which would entitle it to demand relief. U. S. *vs.* Union Pacific Railroad Company, 98 U. S. 569.

heavier as the years went on. During the seventies, to repeat, the Union Pacific enjoyed generally large prosperity. The volume of stock outstanding remained the same, the bonded indebtedness but slightly increased, and the ratio of operating expenses to receipts declined. The first dividend was paid in 1875; in 1876 and 1877 8 per cent was declared, in 1878 5½ per cent, and in 1879 6 per cent. In 1880, however, a consolidation took place with the Kansas Pacific and Denver Pacific railroads, and this operation may well receive somewhat detailed consideration.

The Kansas Pacific, as well as the Union Pacific, was a creation of the Acts of 1862 and 1864, which required it to be constructed from Kansas City westwardly to form a junction with the Union Pacific at a point on the one hundredth meridian. Later, an Act of July 3, 1866, authorized it to change its route, and to connect with the Union Pacific at a point not more than fifty miles westwardly from the meridian of Denver in Colorado.[1] Like the Union Pacific the Kansas Pacific was built by means of construction contracts, which resulted in a total capitalization on its 638 miles of line of $9,437,950 in stock and $22,651,000 in bonds, or $14,793 and $33,455 respectively per mile, —high figures in view of the comparatively level character of the country traversed.[2] The road was not a paying one. It was poorly built and poorly managed, and running parallel with the Union Pacific, it had to meet competition of a very bitter kind. The report of Mr. Calhoun, expert accountant for the United States Pacific Railway Commission of 1887, showed that the total receipts of the road from 1867 to 1879 had aggregated $9,220,218, while the bond and interest account, exclusive of United States interest, had amounted to $15,745,287; leaving a deficit of $6,525,069, or, including the United States accrued interest, of $11,330,772.[3] That is, the Kansas Pacific was in a state of chronic insolvency. In 1874 it was placed in the hands of receivers, and the following year, by an arrangement with its creditors, it funded a considerable amount of overdue interest.[4]

[1] Statutes at Large, 39th Congress, 1st Session, chap. 159.

[2] United States Pacific Railway Commission Report, 1887, p. 55.

[3] Ibid. vol. 8, p. 4975.

[4] Records in Union Pacific Railway Foreclosure Cases, 55th Congress, 1st Session, Senate Document 10, Part 3.

In 1878 a number of securityholders of the Kansas Pacific got together in an attempt to reorganize that property, to take it out of receivers' hands, and to "unite in interest the Kansas Pacific and Union Pacific Railway Companies." Twelve large securityholders consented to contribute to a common pool or fund holdings of securities taken at a fixed valuation, their interests in the pool to be proportional to the amounts of said securities and stock taken at the value referred to.[1] For the securities deposited they were to receive stock at a reduced rate: thus for eight shares of old stock they were to receive one share of new; for $2000 unsubordinated income bonds they were to get ten shares, and for $10,000 subordinated income bonds thirty shares of new stock.[2] The final result would have been to replace securities with a par value of $17,330,350 by stock with a par of $4,855,300, and greatly to lighten the burdens upon the road; though it must be remembered that the $17,330,350 were less than half of the total volume of securities outstanding, that the payment of interest on much of these had been optional only, and that no provision was made for the floating debt.

The scheme fell through, according to Mr. Gould, who was a party to the agreement, because securityholders outside of the pool refused to consent to so drastic a reduction of their holdings; and at his suggestion a consolidated mortgage was substituted for the issues of stock. This mortgage was for forty years at 6 per cent. The total issue was to be for $30,000,000, of which $24,000,000 were to be issued at once for the retirement of earlier bond issues and for payment of arrears of interest.[3] Like the previous proposition the scheme contemplated a scaling in the principal of the junior securities, and the same rates of commutation were retained; but in this case the old Kansas Pacific stock was withdrawn from the operation of the plan, and certain reservations were made for other purposes, so that an actual increase in indebtedness was finally to

[1] Parties to agreement were: Sidney Dillon, Fred L. Ames, Jay Gould, C. S. Greeley, John D. Perry, Robert E. Carr, Adolphus Meier, B. W. Lewis, Jr., Henry Villard, John P. Usher, D. M. Edgerton, Artemas H. Holmes.

[2] United States Pacific Railway Commission Report, 1887, testimony of A. H. Holmes, p. 165.

[3] Ibid. Testimony of Jay Gould, pp. 454–6. The change to a mortgage was made between April, 1878, and May, 1879.

result, and even the interest charges were certain to increase.[1] For the time being, however, by force of the reduction of interest on the funding mortgage in January, 1879, from 10 to 7 per cent, and by the disallowance of some claims for overdue interest, relief was obtained, while the consolidated mortgage was duly issued.

The Kansas Pacific ran west to Denver. Between Denver and Cheyenne the Denver Pacific, 106 miles long, served as a connecting link between the larger systems. The Denver Pacific stock was held by the Kansas Pacific, and 29,979 shares of it were pledged in 1877 as part security for an issue of 10 per cent funding mortgage bonds.[2] The total earnings of the Denver Pacific from 1870 to 1879 had been $3,122,141; the expenses had been $1,709,477, and the net earnings from operation $1,412,664, or an average per annum of $141,266; while for the first eight years of that time the annual interest charge had been about $185,000. The only value of the Denver Pacific stock lay in the control which it secured over a connecting link between Denver and Cheyenne.[3]

Under the conditions of competition existing between the Union Pacific, Kansas Pacific, and Denver Pacific, some sort of agreement or consolidation was both desirable and likely. The Kansas Pacific was entirely dependent on its competitor for access to western business, and this was soon perceived to be equivalent to continuous bankruptcy. Extension to Ogden would have removed the dependence; but this, while to be dreaded by the Union Pacific, was beyond the power of the Kansas Pacific for financial reasons, and no capitalist or group of capitalists before 1878 or 1879 seemed interested in the undertaking. On the other hand, rates were low, and the very success of its exclusive policy forced the Union Pacific to meet the competition of a road which, with no interest charges to pay, was able to cut all rates to the very verge of the cost of operation.

As early as 1875 there was talk of an agreement whereby the Kansas Pacific was to give up its claims for a pro rate on its Pacific business in return for a monopoly of the local business of Colorado,

[1] Records in Union Pacific Railway Foreclosure Cases, 55th Congress, 1st Session, Senate Document 10, part 3 (contains text of mortgage).

[2] United States Pacific Railway Commission Report, 1887, testimony of A. H. Holmes, pp. 130 and 133.

[3] Ibid. vol. 8, p. 4987, Report of William Calhoun, Accountant.

and in connection with the deal was to acquire the Colorado Central Railroad on issue of $10,000,000 Kansas Pacific stock to parties designated by the Union Pacific Company; but this was never carried out. In 1878, when Gould began to be interested in the property, a union by means of stock control seemed feasible. Gould's first purchases were of bonds, and it was as a bondholder that he entered the pool of 1878; but with the purchase of the holdings of the "St. Louis parties," he and his friends obtained control of a majority of Kansas Pacific stock. In fact one of the provisions of the pool was that if on the first day of June, 1878, it should be found that Messrs. Gould, Dillon, and Ames, all large stockholders in the Union Pacific, had not a majority interest in said pool, then they should have an option on such an amount of other interest ratably and for cash as on the basis of the schedule should give them such an interest; and though this majority did not necessarily involve a majority of stock, the operations of the pool aided Gould in the acquisition of control. The union between the Union Pacific and the Kansas Pacific thus secured was, however, of the frailest kind; for Mr. Gould at no time had the permanent interest of either road at heart, and looked for his personal profit rather in their struggles than in agreement between them. For this reason, as he bought Kansas Pacific, Gould sold Union Pacific stock, reducing his holdings from about 200,000 to about 27,000 shares.[1] In 1879 the situation of the two roads was thus much the same as before, and the harmony apparent was of the most superficial kind. One change, however, had taken place to the serious disadvantage of the Union Pacific; for the Kansas Pacific, although still badly built and dependent upon its rival for an adjustment of rates sufficiently favorable to let it into the western business, had now interested in it a group of capitalists quite capable of financing an extension to Ogden, and even of securing connections from Kansas City to the East.

In 1879, doubtless relying upon the strength of Kansas Pacific's new backing, Gould proposed to the Union Pacific a consolidation of the Union, Kansas, and Denver Pacific roads, in which the shares of each were to figure equally at par. The terms were absurd

[1] United States Pacific Railway Commission Report, 1887, testimony of Jay Gould, p. 463.

by every test of productive capacity which could have been applied. The relative earning power and annual interest per mile of the three roads at this time were given by a government accountant as follows:

| | *Annual Net Earnings per mile* | *Annual Interest per mile* |
|---|---|---|
| Union Pacific | $5617 | $3185 |
| Kansas Pacific | 1602 | 2295 |
| Denver Pacific | 1333 | 1750 [1] |

The Union Pacific had reported an annual surplus, the other two roads an annual deficit; the Union Pacific had not defaulted, the Kansas and Denver Pacific had done little else; the highest mark which the Kansas Pacific stock had touched in January, 1879, had been 13, that of the Union Pacific had been 68½. But the question, as Gould well knew, was not one of productive but one of destructive capacity, and the means of coercion which he employed was a demonstration of the ease with which the Kansas Pacific could be made formidable as a competing line. In November, 1879, he purchased the Missouri Pacific from Kansas City to St. Louis; about the same time he bought two minor roads between the Kansas Pacific and the Union Pacific in Kansas, and announced his intention of extending the Kansas Pacific to Salt Lake City, there to connect with the Central Pacific and to form a third transcontinental route. The story is clearly told in the report of the United States Pacific Railway Commission.[2] The result was the consent of the Union Pacific directors to the terms imposed, and the execution of an agreement dated January 14, 1880, whereby the Union and the Kansas Pacific, with all their respective assets and liabilities, were put together at par of their respective capitals, — $36,762,300 and $10,000,000, — to which was added the capital of the Denver Pacific, $4,000,000, forming a new company called the Union Pacific Railway Company, with a capital of $50,762,300, and a bonded indebtedness of $92,984,624.[3] This corporation was larger in every way than the old Union Pacific Railroad, except in one particular — earnings above fixed charges. It had 1821 miles of line instead of

[1] United States Pacific Railway Commission Report, 1887, p. 58.

[2] Ibid. pp. 59 to 65.

[3] Ibid. Testimony of F. L. Ames, p. 668. The combined capital is given in the agreements as $51,762,300, but this is apparently a mistake.

1042; $22,455,134 gross earnings instead of $13,201,077; $10,545,119 operating expenses instead of $5,475,503; and yet, since the consolidation was a union of some strength with a vast deal of weakness, there were few who profited by it save the holders of Kansas Pacific or Denver Pacific stocks. Those lucky and skilful individuals saw the quotations of Kansas Pacific common rise from a high level of 13 in January, 1879, to one of 59 in June, and of 92½ in December; and the stock which had been a football in the market thus become of such value that in 1887 Gould was able to lay before a committee of Congress, in justification of the terms described, a table which showed for 1880 market prices of Kansas and Union Pacific stock which were approximately the same.[1]

It was to Gould, as chief owner of Kansas Pacific and holder of practically all of the Denver Pacific stock outstanding, that the lion's share of the profits went; but Mr. Gould was not satisfied with a harvest on these stocks alone. In the course of his operations he had become possessed of certain branch and minor roads in whole or in part. Thus he held $945,887 in bonds of a company known as the St. Joseph & Western Railroad Company, and 5013 shares of its stock; $634,000 in bonds of the St. Joseph Bridge Company; and $59,000 in St. Joseph & Denver Pacific Railroad receivers' certificates; while to convince the Union Pacific directors of the wisdom of accepting his plan of consolidation he had acquired the Missouri Pacific, the Kansas Central, and the Central Branch Union Pacific railroads.[2] The earning capacity of none of these lines was large, that of the Missouri Pacific being the greatest. The St. Joseph & Western had been sold in foreclosure in 1875, and had continued to be managed thereafter by a receiver. What value it had was due

[1] Quotations of Kansas Pacific common during 1879 (Chron. 1880):

| January | | February | | March | | April | |
|---|---|---|---|---|---|---|---|
| Low | High | Low | High | Low | High | Low | High |
| 9⅛ | 13 | 11½ | 22¼ | 17 | 22½ | 20½ | 60 |
| **May** | | **June** | | **July** | | **August** | |
| Low | High | Low | High | Low | High | Low | High |
| 50 | 59¾ | 54 | 59 | 56 | 60 | 53⅝ | 59½ |
| **September** | | **October** | | **November** | | **December** | |
| Low | High | Low | High | Low | High | Low | High |
| 55 | 73½ | 70 | 85¼ | 83½ | 92 | 85 | 92½ |

[2] United States Pacific Railway Commission Report, testimony of Jay Gould.

to the fact that, as extended to Grand Island, it gave to the Union Pacific an outlet to the East other than the one at Omaha. The value of the Bridge Company bonds and of the receivers' certificates was dependent upon this same property. The Kansas Central was a narrow-gauge road and had been sold under foreclosure in April, 1879. The Central Branch Union Pacific had been designed to join with the Kansas Pacific, but had been left without western connection when this latter road had failed to meet the Union Pacific at the hundredth meridian. At the time of the consolidation, according to the United States Pacific Railway Commission, "the coupons for six years were in default, and were retained uncancelled as security for the income mortgage. The company had never earned sufficient to pay its own coupons, without taking into account the accruing interest to the United States in any form." [1] The Missouri Pacific was more prosperous, but need not here concern us. Mr. Gould had paid various prices for the above, ranging from $40 for the St. Joseph & Denver bonds to $238 for the stock of the Central Branch Union Pacific. In the case of each road he turned over his purchase to the Union Pacific for the same or a greater price.[2] Thus for the St. Joseph & Western bonds, for which he had paid 40, he received par in Union Pacific stock selling as high as 94 in January, 1880; for $634,000 bonds and 4000 shares of stock of the St. Joseph Bridge Company, costing $480,440, he received 6340 shares of Union Pacific stock; for $479,000 in bonds and 2521 shares of stock of the Kansas Central, he received 4790 shares of Union Pacific; and for 7616 shares of Central Branch Union Pacific, costing $1,826,500, he received $913,500 in Union Pacific six per cent bonds and $913,500 in Kansas Pacific six per cent bonds.[3] The result was the issue of considerable amounts of stock of the consolidated and bonds of the consolidating companies, without equivalent value received.

The Union Pacific Railway Company, therefore, began its career in 1880 in worse shape than the Union Pacific Railroad Company, which had preceded it, for it suffered not only from an initial watering of stocks and bonds, but from a watering of assets which had

[1] United States Pacific Railway Commission Report, 1887, p. 100.

[2] Except the Missouri Pacific, which Gould retained.

[3] United States Pacific Railway Commission Report, 1887, testimony of Jay Gould, pp. 467–9, 523, 524.

followed. Including the government subsidy and accrued interest thereon, the total bonds and stocks of the company in 1880 were $179,058,902, or $98,329 per mile, of which $27,876 were stock, $45,372 mortgage bonds, and $25,081 government subsidy and interest. The figures per mile were slightly lower than in 1870, and yet the water in the capitalization was more abundant, for the average value of the assets had declined still more. A dividend-paying road had been combined with non-dividend payers, with the result of large profits to the promoters of the consolidations, but of serious harm to the solvent party.

Between 1880 and 1883 a number of branches were constructed, to provide funds for which the capital stock of the Railway Company was increased $10,000,000. Of these the Denver & South Park was constructed in the years 1881 to 1883, and was the last of Mr. Gould's gifts to the parent line. This road was handled by several construction companies, in the last of which Gould took a quarter interest, receiving stock of the Denver & South Park Railroad Company as a dividend on his investment.[1] In November, 1880, acting in behalf of the Union Pacific Railway Company, he bought the stock of the Denver road at par for cash, benefiting in his capacity as quarter owner by his action as representative and stockholder of the Union Pacific.[2] In relation to the road Mr. Charles F. Adams, Jr., subsequently said: "The chief source of revenue . . . was in carrying men and material into Colorado to dig holes in the ground called mines, and until it was discovered that there was nothing in those mines the business was immense." [3] A more important and genuinely beneficial project was the organization in 1881 of the Oregon Short Line Railway Company to construct and operate a railway from Granger on the Union Pacific to and into the state of Oregon, a distance of 610 miles, with the intention of securing the Washington and Oregon business. The Northern Pacific was in financial difficulties at the time, and it was not expected that it could anticipate the new road; but even though this expectation was disappointed, and the Oregon Short Line was second in reaching the

[1] United States Pacific Railway Commission Report, 1887, testimony of Charles Wheeler, pp. 1735–6. Amount, $571,000.

[2] Ibid. Testimony of John Evans, pp. 1853–4.

[3] Ibid. Testimony of C. F. Adams, p. 47.

disputed territory, its value was great and steadily grew.[1] The road was built by the construction department of the Union Pacific, and was financed by the organization of a subsidiary corporation which issued stock and bonds to an amount of $25,000 per mile, one-half of the stock being reserved in the Union Pacific treasury for the purpose of control, and the Union Pacific guaranteeing the payment of interest on the bonds. This branch at least was not unloaded on the main line by interested parties, and forms an essential part of the system to-day. Other branches were bought or constructed at the time, but do not require detailed mention.

Gould for the time had obtained from the Union Pacific all that he thought possible, and quietly unloaded his stock, while keeping up the payment of dividends. By 1883 he was substantially clear, but he had left his mark; the consolidation of 1880, with the forced purchase of worthless branches, aided as it was by the high capitalization caused by extravagant original construction, and accompanied by a steadily increasing intensity of competition between transcontinental lines, had diminished the surplus to a dangerous extent. At the same time the prosperity of the country as a whole was declining; the wheat crop of 1881 was only three-quarters as large as the crop of 1880, and the corn crop was the smallest since 1874; though the decline was not so marked in Kansas and the far West as in the states east and south of Omaha and Kansas. By 1882, says Noyes, all the markets were moving downward, and after the reaction of that year, the volume of internal trade decreased continuously until after the panic of 1884.[2]

The evidence of distress on the part of the Union Pacific was the mounting up of the floating debt. In November, 1882, President Dillon stated that it then amounted to $3,400,000, and that a loan of $5,000,000 was to be negotiated to take care of it.[3] The annual report at the end of the year stated the net debt to be only $842,743, but included in the assets used to offset the gross debt $2,768,437 in fuel and material on hand, and $927,648 in balances due from auxiliary roads; so that early the following year it was again a subject of discussion, and the stockholders recommended to the directors the issue of collateral bonds in order to wipe it out. Pur-

[1] United States Pacific Railway Commission Report, 1887, pp. 91 ff.

[2] Thirty Years of American Finance, pp. 86 to 98. [3] Chron. 35: 578, 1882.

suant to the recommendation the directors executed to the New England Trust Company of Boston an indenture under which it proposed to issue trust bonds to an amount equal to 90 per cent of the securities deposited. By 1884 the gross floating debt amounted, nevertheless, to $11,306,595, as against $9,852,325 gross in 1882, and the quick assets, exclusive of fuel and material, counted up to $8,068,898, instead of to $6,241,145. The chief increase in liabilities, as always, had taken place in bills payable, meaning that the road had been giving its notes for the payment of current indebtedness, with the consequent necessity of paying a high rate of interest, and of making frequent renewals. Meanwhile dividends had been stopped and salaries cut down.

At this juncture Mr. Sidney Dillon resigned the presidency, and Mr. Charles Francis Adams, Jr., was elected his successor. Mr. Dillon was well along in years, was said to be in poor health, and doubtless missed the support which Mr. Gould had been accustomed to render him. Mr. Adams was a younger man, only forty-nine years of age as against the sixty-nine of Mr. Dillon. He had been a member of the Massachusetts Railway Commission from 1869 to 1879, had served as government director of the Union Pacific in 1878, and now brought to his position as president an inexhaustible fund of energy, large resourcefulness, and more important still, a nice sense of his obligations towards the bondholders and shareholders of his road. Under his régime the economies earlier initiated were continued and extended; employees were discharged until, by June 28, 1884, the company had only about 10,000 men in its employ instead of the 20,000 who had been on the rolls at one time; and rolling mills, etc., were closed wherever the company found it cheaper to purchase rails and equipment at current prices. This, with the cessation of dividends, left a considerable surplus revenue applicable to the payment of the floating debt. In addition, bonds and stock from the company's treasury were sold between January 1, 1884, and January 1, 1887, for which $6,550,000 were obtained; and the aggregate of resources made available was $16,200,000, of which $8,251,368 were applied to the floating debt, $6,708,632 to betterment of the road and branch-line construction, and $1,240,000 to increase of equipment.[1] In addition the proceeds

[1] United States Pacific Railway Commission Report, 1887, p. 67.

from land sales were used to the same general end. In August, to reassure investors, President Adams stated that no part of the floating debt was pressing, and in November he repeated the statement; the truth of which was made evident by the payment of the last bit of net unfunded indebtedness on August 22, two years later. The result was highly creditable, although the continued cessation of dividends provoked some protest.

Much could be done at this time by able and energetic management; there was, however, much that could not be done; and it is to this that we must attribute Mr. Adams's failure to put the road in a permanently stable position. For first, the competition which the Union Pacific was obliged to meet was constantly increasing in severity. In 1881 the Atchison, Topeka & Santa Fe was extended to a junction with the Southern Pacific at Deming; in 1883, in the language of the annual report, "Not only was the Rio Grande completed to Ogden, making, in connection with the Atchison, Topeka & Santa Fe and the Burlington & Missouri extension of the Chicago, Burlington & Quincy, a direct competing route with the Union Pacific from Chicago and all eastern points to a common western terminus, but the Northern Pacific also was connected through, making a third transcontinental route."[1] In 1887 the Atchison built 450 miles of line and the Chicago, Rock Island & Pacific was scarcely behind, so that Kansas and Nebraska were covered with a network of lines, which transformed the natural local traffic of the Union Pacific into competitive business of the most uncertain kind. At the same time the profitable high grade business was giving way to a larger volume of mineral traffic, and the average length of haul was increasing, all of which resulted in a decrease of about 45 per cent in the average receipts per ton mile between 1881 and 1890, a slow increase in gross earnings which bore little relation to the greatly increased volume of business done, and a fluctuating progress of net earnings, which were actually over $3,000,000 less in 1889 than they had been eight years before.

And second, during this time the fixed charges of the Union Pacific did not materially decrease. They were $7,626,626 when Mr. Adams assumed the presidency, and $7,309,142 five years

[1] Annual Report, 1884, p. 5.

later; and the necessity for further decrease was shown by the fact that the total net income of the road was $11,402,199 in 1884, $10,339,402 in 1889, and $9,561,673 in 1890. What Mr. Adams could do he did, and the funded debt under his régime decreased from $90,760,582 in 1884 to $82,090,585 in 1889, and to $73,968,885 in 1890; the company steadily buying up its own indebtedness: but the conditions which he had to face were too exacting, and the saving made here was offset in other ways.

To save itself the Union Pacific was driven to a rapid extension of its branch mileage, which Mr. Adams held to be the only means by which fixed charges could be paid.[1] Between 1884 and 1890 3132.45 miles were built or acquired, all under separate organizations, but with their accounts and management under the supervision and control of the officers of the parent line; and the amount invested in branch-line securities was raised from about $28,000,000 in 1881 to $41,879,724 in 1892. These roads reported annual deficits, which were either paid out of earnings or carried as floating debt. The report of the Government Directors in 1891 declared that $15,000,000 out of $21,400,000 of floating debt were the result of expenditures and advances in the construction of branch and tributary lines and the purchase of stock in such lines for the purpose of control.[2] But speaking in 1887, Mr. Adams declared the branches to be worth $5,000,000 a year to the main line, entirely apart from anything which appeared in the accounts of the branches themselves, and in a letter to the Government Directors in 1884 he said: "The branches and auxiliary lines of the Union Pacific should be considered the only real security the Government has for the repayment of its indebtedness. . . . Were it not for these branches the Union Pacific would be confined to such small local traffic as it could pick up at points directly upon its main line; and to its share of the through transcontinental business which has recently been subdivided by four through the construction of competing routes."[3] The most important of the branches remained the Oregon Short Line, with the connecting line of the Oregon Railway & Navigation

[1] United States Pacific Railway Commission Report, 1887, testimony of C. F. Adams, pp. 45–6.

[2] Chron. 53: 436, 1891.

[3] Annual Report, 1884, p. 165.

Company, of which the Union Pacific became finally possessed in 1889. This last road had been long considered the natural outlet of the Northern Pacific to the Pacific coast, but had been leased by the Union Pacific in 1887 through the Oregon Short Line with a guarantee of 6 per cent dividends upon its stock as well as interest upon its bonds for 999 years. In 1889 negotiations with the Northern Pacific resulted finally in the sale of the Oregon Railway & Navigation stock held by Mr. Villard and his friends. Pending the issue of a collateral trust mortgage the stock was deposited with a trust company, a note was given for the amount, and the sum was carried as floating debt. Whatever the value of the property to the Northern Pacific, it proved of great worth to the Union Pacific, providing it with an independent outlet to the coast, and giving it a haul on its main line of over 800 miles on all interchanged traffic. The method of payment proved a dangerous one, however, in that it so largely swelled the volume of the Union Pacific's quick liabilities.

In 1891 Mr. Gould again began buying Union Pacific stock. Mr. Adams therefore resigned late in the year, and Mr. Dillon was elected to his position. The time was not ripe for expansion of any kind, and Mr. Gould's death the following year put an effectual check on any schemes which he might have entertained. The immediate problem was the floating debt, swollen to unwieldy proportions by the acquisition of branch lines, and in particular by the purchase of the Oregon Railway & Navigation Company. During 1890 a block of collateral bonds was issued and sold, but the remainder of the proposed issue was kept back in the hope of a better price. While waiting, Mr. Gould devised a scheme for the postponement of the payment of these and of other quick liabilities by the issue of three-year collateral notes, to be underwritten by a syndicate composed of himself and of other gentlemen interested in the property. These notes were to bear 6 per cent, and were to be issued at 92½ to such holders of the floating debt as would accept them, the syndicate taking care of the balance. The authorized amount was to be $24,000,000, of which $5,500,000 were to be issued at once. The plan was declared operative on September 28, 1891. If, now, the Union Pacific had been a moderately capitalized corporation, with fixed charges normally well below its earning capacity, and if, in 1894, when the notes were to mature, the market conditions had been more favorable than in 1891, it is probable that this scheme, temporary as it was, would have met the needs of the situation. Since neither of these contingencies occurred the insufficiency of the plan may be said to be in part the misfortune of the Union Pacific and in part its fault. It was a particular misfortune that the severest panic since 1873 should occur when the road was staggering under a load which it could scarcely bear; but it was altogether a fault that the railroad should have been so burdened as to be able to lay by no reserve in good times for the hard times which were bound to come.

In 1892, therefore, the Union Pacific was in a difficult position. Its capitalization was high; its earnings had shown scarcely any increase for five years; its surplus had not been sufficient to prevent the accumulation of a large floating debt; it had to prepare to raise a large sum of money in two years for the payment of its short time notes; and, in addition, there was ahead a fact of which little has been said so far, — the maturing of the government indebtedness.

Briefly sketched, the history of this indebtedness was as follows: The Acts of 1862 and 1864 had provided for the issue of government bonds for stated amounts per mile on the subsidized portions of the system in aid of construction, which bonds were to mature thirty years from date of issue, and to have a lien on the property covered second only to the first mortgage of the company. The rate of interest was 6 per cent, payable to the bondholders by the Government; and in 1875 the Supreme Court decided that the company was not obliged to repay to the Government the accruing interest before the maturity of the bonds.[1] This ruling was regarded as a victory for the company, but meant the steady piling up of arrears of interest, lessened only by the retention by the Government of one-half the amounts due for government transportation, and, under the Thurman Act, of such additional sum not in excess of $850,000 as, added to the whole compensation for government services and to the 5 per cent of net earnings set aside under the Act of 1862, should make the annual contribution equal to 25 per

[1] 91 U. S. 72.

cent of the net earnings of the company, unless the remaining 75 per cent should be insufficient to pay the interest on the first mortgage bonds; in which case the Secretary of the Treasury was authorized to remit a portion of the 25 per cent of net earnings required.[1] The Thurman Act did not fulfil expectations. The Supreme Court in 1891 held that expenditures for new construction and new equipment could not be deducted from gross earnings in ascertaining net earnings,[2] but the road met hard times and the maximum limit of the contributions to the sinking fund was not attained, and in investing the fund in government bonds the Secretary of the Treasury was compelled to pay high premiums, thus reducing the net interest; so that from the beginning to 1892 the question of indebtedness to the Government occasioned constant dispute and litigation, introduced uncertainty into the affairs of the railroad, and caused hard feelings between it and the Government. In 1892 the necessity for some settlement was near at hand. The principal of the government debt matured as follows:

| | |
|---|---|
| November 1, 1895 | $640,000 |
| January 1, 1896 | 1,440,000 |
| February 1, 1896 | 4,320,000 |
| January 1, 1897 | 6,640,000 |
| January 1, 1898 | 17,342,512 |
| January 1, 1899 | 3,157,000 |
| | $33,539,512 |

Deducting from this amount the sums paid to the Government and the company's credits for mail and carriage, and adding arrears of interest, the sum due the Government at the last of 1893 was approximately $52,000,000.[3] It was obviously highly difficult for the company to pay this sum in 1892 or 1898 or any other time, and for some years both the company and the Government had been earnestly discussing schemes for refunding, and the advantages and

[1] Statutes at Large, 45th Congress, 2d Session, chap. 96.

[2] The Court held that while up to the passage of the Thurman Act expenditures for improvements could be deducted from gross earnings in calculating net, the language of that Act seemed to preclude the deduction of any charges for improvements or betterments, or increase of permanent value of the works in any manner whatever. See 99 U. S. 402; 99 U. S. 455; 138 U. S. 84.

[3] Report of the Government Directors for 1893.

disadvantages of the ownership and operation of the road by the United States. Thus in 1892 an overwhelming obligation was hanging over the Union Pacific; and did not crush it only because the inability of the road to pay was so evident, and the inadvisability of government ownership was so strongly believed in, that every one felt that the necessary concessions would be made.

In 1893 the sinking-fund 8 per cent bonds matured to the amount of $5,176,000, and were partially extended and partially paid off through the medium of an underwriting syndicate; but this was the last attempt to meet indebtedness coming due. During the year both gross and net earnings fell off enormously, owing to the general depression of business, and particularly to the stagnation upon the Pacific coast. Freight rates were said to be in a state of chaos; and the Union Pacific served notice that it would withdraw from the Western Passenger Association on October 10. As the year wore on the continued decrease in earnings made the situation desperate. "The company for the year ending December 31, 1892," said Mr. John F. Dillon, counsel for the Union Pacific, in November, "had a surplus of $2,000,000. In the month of September (1893) there was a loss of net revenue of $1,500,000 as compared with the preceding year, and from January 1 to August 31 there has been a falling off in net revenue of over $2,500,000. The company is indebted for labor and materials on October 1 to the amount of $1,500,000; and its sinking-fund and interest charges for September would be more than $1,000,000; for October $750,000, for November $850,000, for December $1,000,000, and for January $1,000,000. There will be a deficit for the year 1893 of at least $3,000,000 and the company is without money or means to meet these obligations. . . ."[1]

Under these conditions a receivership was the only device which could prevent the dismemberment of the system and protect the interests of all the creditors; and accordingly, on application of parties friendly to the company, Messrs. S. H. Clark (president of the Union Pacific), O. W. Mink (comptroller), and E. E. Anderson (government director), were appointed in October;[2] Mr. Clark taking charge of the operation of the road, and Messrs. Mink

[1] Chron. 57: 684, 1893. [2] Ibid. 57: 639, 1893.

and Anderson of the financial and legal business.[1] One month later, on application of the Attorney-General, Messrs. John W. Doane and Frederick R. Coudert were appointed additional receivers to safeguard the government interests and to assist the other receivers in the general administration of the property.[2] These gentlemen remained in office until the reorganization was complete, though various portions of the system passed from their jurisdiction from time to time.

The appointment of receivers closed a long struggle to maintain the solvency of the road. A reorganization was now in order, and in this it was to be possible to do what Mr. Adams had not been able to do, — namely, to rearrange the capitalization of the road, thereby permanently lessening the fixed charges and securing a reserve of earning capacity sufficient to avoid bankruptcy when receipts for any cause should show a considerable decrease. This was the fundamental condition of future prosperity. Besides, the debt to the Government had to be settled, cash raised to pay the floating debt, including the three-year notes of 1891, and the system held together so that its earning capacity should not be destroyed.

As might be expected, it was the debt to the Government which was most publicly and persistently discussed. There seemed to be four ways in which this might be handled:

First, the Government might have cancelled the obligation and have remained satisfied with the enormous economies which it had secured in the transportation of mails and other government business. In the seven years between 1867 and 1873 alone the Quartermaster-General estimated that the Union Pacific had saved the Government $6,507,283 in the cost of moving troops and supplies,[3] and there was no doubt that by 1896 the investment of the Government, with interest, had been many times regained. But it was pointed out not only that the Union Pacific deserved little considera-

[1] Sen. Com. 1896, 54th Congress, 1st Session, Doc. No. 314, p. 42, testimony of E. E. Anderson. For bill of complaint see Report of the Commissioner of Railroads, 1894, pp. 99–120.

[2] Ibid. pp. 391–2, testimony of O. W. Mink. This gave to the Government three out of the five receivers. For petition of the Attorney-General see Report of the Commissioner of Railroads for 1894.

[3] Chron. 16: 292, 1873.

tion, in that its earnings had been wrongfully diverted from the payments demanded by the Thurman Act by the manipulations of Gould and others, but that the precedent of renouncing a just claim would be an extremely bad one for the Government to set.

Second, the Government might have exacted larger payments to the sinking fund, and have extended the debt at an unchanged rate of interest until it should be automatically discharged. This was the proposal of Mr. Hampton, Commissioner of Railroads, who suggested the amendment of the Thurman Act as follows: it should embrace all the United States bond-aided Pacific railroads; it should compel the contribution of 50 per cent of net earnings to a sinking fund instead of 25 per cent, and should extend the indebtedness to the Government until discharged as provided. If any company should abandon a portion of a subsidized line or divert its business from a subsidized to an unsubsidized line, that company should transfer the conditions which were attached to the former to the latter, in order to protect the interests of the United States Government.[1] The weak points in this scheme were many. Among them may be pointed out the fact that contributions to the sinking fund under the Thurman Act had been necessarily invested in government bonds, which, in view of the premium at which they were necessarily purchased, yielded a very small return. To double the contributions would have been to double the amount of the railroad's funds sunk in but slightly remunerative investments; and the Government did not seem inclined to permit the company to adopt the only practicable alternative, that of investing its sinking fund in its own securities. Also, Mr. Hampton's amendment would have continued to an enhanced degree the constant suspicious supervision of the company by the Government which had been, perhaps, the chief evil result of the Thurman Act.

Third, the Government might have consented to a refunding of the indebtedness to it at a lower rate of interest. This was most urgently pressed by representatives of the road. Mr. A. A. H. Boissevain, representing the Dutch bondholders, proposed to redeem the first mortgage by the securities in the sinking fund so far as possible, and to renew the rest at a lower rate of interest; — after

[1] Report of the Commissioner of Railroads, 1895, p. 14.

which the Government was to be given a 100-year 2 per cent bond for the principal and interest of its claim.[1] Attorney-General Olney similarly suggested a renewal of the first mortgage bonds at a rate of not over 5 per cent, and an exchange of 100-year 2 per cent bonds for the government claim; though he differed somewhat from Mr. Boissevain as to the lien which these bonds should have.[2] Congress and the Government Directors in 1894 were inclined to insist on harder terms. The latter, in their annual report, proposed that the first mortgage bonds be paid off in cash, and that a 100-year 3 per cent instead of a 2 per cent bond be given to the Government, with elaborate provision for a sinking fund; and the former had before it in the Reilly Bill a very similar suggestion.[3] As a counter-proposition the railway company offered to pay off the first mortgage bonds in cash if the Government would take a 50-year 2 per cent instead of a 3 per cent bond for its claim. "The petitioners further represent," it said, "that it will be utterly impossible to obtain the very large sums referred to from the stockholders unless it be possible to offer to them in satisfaction of their assessments reasonable security for the moneys so advanced. At a meeting recently held, at which were present representatives of a large amount of the stock of the said company, the conclusion was reached that if the debt to the Government could be funded substantially on the terms of the Reilly Bill, but at a rate of interest of 2 per cent per annum instead of 3 per cent, the said stockholders would endeavor to raise the funds needed for the purpose of meeting the requirements of the Reilly Bill."[4] Finally, Mr. Pierce, on behalf of the Fitzgerald Reorganization Committee, proposed that the Government either take 4 per cent bonds for the principal of its debt, and preferred stock for the interest, carrying into the settlement with the Government the scheme which was found best adapted to the satisfaction of other creditors; or that it take a 3 per cent first mortgage bond for its principal, and a second mortgage non-interest-bearing bond for its interest; or that it accept a lump sum of money equal to the value of its lien, which he informally estimated as 50 per cent of the total

[1] Ry. Rev. 34: 335, 1894.

[2] Chron. 58: 775, 1894.

[3] Ibid. 60: 132, 1895.

[4] Report of the Commissioner of Railroads, 1895, pp. 9–10.

amount due.[1] The plan of refunding was the most obvious as well as the most practicable of all suggestions. It had, however, the disadvantage from the point of view of the Government of surrendering some part of the government claim, and from that of the company of continuing the relations of the Government with the road.

Fourth and last, the Government might have demanded payment in cash. The sum which the company would have had to obtain was extremely large, but the accumulated sinking fund reduced it considerably, and many thought that the balance could be raised. In March, 1896, before a Senate committee, Mr. John Rooney, for the first mortgage bondholders, proposed that the Government, through a commission, should buy in the Union Pacific at foreclosure sale, should issue a new general mortgage at a lower rate of interest than the existing prior liens, and should pay off both the first and the government mortgage with the proceeds; — the road to be turned over to the subscribers.[2] This suggestion took place among many others which were in the nature of a compromise. Thus the reorganization committee, in 1895, offered to pay the principal of the government debt provided that the interest were cancelled;[3] and Receiver Anderson proposed in 1896 that the company pay the principal of the debt by adding funds raised by it to the amount of the sinking fund, and settle the arrears of interest with a 50-year 2 per cent bond. Full payment in cash was, of course, what the Government desired, and everything short of that it hesitated to accept; but equally, of course, full payment was what the bondholders of the road were most unwilling to concede; and hearing after hearing took place before committees of the Senate and of the House without definite result.

Meanwhile the general reorganization of the company was going on. In November, 1893, the various interests and factions of the road held a conference in New York, which resulted in the choice of a reorganization committee as follows: Senator Brice, chairman; Mr. A. H. Boissevain, for the foreign holders; General Louis Fitz-

[1] Senate Commission, 54th Congress, 1st Session, Document 314, testimony of W. S. Pierce. See generally the report of this committee for a discussion of alternatives from the government point of view.

[2] Ibid. Testimony, pp. 451–2.

[3] Chron. 60: 303, 1895.

gerald, president of the Mercantile Trust Company, for the Gould interests; Mr. Carr, for the estate of F. L. Ames; General Dodge, for the Denver and Gulf roads' interests; and Colonel H. L. Higginson, for the Oregon Railway & Navigation interests.[1] Subsequently Mr. J. P. Morgan accepted a place.[2] This committee was the only comprehensive one appointed until 1895; but numerous other committees sprang up to represent special interests of one kind or another, appearing frequently as interest on new classes of bonds was defaulted, and having, with the main reorganization committee, to deal specifically with the payment of the floating debt and the reduction of fixed charges. Upon the ability of the committees to agree depended the retention of the Union Pacific in something like its existing shape.

Aside from the question of the government debt there seemed to be a general agreement as to what was needed to be done. Every suggestion contemplated the payment of the first mortgage in full and the reduction of the interest upon the junior securities; most included with this an assessment on the stock, and one at least proposed the cancellation of the guarantee on the stock of the Oregon Railway & Navigation Company.[3] The principles were obvious. A large sum of money had to be raised with which to pay the floating debt and to meet possible demands by the Government. This had to come from the junior securities or from the stock, and preferably from the stock, which represented ownership in the enterprise. On the other hand, reductions in fixed charges had to come from the junior securities as the youngest interests which had a mortgage lien. Differences of opinion occurred upon the details. Should there or should there not be a foreclosure? How large an assessment was required? How great must the reduction in interest charges be, and should bonds or stock or both be given to the junior securities in exchange for their holdings? Should the system as it stood be preserved, or should certain parts of it be let go?

In June, 1894, Mr. Boissevain stated that the reorganization committee thought that they should be in a position to formulate a

[1] Ry. Times, 64: 732, 1893. Mr. Brice was also a member of the Senate Committee on Pacific Railroads.

[2] Ry. Age, 18: 883, 1893.

[3] Ry. Times, 65: 336, 1894.

complete plan of reorganization speedily after the terms of the adjustment of the debt to the United States had been approved by Congress. "It is our opinion that the fixed charges of the reorganized company . . . should not exceed $8,500,000 per annum. Certain classes of existing bonds secured by mortgage on portions of the system cannot be and should not be disturbed, as they are amply secured by property earning the interest which is payable thereon. Other bonds, however, must be converted in whole or in part into securities not imposing a fixed charge upon the reorganized company. While the reorganization committee has not approved of any definite plan, we believe that holders of bonds which must be disturbed and creditors and stockholders interested in the system can be provided for upon an equitable basis by the creation of the following securities:

(*a*) An issue of general mortgage bonds (at 4 per cent), secured by a general mortgage covering the entire system, subject to such mortgages as cannot be disturbed, and to the lien of the United States upon the main line and Kansas Pacific division for the adjusted debt.

(*b*) An issue of 5 per cent preferred stock.

(*c*) An issue of common stock.

The plan of reorganization would require provision to be made to take up the trust notes secured by valuable collaterals. The funds required for this purpose and for the other cash requirements of the reorganization would be met in part by a reasonable assessment upon the stockholders, and in part by the sale of new securities." [1]

A not dissimilar suggestion was made by the Government Directors in 1894. They proposed to ascertain the minimum net earning power of the railroad or railroads to be reorganized, and to issue a blanket mortgage of 3 per cent 100-year bonds to an amount such that the accruing interest would not exceed the net earning power. By sale of a portion of these bonds, together with a $10 assessment on the stock, and the use of the moneys and securities in the sinking fund, they would have paid off the prior liens, and then, after ex-

[1] Ry. Times, 65: 750, 1894. The reorganization committee stated that this plan was not final. They concurred, however, with Mr. Boissevain in his recommendation of the above scheme.

changing the new 3 per cent bonds for the government claim, they would have used the balance to retire the junior securities, adding preferred stock, so much as necessary, to compensate for the difference in yield between the old securities and the new ones received. The amount of securities required they estimated at $150,000,000 3 per cent bonds, $20,000,000 preferred stock, and $61,000,000 common stock; the latter exchanging for old common stock at par.

Both of these plans contained excellent features, chief among which were their provisions for the raising of cash and their use of preferred stock. The cash which Mr. Boissevain proposed to raise was to meet the floating debt, for he hoped to refund the government indebtedness; and while he may scarcely seem to deserve commendation for not attempting to fund the quick liabilities as well, this is not the case, as the history of the Union Pacific itself can demonstrate. The Government Directors intended to use the cash procured not only for settling the floating debt, but also for partially retiring the prior liens, so under their scheme an assessment was quite inevitable; and having made that as large as they dared they are not to be criticised for resorting to the sale of securities for the additional funds required, especially since these securities were to have a first lien on the road. As regards the preferred stock it is not clear from his statement at the time whether Mr. Boissevain had in mind the exchange of junior securities for bonds and stock or some for bonds and some for stock alone, but subsequent developments show that his intention was the former. Thus his idea was the same as that of the Government Directors, viz., to give the junior bondholders a right to a low rate of interest well within the earning capacity of the road, and to join with this the right to a higher return whenever the road should earn it. Mr. Boissevain's estimate of the maximum fixed charges which the road could safely stand was, however, high, and the plan of the Government Directors, if conservatively carried out, would have been better. Finally, the Government Directors contemplated foreclosure, while Mr. Boissevain did not; the relative merits of the plans on this point depending largely on the terms which the bondholders could be induced voluntarily to accept.

During 1894 and 1895 discussion was active, both in Congress and out, while the reorganization committee worked over the scheme which Mr. Boissevain had put forward, without making any formal announcement of a plan. Everything depended on the terms upon which the United States should insist. The reorganization committee hoped for a refunding of the government debt at 2 per cent. It had suggested that it would raise the funds to pay off the prior liens if Congress would take a 2 per cent 50-year bond in satisfaction of the government claim, would extend the provisions contained in the Reilly Bill to a committee charged with the duty of purchasing the property of the Union Pacific, and would grant the committee the power to form a successor corporation for the general purpose stated in the Acts of 1862 and of 1864, and with the general powers given in those Acts, together with the same rights, privileges, and freedom of action that were exercised and enjoyed by other railroads.[1] Subsequently it had offered to pay the principal of the government indebtedness in cash, providing that the Government would relinquish all claims to interest.[2] If either of these propositions was accepted it was willing to go ahead; while if both were refused, and no official counter-proposition was made by the United States, it seemed idle for the general reorganization committee or any other committee to promulgate a plan.

But meanwhile the Union Pacific system was disintegrating; partly from the efforts of the receivers to rid themselves of branches and contracts which had become burdensome, and partly through the action of bondholders of subsidiary roads who refused to wait for the slow action of Congress, and insisted on foreclosure of their liens. As early as August, 1893, ex-Governor Evans, a prominent stockholder of the Union Pacific, Denver & Gulf, had petitioned for an accounting from the Union Pacific, alleging that the branch was being bled for the advantage of the main line. When receivers for the Union Pacific system were appointed Mr. Evans petitioned for a separate receiver, and was granted his request. Litigation followed, and an attempt was made to get Mr. E. E. Anderson appointed as co-receiver; but the machinery of foreclosure and sale were duly put in motion and the line became separated from the parent company. In October, 1893, in view of an impending default, the Fort Worth & Denver City Railway Company was placed

[1] Chron. 60: 132, 1895. [2] Ibid. 60: 303, 1895.

in the hands of receivers, as was the same month the Denver, Leadville & Gunnison and the St. Joseph & Grand Island. In April, 1894, a receiver was appointed for the Leavenworth, Topeka & Southwestern; in June one for the Oregon Railway & Navigation Company. Foreclosure proceedings against these and other branches were instituted, and were attended by a very considerable measure of success.[1] On the other hand, the receivers were anxious to get rid of onerous contracts and unprofitable branches. On the 16th of March, 1894, they formally abandoned the Leavenworth, Topeka & Southwestern. In July, 1894, they petitioned to be relieved from certain guarantees and contracts, and asked instructions concerning the operation of certain lines. Judge Sanborn, in the United States Court at St. Paul, set November 15 for a hearing, and appointed a special master to take testimony. The master reported in October. He recommended the continuance of operation of most of the lines in question, but found that the receivers were not bound by the disputed contracts; and in November Judge Sanborn confirmed the bulk of his report. The net result was a reduction in the mileage of the Union Pacific from 8167 in the latter part of 1893 to 4469 in May, 1895; at which time proceedings against the Oregon Short Line Railroad Company threatened to withdraw 1424 miles besides.

With matters in this state the reorganization committee was genuinely discouraged by the refusal of Congress to pass the Reilly Bill, providing for a refunding of the government debt; although this had been reported to the House with the alternative amendment proposed by the committee accepting the payment in cash of the principal of the government debt in full satisfaction of claims against the company.[2] Since Congress had earlier refused a proposition to pay off the prior liens in full on condition that the government debt be refunded at 2 per cent,[3] it was felt that nothing but cash payment of principal and interest would be acceptable, and this the committee refused to undertake. On March 8 the announcement was made that the reorganization committee of the Union

[1] For a summary of the foreclosure suit pending in 1895 see the Report of the Government Directors for that year.

[2] Chron. 60: 303, 1895.

[3] Chron. 60: 132, 1895.

Pacific road had abandoned its task and would return the securities deposited with it, and a few days later the actual disbandment took place.[1]

Between March, 1895, and the following October little progress was made. With the dissolution of the general reorganization committee disappeared the one body capable of formulating a comprehensive scheme and of securing its widespread acceptance. The committees which remained represented each some one or two mortgages, and were thus confined too narrowly in their sympathies to command much confidence from bondholders as a whole. Late in 1895, however, new interests undertook the reorganization of the property, and another general committee was formed, comprising General Louis Fitzgerald; Marvin Hughitt, president of the Chicago & Northwestern; Chauncey M. Depew, president of the New York Central; Jacob H. Schiff of Kuhn, Loeb & Co.; Oliver Ames, director of the Union Pacific; and T. Jefferson Coolidge, Jr., president of the Old Colony Trust Company.[2] This committee's plan of action was noteworthy in three particulars. First, it contemplated a foreclosure sale. This, it is true, was but resignation to the inevitable, for foreclosure suits were already under way, and an attempt to check them would have had scarcely a possibility of success. Second, it made no definite provision for the government debt. A certain amount of bonds and stock were reserved from the securities proposed to be issued for the purpose of settling the government claim, but the exact method in which that indebtedness should be treated was left for future arrangement. Third, it did not attempt to meet the collateral trust notes of 1891, which constituted so large a portion of the floating debt. "The securities embraced in these trusts," it declared, "are largely those of companies which have already, by orders of court made in the original general receivership, or in independent foreclosure proceedings, lost in part or in whole their character as parts of what has been known as the Union Pacific system. Independent reorganization of many of these properties are pending. The purposes which brought into existence guarantees of the obligations of many of these auxiliary companies have been accomplished by construction or otherwise, and

[1] Ry. Rev. 35: 153, 1895. [2] Chron. 61: 663, 1895.

considerations will not exist, upon reorganization, for continued relations with (them) upon the basis of any assumption of their fixed charges."[1] Thus, at the very outset, this new committee removed the three matters which had given its predecessors the most trouble. The proposed foreclosure made it both easier to get assents to a plan and more difficult to block its operation; the postponement of the question of the government debt allowed the committee to go ahead without waiting for Congress; and the refusal to provide for the collateral notes relieved it of many difficulties, and threw the holders of these notes back upon the collateral which they had exacted as security.

The plan of the Fitzgerald Committee followed, for the rest, the general lines earlier laid down by the Brice Committee. To retire all existing mortgage indebtedness it proposed to issue:

| | |
|---|---|
| First mortgage railway land grant 50-year 4 per cent gold bonds | $100,000,000 |
| 4 per cent preferred stock | 75,000,000 |
| Common stock | 61,000,000 |

The reasoning by which these sums were arrived at was as follows:

| | |
|---|---|
| The lowest net earnings the Union Pacific Railway had ever recorded had been those of 1894 | $4,315,077 |
| The committee planned to issue $100,000,000 4 per cent 50-year bonds, on which the interest would be | 4,000,000 |

This would be all the company would have to pay in any one year.

| | |
|---|---|
| The average net earnings for the 10 years before 1894 had been | $7,563,669 |
| To the $100,000,000 bonds the committee proposed to add $75,000,000 preferred stock. The annual dividend on this would be | 3,000,000 |

Payment on bonds and preferred stock together thus equalled the average earnings.

| | |
|---|---|
| Net earnings between 1885 and 1894 had gone in some years as high as | $9,000,000 |

To the above bonds and stock the committee wished to add $61,000,000 common stock, on which dividends might be paid if it seemed advisable.

[1] Chron. 61: 705, 1895. (Reorganization plan in full.)

New common stock exchanged at par for old; new bonds and preferred stock exchanged for old bonds, with a residue which was to be set off against the government debt and to be used for cash requirements. The cardinal principle of the reorganization was that no new 4 per cent bonds should be issued in exchange where the old mortgage did not contribute the full value; or, to put it more accurately, that no securityholders were to be given the right to claim a sum greater than their property could earn as judged from past experience. At the same time enough preferred stock was distributed to give bondholders the same returns as before when the road should earn it. A $15 assessment was levied upon stockholders. This was several times the quoted price of the stock early in 1896, but was not more than the stock would probably soon sell for after reorganization. A syndicate agreed to advance $10,000,000 to $15,000,000, for payment of coupons as they fell due and for expenses, in return for which they received $5,000,000 in preferred stock quoted at 59, or 19 per cent on a capital of $15,000,000 at current prices. In addition the bankers who managed the syndicate received $1,000,000 in preferred stock; making a total expenditure of $6,000,000, a not exorbitant commission. Besides the bonds and stock for strictly reorganization purposes, there was reserved to dispose of equipment obligations, and for reorganization and corporate uses, $13,000,000 in 4 per cent bonds and $7,000,000 in preferred stock. Reorganization uses, as defined by Mr. Pierce, were those which might arise unprovided for and of an extraordinary character, all of which could not be foreseen. Corporate uses were those which would be proper to the corporation thereafter, such, for instance, as the issue of securities in extension of the property.[1]

After all the securities of the old corporation had been accounted for there remained $35,755,280 of the first mortgage bonds and $20,864,000 of preferred stock as a fund or resource for the settlement of the government debt; or, in round numbers, an amount of 4 per cent bonds equal to the principal of that debt and an amount of preferred stock equal to the accrued interest. Just how this was to be used the committee did not pretend absolutely to say. "We

[1] See testimony of W. S. Pierce, Senate Commission, 1896, 54th Congress, 1st Session, Document 314.

desire to meet any proposition of the Government," said Mr. Pierce, "or to suggest any proposition which, after investigation, we believe will meet the approval of the Government within the limits of the financial possibilities of the property based upon this plan. In other words, we have made no sort of a hard and fast rule." In case the Government should prove obstinate and should refuse settlement on reasonable terms, it was the idea of the committee that it would be entitled on foreclosure to its share as a second mortgage bondholder only, and that the property would pass under the sale free from all liens, including that of the United States. "Our view upon that point," said Mr. Pierce, "is that when the Government subordinated its lien to that of the first mortgage bondholders, it did so deliberately and in terms effective for that purpose. The Government then consented to all remedies that were necessary for the protection of this prior lien; and an indispensable element of such priority would be the right of foreclosure. And unless there was a concealed purpose on the part of the Government, that right of effective foreclosure was undoubtedly impliedly granted." [1]

Subsequent negotiations with the bondholders brought a reduction in the proposed issue of mortgage bonds from $100,000,000 to $75,000,000, affecting the Kansas Pacific consols and the Union Pacific Sinking Fund 8s. Thus the former were allotted 50 per cent in first mortgage 4s and 110 per cent in preferred stock, instead of 80 per cent in 4s and 50 per cent in preferred as before; and the latter 75 per cent in 4s and 100 per cent in preferred stock, instead of 100 per cent and 50 per cent respectively. This reduced the proposed charges $1,000,000, and proportionately strengthened the scheme.

On the whole, the plan was a strong one. It reduced fixed charges from over $7,000,000 to under $4,000,000, with an eventual lower limit of $3,000,000, and this amount such good authorities as Messrs. Mink and Clark pronounced the road safely able to earn in spite of the reduction in its mileage.[2] During the receivership, moreover, the system had become purged by the cancellation of onerous contracts and the lopping off of unprofitable branches, and though some lines were lost which it was desirable to retain, the Union Pacific was not precluded from the repurchase of these, and did in fact regain

[1] Testimony, Senate Commission, 1896, p. 23. [2] Ibid.

the most important. The bondholders were put in no worse position than before, for they could never permanently get more than the earnings of the road, and this the new distribution of securities generally assured them. The position of the common stockholders was improved, for whereas between 1883 and 1893 fixed charges had only once fallen below $7,300,000, now less than $7,000,000 were to be taken before their claims were heard, while both the gross and the net earnings of the road promptly regained their old level. Finally, the general principle was sound, as has been emphasized several times before. It gave to each class of securities a claim to interest strictly proportional to the earning capacity of the road, and added to this a preferred stock on which no payment was to be made unless earned; while it provided for a liberal assessment upon stockholders, and attempted no funding of the current liabilities incurred during the past troubled years.

The time limit for deposits under the plan was originally set at December 31, 1895. It was then extended to January 15, 1896, and later to January 29 of that year. By January 8 the reorganization committee was able to announce that it had secured majorities of all of the first mortgage bonds outstanding except an inconsiderable shortage in one class. This was followed, in spite of some opposition among London brokers, by the deposit of a majority of the shares of the company, and by the assent of other securities. In January, 1896, in a letter to the chairman of the House Committee on Pacific Railways, Mr. Fitzgerald stated that his committee embraced a substantially single representation of all Union Pacific mortgage bonds in circulation except those held by the United States.[1]

Foreclosure proceedings had been long under way. In January, 1897, the Government agreed to join in them in consideration of a guarantee of a bid at least equal to the original amount of government bonds, less payments made by the company to the Government, with interest at $3\frac{1}{2}$ per cent per annum.[2] The guarantee was

[1] Chron. 62: 187, 1896.

[2] Report of Commissioner of Railroads, 1897, p. 8. The Government's dealings with the reorganization committee followed upon the defeat in the House of a renewed proposition for refunding the Government's loan.

to be of cash, so that the Government's relations with the property would terminate completely upon confirmation of the sale. This was the first affirmative action which the Government had taken, and the reorganization committee accepted it, despairing of better terms. The guaranteed payment was in part offset by sinking-fund assets of $17,062,664, leaving a net amount to be provided of $28,691,336.[1] By August, 1897, foreclosure of the main line had been ordered by the courts in all the states through which the Union Pacific passed, both under the first and the government mortgages. Previous to this the plan of reorganization had been declared operative, and articles of incorporation for the new company had been filed; while the first instalment of the assessment on the stock was called by the middle of the month. An unexpected development now occurred. Although willing to join in foreclosure proceedings, the Government found the decrees of foreclosure to some extent unsatisfactory, and prepared the papers for an appeal. Objection was particularly made to the fact that the Omaha Bridge mortgage, amounting to about $1,200,000, was adjudged superior to the lien of the Government on that part of the road between Omaha and Council Bluffs, and that the money and assets in the hands of the receivers accruing from the operation of the roads were ordered to be sold instead of being reserved to meet a deficiency judgment expected to be obtained. Learning this, the reorganization committee increased its guarantee by over $4,000,000, making the total guaranteed bid $50,000,000 instead of $45,754,060. "This increase," said the Attorney-General, "removed the objections to the decrees so far as the money contents were concerned. In all else the decrees were just and satisfactory." [2] Even so, perhaps partly for political reasons, the Government was not ready to allow a sale, and later in the year gave notice that it would apply for a postponement to December 15, in order to give Congress an opportunity to consider the matter. The prospect of renewed congressional agitation stimulated the reorganization committee to prompt action. "The Committee," it declared, "has reached the conclusion that the interests

[1] The guarantee was provided by a syndicate with the same personnel as that which had agreed to advance the money for reorganization expenses.

[2] Chron. 65: 730, 1897; Report of Commissioner of Railroads, 1897, p. 9.

of the securityholders represented by it and of the syndicate furnishing the funds to finance the reorganization demand reorganization without any further delay. In this situation the committee contemplates . . . to oppose any adjournment of the sale of the main line and to bid it in, if need be, for the full amount of the Government's claim, the additional sum involved in this being \$8,000,000."[1] Postponement of the sale of the Kansas Pacific was to be allowed, the committee meanwhile making up its mind on what terms to bid it in. This proposition was telegraphed to Washington and quickly accepted. It constituted a complete surrender on the part of the committee, so far as the Union Pacific proper was concerned. Instead of being refunded, the government debt was paid off in cash; instead of compromising for the principal alone, both principal and interest were paid in full. The result reflects credit on the sharpness of the Attorney-General, but the method was scarcely worthy of the Government which he represented.

November 1st and 2d, 1897, the property was sold under foreclosure of the government and first mortgage liens, and the prices were:

| | |
|---|---|
| For the Union Pacific main line, | \$40,253,605 |
| For bonds in the government sinking fund, | 13,645,250 |
| | \$53,898,855 |
| In addition the Government received in cash in the sinking fund as of November 1st, | 4,549,368 |
| | \$58,448,224 |
| In addition to this sum the committee was obliged, under its agreement with the Government, to buy up the first mortgage, amounting to | \$27,637,436 |
| The total of the first and second mortgages was | 67,891,041 |
| Adding | 13,645,250 |
| Of securities purchased for cash, the total payment aggregated over | 81,500,000[2] |

On February 12, 1898, the reorganization committee bought in the Kansas Pacific, guaranteeing for the Government a bid at the sale which should equal the principal of the government debt, *i. e.* \$6,303,000.[3] Other minor roads were also bought back on fore-

[1] Ry. Age, 24: 897, 1897.

[2] Report of the Commissioner of Railroads, 1898, p. 9.

[3] The entire indebtedness of the Kansas Pacific to the Government was \$12,891,900. After the sale the Government brought suit for the balance, but received a decree for \$821,898 only.

closure sales, and from time to time as the mortgage committee sold the collateral back of the trust notes of 1891 the Union Pacific Railroad Company bought portions of the same. In 1899 the Union Pacific stock was increased $27,460,000, and the new issue was exchanged share for share with Oregon Short Line stock, thus regaining control of that important property. Later the same year a further increase was effected to retire $14,000,000 Oregon Short Line bonds and $11,000,000 Oregon Railway & Navigation Company preferred stock. The net result was to avoid any considerable dismemberment of the system. Whereas 7673.59 miles had been reported for 1892, 5399.01 were reported for 1899. The main line from Portland, Oregon, to Omaha and Kansas City, via Ogden, Cheyenne, and Denver, was kept intact, the principal losses being of branch lines in Nebraska and Kansas.[1]

A detailed account of the later financial operations of the Union Pacific divides the company's recent development into three parts:[2] First, the regaining of control of the principal auxiliary systems and branch lines which the receivership had temporarily separated from the parent stem; second, the purchase of large amounts of stock in the Southern Pacific and the attempt to share in the control of the Burlington, which latter involved the purchase of Northern Pacific stock and the formation of the Northern Securities Company; and third, the sale of the stock acquired in the fight over the Burlington, and the subsequent purchase of Alton, Atchison, Baltimore & Ohio, Illinois Central, and other stocks. The repurchase of auxiliary lines has just been alluded to; and into the history of the Burlington struggle there is no need to go at length.

On June 30, 1900, the Union Pacific, Oregon Short Line, and

[1] Cf. H. R. Meyer, The Settlements with the Pacific Railways, Quarterly Journal of Economics, July, 1899. The receivership records have been published in fourteen volumes.

At its final meeting in 1898 the reorganization committee nominated a proxy committee of five members "to permanently represent, at the annual and other meetings, such holders of common and preferred stock as (should) desire to entrust their proxies to the said committee for the purpose of maintaining the management and general policies inaugurated by the reorganization committee." This took the place of a compulsory voting trust.

[2] Thomas Warner Mitchell, The Growth of the Union Pacific and its Financial Operations, Quarterly Journal of Economics, vol. 21, p. 569, 1907.

Oregon Railroad & Navigation Companies operated 5427.89 miles of line. The system stretched from Kansas City and Council Bluffs to Ogden, and reached the Pacific coast in the Northwest at Portland. It had no rails of its own in California, but was dependent on the Southern Pacific tracks for connections both at Ogden and at Portland. The Southern Pacific extended from New Orleans through Texas, New Mexico, and Arizona to California, and thence up the coast to Sacramento. At Sacramento it divided; one line continued north to Portland, and one turned northeast through Nevada to Ogden, Utah. Now, in 1901 it so happened that the Southern Pacific was for sale. Crocker, Stanford, and Huntington, who had controlled it, were dead, and their successors were not eager to retain the railroad as an independent line. Mr. Harriman seized the opportunity. In 1901 he bought for the Union Pacific 750,000 shares out of a little less than 2,000,000, and the following year he increased his holdings to 900,000. The Union Pacific financed the purchase by the issue of collateral bonds. The acquisition was of vast importance. Not only did it afford a direct connection between Ogden and the coast, but it eliminated one of the Union Pacific's four great competitors in transcontinental business, and made Mr. Harriman the dominant figure in the Southwest.

North of the Ogden-San Francisco line the conditions were less satisfactory. The Great Northern and the Northern Pacific were here supreme, and in 1901 were negotiating for the purchase of the Burlington to give them an entrance into Chicago. Mr. Harriman asked for a share in this purchase but was refused. He thereupon began to buy Northern Pacific stock in the endeavor to secure by this a half control in the more eastern road. It was the struggle which then ensued between Mr. Harriman and Mr. Hill which caused the stock exchange panic of May, 1901, and which resulted in the formation of the Northern Securities Company, in which Mr. Harriman was allotted a large though not a controlling interest. On the break-up of the Northern Securities Company the Union Pacific received back some $25,000,000 in Great Northern and $32,000,000 in Northern Pacific shares,[1] worth at market prices about $100,000,000.[2]

[1] Besides $824,910 in Northern Securities stubs.

[2] See B. H. Meyer, A History of the Northern Securities Case, Bulletin of the University of Wisconsin, July, 1906.

This Northern Securities episode had little effect on traffic conditions in the Northwest, but it did profoundly influence the financial policy of the Union Pacific during the following years.[1] The dissolution of the Northern Securities Company gave to the Union Pacific Great Northern and Northern Pacific shares, which were valuable as investments only. And as investments these stocks soon became undesirable. We have said that the combined value of the securities transferred approximated $100,000,000 at the time of transfer. From that time on the stocks appreciated in value till they were worth from $145,000,000 to $150,000,000, and yielded an income of less than 3 per cent on their market price. It was good policy to sell them, and $118,000,000 worth were accordingly disposed of, leaving some $30,000,000 worth still in the hands of the company.[2] What should be done with the enormous resources thus secured? Some of the cash was used to buy Chicago & Alton stock, — some of it was put out in demand loans. But beginning with June 30, 1906, the Union Pacific and Oregon Short Line began investment in stocks of other companies on a great scale. $41,442,028 were put into Illinois Central stock; $10,395,000 into Atchison preferred; $45,466,960 into Baltimore & Ohio, common and preferred; $19,634,280 into New York Central; and lesser amounts into Chicago, Milwaukee & St. Paul, Chicago & Northwestern, St. Joseph & Grand Island, and other

[1] As in the Southern Pacific purchase the acquisition of the Northern Pacific stock was financed mainly by the issue of convertible collateral bonds. Some $30,000,000 besides, it is supposed, were borrowed from the banks.

[2] Testimony of Mr. Harriman before the Interstate Commerce Commission. It is true that the Northern Securities stock held by the Union Pacific system had been pledged as security for an equal amount of Oregon Short Line 4 per cent and Participating 4s, and that when these bonds were refunded there was pledged for the new issue whatever the Union Pacific interests should receive in exchange for their Northern Securities holdings, and any other shares or bonds at not exceeding 80 per cent of their appraised value. But the purchase of the Southern Pacific and of the Northern Pacific stocks had been previously financed by an issue of convertible collateral bonds for which other collateral had been pledged. From 1904 on, the rising price of Union Pacific stock made conversion desirable and rapidly released the securities back of the original issue. These released securities, with $18,000,000 Southern Pacific preferred stock paid to the Union Pacific in 1904 (with $2,460,960 cash), proved a sufficient pledge for the Oregon Short Line refunding bonds, and the Great Northern and Northern Pacific stock shares were therefore free for other purposes.

companies. In all, $131,693,271 were invested during a little over seven months.[1] This has been the characteristic feature of recent Union Pacific finance. The large purchases of stock in other roads have assured it favorable connections in the Illinois Central and in the Baltimore & Ohio, and have modified the severity of competition with the Atchison.[2] Including the Southern Pacific, its system reaches from Chicago to Portland, San Francisco, Los Angeles, and the Gulf, and has an influential voice in two of the principal roads connecting Chicago with the Atlantic seaboard. At the same time, the extensive investment of Union Pacific funds to secure gains unconnected with increase of traffic over its lines has provoked merited criticism. A railroad is, after all, a machine for transporting passengers and goods, not an engine of speculation; and both from the point of view of the community which it serves and of the investors who hold its securities it is advisable that its income should depend on the business which its managers conduct and are responsible for, and not on circumstances over which they have no control. So far as Union Pacific purchases have been designed to open connections or to modify competition they have had a sound foundation. So far as they have been financial operations only they are not to be commended.[3]

From the point of view of operation the success of the Union Pacific has been remarkable. Like most roads it came out of its receivership in better shape than it went in, but with much lacking for the efficient and economical handling of its traffic. Since 1900 over $52,000,000 have been invested in betterments and in new equipment, of which some $15,000,000 have been withdrawn directly from income. Maintenance charges have also been liberal, particularly in the last few years. Grades and curves have been eliminated, steel bridges have been put in place of wooden, new and

[1] Annual Report, 1907. See also Interstate Commerce Commission, Report in the Matter of Consolidations and Combinations of Carriers, Relations between such Carriers, and Community of Interests therein, their Rates, Facilities, and Practices, 12 I. C. C. Rep. 319.

[2] The Union Pacific acquired a half interest in the San Pedro, Los Angeles & Salt Lake Railroad Company in 1904.

[3] Recent reports suggest that a holding company is to be formed, which will take over the securities now owned by the Union Pacific Railroad.

heavier rails have been laid, ballast supplied, and equipment greatly enlarged and improved. Whereas in 1896 13 per cent of all the Union Pacific system was laid with iron rails, and only 24 per cent had rails weighing more than sixty pounds to the yard, in 1907 there was no iron reported, and only 33 per cent of the track did *not* have rails weighing more than sixty pounds to the yard. The average capacity of freight cars was a shade over twenty tons in February, 1898; it was over thirty-four tons on June 30, 1907, and the new freight cars added during the last-named year averaged a capacity of sixty-seven tons apiece.

In consequence of these improvements the Union Pacific has been able to handle a very greatly increased business. Between 1899 and 1907 the tons of revenue freight carried one mile increased from 1,393,207,990 to 5,704,061,535, and the passengers carried one mile from 167,117,388 to 680,278,509. This fourfold increase has been packed away in the larger cars, which in turn have been combined into longer trains. Twenty-one tons are now put into the average freight car, and thirty-two freight cars form an average train. In 1899 the average car held twelve tons and twenty-nine of them carried a train-load. Sixty-six is the average number of passengers per train to-day; thirty-three was the average number in 1899. And so the increased business has not occasioned a proportionate growth in cost. It takes but little more than three times the outlay in conducting transportation to do over four times the work, and other railroad expenses have varied even less.

This increased business and less rapidly increasing cost has meant, finally, an increase in profits, and explains how it has been possible in seven years to take $15,000,000 from income for improvements besides liberally maintaining the property. The Union Pacific is prosperous as it never has been before. In 1907 its total fixed charges, in round numbers, were $8,600,000, and its net income was $45,000,000. Of this income $23,500,000 were paid out in dividends, $1,960,000 appropriated for betterments, additions, and new equipment, and $10,700,000 carried to surplus. There were $69,000,000 in bills payable, incurred since 1906, in part for improvements and the like, but largely in the course of the company's financial experiments; but $75,000,000 in convertible bonds have been authorized to cover them. Stock and bond issues are much larger than in 1899 and will be larger still when the new convertibles are all sold. Fixed charges, however, are less than $5,000,000 greater than they were eight years ago. In order to imperil bond interest net earnings will have to decline by 81 per cent; and even were this to happen it is probable that some margin could be retained by a decrease in the generous sums now being spent for the maintenance of equipment and of road.[1]

[1] Dividends upon Union Pacific Railroad Stock:

| | *Per Cent* | | | | | | |
|---|---|---|---|---|---|---|---|
| | 1898 | 1899 | 1900 | 1901–4 | 1905 | 1906 | 1907 |
| Common | | | 3½ | 4 | 4½ | 8 | 10 |
| Preferred | 1½ | 3½ | 4 | 4 | 4 | 4 | 4 |