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Bonds - Income Bonds - Rights of Bondholders and Deductibility of Interest for Federal Income Tax Purposes

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COMMENTS

BONDS—INCOME BONDS—RIGHTS OF BONDHOLDERS AND DEDUCTIBILITY OF INTEREST FOR FEDERAL INCOME TAX PURPOSES— An income bond is an obligation of a corporation on which interest is payable only out of earnings, as distinguished from the ordinary corporate bond on which interest is a fixed charge regardless of earnings.[1] Long regarded as a hybrid security which is to be issued only as a last resort, income bonds have grown surprisingly in popularity over the past two decades.[2] It is the purpose of this comment to consider the historical background of income bonds, to make a comparative analysis of the bond indentures as they affect investors' rights, and to consider the deductibility of income bond interest in determining taxable income for federal income tax purposes. A study of the twenty-three companies whose income bonds are currently listed on the New York Stock Exchange[3] is the focal point for this comment, but the particular problems incident to unlisted bonds of small and closely-held corporations will also be considered.

I. *Rights of Income Bondholders*

Income bonds were issued chiefly in depression eras, notably 1873, the years following 1920, 1931 to 1937, and during the railroad reorganizations of the 1940's.[4] The income bonds were exchanged for fixed interest bonds or were issued to unsecured creditors to allow the corporation to extend the maturity dates of its obligations and to avoid interest during the interim, if earnings were not adequate. Their use was especially beneficial in the adjustment of the debt structure of railroads, because burdensome fixed charges could be avoided and yet reasonable protection to the creditor was assured through the relatively constant income. These bonds acquired a bad name with investors,

1 2 JONES, BONDS AND BOND SECURITIES, 4th ed., §606, p. 10 (1935): "Income bonds are the obligations of a corporation which are made payable as to either principal or interest, or both, only out of net earnings of the corporation." The comment will discuss only bonds, the interest on which is contingent upon earnings, because the modern bonds generally provide that the principal is to be paid regardless of earnings.

2 Chicago, Milwaukee & St. Paul Reorganization, 131 I.C.C. 673 at 694 (1928). Beginning in the 1930's, the Commission has approved reorganizations where income bonds played an important part in the capital structure.

3 See Appendix infra for a complete list of these bonds in alphabetical order.

4 1 DEWING, FINANCIAL POLICY OF CORPORATIONS, 5th ed., 232 (1953). According to Dewing, the earliest example of an income bond which has attracted attention was issued in 1848 by the Chesapeake and Ohio Canal Company.

commonly being called adjustment bonds.[5] However, the fact that nine out of the thirty-one income bonds listed on the New York Stock Exchange have been issued in a voluntary exchange for preferred stock since 1950[6] indicates that their value is being increasingly recognized.

The advantages to the corporation of income bonds over other securities are several. First, the market may not be ripe for the issuance of additional equity certificates; and conventional debt obligations may be equally unfeasible since fixed interest would climb too high because the earnings-times-fixed-charges ratio is low.[7] Second, in the case of corporations subject to governmental rate regulation making, the rate-making commission may, on the basis of a hypothetical debt ratio, reject applications for rate increases on the ground that the applicant has unnecessarily reduced earnings by paying more in taxes than would be necessary if part of the corporation's capitalization included securities with interest obligations.[8] Further, because banks and insurance companies are restricted in their selection of investment stocks, an issue of income bonds may appeal to a broader buying market. Finally, the deduction of the interest payments from corporate gross income for federal income tax purposes has probably been the most important current advantage. There are, however, some disadvantages to the corporation. In the past there has been investor resistance to buying income bonds,[9] although the present trend may be indicative of a growing acceptance. Also, under a carefully drawn indenture, interest must normally be paid when there are earnings,[10] whereas the use of preferred stock leaves discretion to the board of directors in declaring a dividend.[11]

5 Hansen, "Legal and Business Aspects of Income Bonds," 11 TEMP. L. Q. 330 at 332 (1937).

6 See Appendix infra, Nos. 1, 5, 7(c), 9, 10, 12, 15, 19(a), 22.

7 Investment regulations controlling the amount of stock that banks and insurance companies may hold provide an additional incentive for issuing income bonds in a reorganization. Thus if stock is issued in exchange for fixed interest bonds, such regulations may not permit it to be retained, with a resultant sale at a probable loss. Issuance of income bonds alleviates this problem.

8 Ardery and Abner, "Income Bonds Revisited," 57 PUB. UTIL. FORT. 517 at 523 (1956): "Many commissions appear to believe that there really is not only nothing immoral in carrying heavier debt in order to relieve the tax burden, but they seem to think it almost immoral not to do this, where the alternative is subjecting the public to higher rates."

9 GUTHMANN AND DOUGALL, CORPORATE FINANCIAL POLICY, 2d ed., 146 (1948).

10 Central of Georgia Ry. v. Central Trust Co. of New York, 135 Ga. 472, 69 S.E. 708 (1910).

11 See 12 FLETCHER, CYC. CORP., 1957 Rev. Vol., §5447 et seq.

From the point of view of an investor, several problems must be resolved regarding income bonds. Determination of the amount of earnings has caused difficulty. In the past, much of the controversy on this point has centered on the treatment to be accorded expenditures for assets of a relatively permanent nature.[12] In *Day v. The Ogdensburgh and Lake Champlain R. Co.*,[13] the court permitted a deduction from earnings for expenses incurred in leasing another road. The court held that the indenture did not limit the board of directors' discretion in the determination of earnings. A later New York case[14] reached a similar result, declaring that the statement in the indenture, permitting expenses and necessary repairs to be deducted from gross revenues, left the "fullest discretion" in the board to determine whether there are any earnings applicable to the payment of interest, and imposing only a requirement that the board act in good faith. When income is more definitely defined, however, any limitation on the board's discretion will be given effect.[15] Thus the cost of acquiring a new line cannot be charged to earnings. When limitations are imposed, the cases have uniformly permitted a deduction for depreciation.[16]

The indentures examined[17] indicate that this problem of drawing the line between necessary expenses, deductible in determining income for interest payments, and capital additions, not so deductible, has been the subject of careful draftsmanship. The indenture usually begins with the statement of a set rate

12 The often-quoted rule in Union Pacific R. Co. v. United States, 99 U.S. 402 at 420 (1878) is: "As a general proposition, net earnings are the excess of the gross earnings over the expenditures defrayed in producing them, aside from, and exclusive of, the expenditures of capital laid out in constructing and equiping the works themselves." Yet, it is interesting to note that the court permitted almost two million dollars over a six-year period for expenditures for "Station buildings, shops, and fixtures" in determining net income.

13 107 N.Y. 129 at 142 (1887). The indenture stated that interest was to be paid out of the net earnings of the company "after satisfying the expenses of operating and maintaining the same."

14 Thomas v. The New York and Greenwood Lake Ry. Co., 139 N.Y. 163, 34 N.E. 877 (1893).

15 Spies v. Chicago & E.I.R. Co., (S.D. N.Y. 1889) 40 F. 34.

16 Whitridge v. Mt. Vernon Woodberry Cotton Duck Co., (D.C. Md. 1913) 210 F. 302. As explained in Edwards v. International Pavement Co., 227 Mass. 206, 116 N.E. 266 (1917), all necessary expenses incurred in producing the revenue must be deducted before there is net income available for interest.

17 The phrase, "indentures examined," refers to the indentures of all the income bonds that were listed on the New York Stock Exchange as of April 1, 1958. See note 3 supra.

of interest being payable only out of "available net income." Available net income is usually defined as net income minus certain specified deductions.[18] Two of the indentures expressly define net income as that amount determined by the accounting procedures of the Interstate Commerce Commission.[19] The typical indenture, however, does not expressly define net income,[20] the implication being that it is to be determined by the general accounting procedures followed by the company in the past. For the indentures issued by railroads, compliance with the "Uniform System of Accounts for Steam Roads"[21] in determining "net income" seems justified.[22] Compliance with Regulation S-X presumably would also be warranted.[23] Once net income is found, the specific deductions must then be taken before arriving at "available net income." These specific deductions tend to eliminate the historical problem of the *Day* case, because deductions for capital improvements, with definite limits, are permitted in determining available net income.[24]

The right to an accounting to permit independent judgment as to whether net income exists has often been asserted by the bondholders. The granting or denying of such a remedy rests on the court's conception of the nature of the corporation's obligation. Thus, where the corporation's promise to pay interest if earned was not considered to create a trust relation between the company and the bondholders, an accounting was denied. The bondholder's remedy was stated to be an action at law for breach of contract.[25] The court's rationale was that since the promise did not create an equitable lien on the funds of the corporation,

18 Two of the indentures examined define income available for income bonds to be "net income before taxes." See Appendix infra, Nos. 1, 10.

19 See Appendix infra, Nos. 4, 6.

20 See Appendix infra, e.g., Nos. 1, 3.

21 24 Stat. 386 (1887), 49 U.S.C. (1952) §20(3), 49 C.F.R. (1949, 1958 Supp.) §10.

22 See Kansas City So. Ry. v. United States, 231 U.S. 423 at 453 (1913). The court states that the classification of accounts as prescribed by the Interstate Commerce Commission requiring some of the expenses in lowering the grade of the road to be charged as operating expenses rather than to a property account does not interfere with the preferred stockholder's contractual rights to dividends depending on income.

23 Regulation S-X contains the uniform accounting rules issued by the Securities and Exchange Commission.

24 The Baltimore and Ohio Railroad Company's Convertible 4½% Income Bonds, due 2010, provide an example. Annual payments of $5,000,000 or 2½% of total operating revenues, whichever is less, to a Capital Fund are expressly authorized before provision is made for interest payments to the income bondholder.

25 Thomas v. The New York and Greenwood Lake Ry. Co., 139 N.Y. 163 at 176-177, 34 N.E. 877 (1893).

equity does not have jurisdiction to order an accounting. Some courts will grant an accounting, however. One court so held when the trustee refused to enforce the indenture provision requiring the corporation to furnish an earnings statement.[26] Also, if a company has failed to keep separate accounts of the earnings of that part of the assets specifically described in the indenture, the income of which is pledged, an accounting has been ordered.[27] An accounting has also been granted simply on the theory that there is no other way to determine if there is income available for the bondholders.[28] Because a suit for breach of contract will fail where the bondholder cannot establish the existence of earnings,[29] such liberality in permitting an accounting is desirable. The indentures examined usually provide that the company will furnish to the trustee a detailed financial report.[30] Thus, the trustee and the income bondholders have all the information necessary to determine whether the company is paying interest when it is earned. In the absence of such a provision, the bondholders must face the difficulties inherent in procuring an equitable decree for an accounting.

The provisions regarding the cumulative feature of interest are important to the investor. Only six of the bonds examined are non-cumulative.[31] Nine are fully cumulative.[32] The remaining are cumulative, but cumulations are usually limited to three or four years' interest payments.[33] An interesting problem arises when the principal becomes due and there has not been sufficient net income to pay the accumulated interest. Two interpretations of the contract are possible. The cumulative feature might mean that the interest will accumulate and be paid in later

[26] Buel v. B. & O. Southwestern Ry. Co., 24 Misc. 646, 53 N.Y.S. 749 (1898). An important factor was the rather apparent collusion between the company and the trustee who represented the bondholders.

[27] Spies v. Chicago & E.I.R. Co., (S.D. N.Y. 1889) 40 F. 34. An accounting was granted even though the indenture stated that the board's determination of income was conclusive.

[28] Barry v. Missouri, K. & T. Ry. Co., (S.D. N.Y. 1886) 27 F. 1; Morse v. Bay State Gas Co., (C.C. Del. 1897) 91 F. 938. Cf. also Williams v. Green Bay & W.R. Co., 326 U.S. 549 (1946), holding that a dismissal of a suit brought by income bondholders for payment of interest on the ground that it interfered with the internal corporate affairs was improper.

[29] See Corcoran v. C. & O. Canal Co., 1 McArthur (8 D.C.) 358 (1874).

[30] See Appendix infra, e.g., Nos. 5, 7(c).

[31] See Appendix infra, Nos. 5, 7(c), 14(c), 18, 21(a), 21(b).

[32] See Appendix infra, Nos. 1, 2, 3, 6(a), 6(b), 10, 12, 13(a), 16.

[33] See Appendix infra, e.g., Nos. 4, 9.

years only if there are earnings in later years.[34] The other possible theory is that, whether or not there are earnings, the accumulated interest becomes a fixed debt at maturity and must be paid with the principal,[35] irrespective of whether earnings so permit. The cases do not give a uniform answer. Once again the draftsmen of the newer indentures have seen the problem and have given a specific answer, usually by making the interest payable upon maturity of the principal, whether or not there are earnings.[36] Interest on these same bonds, however, is cumulative only to a limited extent. This achieves a compromise position because, although the interest is not fully cumulative, to the extent that it is cumulative the investor knows that the company must pay it.

Some thought should be directed to the treatment given to preferred stockholders in determining the comparative advantages and disadvantages to the investor of an income bond in a similar company.[37] First, it is necessary to distinguish a preferred stock with a mandatory right to dividends, if there are earnings, from a preferred stock whose right is one of priority, dividends being payable on the preferred stock before any are paid on the common. Where the preferred merely has priority, the preferred stockholders are bound to abide by the board's decision as to whether dividends shall be paid, absent bad faith on the part of the board.[38] The income bond with a distant maturity date and the preferred stock with dividends that are mandatory, if earnings permit, are quite similar. Some writers draw minor distinctions even here,[39] but aside from the tax differences, such

[34] Such a result could be defended on the historical ground that the income bond was issued only in a time of financial difficulty. This type of obligation is issued to aid the reorganized company by avoiding a high fixed charge. Therefore, if the interest had to be paid on maturity of the principal, much of the benefit of the reorganization would be illusory because the problems due to the unsound capital structure would not be solved, but only postponed. Despite this argument, see note 36 infra to see how the cumulative interest is handled by the modern indenture.

[35] Barry v. Missouri, K. & T. Ry. Co., (S.D. N.Y. 1886) 27 F. 1 at 7; Sears v. Greater N.Y. Development Co., (1st Cir. 1931) 51 F. (2d) 46.

[36] For example, see the Chicago, Milwaukee, St. Paul & Pacific R. Co.'s General Mortgage 4½% Income Bonds, Series A, due 2019. The interest accumulates up to 13½% of the principal amount of the bond. It becomes due and payable when the principal is due and payable, or on default. The Erie Ry. Co.'s General Mortgage 4½% Income Bonds, Series A, due 2015 is similar.

[37] See Aikman, "Comparative Analysis of Income Bonds and Preferred Stock," 1 TEX. L. AND LEGIS. 175 (1947).

[38] 12 FLETCHER, CYC. CORP. 1957 Rev. Vol., §5443, p. 222, n. 49; 133 A.L.R. 653 (1941). See 8 A.L.R. (2d) 893 (1949).

[39] 1 DEWING, FINANCIAL POLICY OF CORPORATIONS, 5th ed., 235 (1953). Dewing says

distinctions do not appear to be of material significance.[40] The tax differences are clear; a letter written to the preferred shareholders of one corporation,[41] explaining why the management favored the proposed exchange of preferred stock for income bonds, stated that the investor would have about the same contractual rights and would be in a better economic position because deductibility of the interest for tax purposes would result in higher profits for the company.[42]

The income bond indentures provide the security holder with several rights on default. The right to force the company to pay interest is commonly stated in these terms: Failure to pay interest when due, continuing for ninety days after the due date and payable is a default.[43] Interest is due and payable semi-annually if there are earnings. If there is a default in making interest payments or in failing to meet any other of the company's obligations, the bondholders have a right to accelerate the principal.[44] The usual provision is that the trustee may accelerate and that the trustee must accelerate if the holders of a set percentage of the bonds so demand.[45] This provision is in accord with the Trust Indenture Act which requires that the trustee be given power to recover judgment in case of a default for the whole amount of principal and interest remaining unpaid.[46] A contingent voting right, given by two of the corporation indentures that were examined,[47] vests on default.

The income bondholder's rank on liquidation should be considered in connection with a default. Three of the indentures ex-

it is much more difficult to draft a preferred stock contract making dividends mandatory, which the courts will interpret as a definite contractual obligation to pay, than it is to draft an income bond indenture imposing a definite obligation.

40 Arizona Western Ins. Co. v. L. L. Constantin & Co., (3d Cir. 1957) 247 F. (2d) 388. See 42 YALE L. J. 989 at 992 (1933).

41 Chicago & Eastern Illinois R. Co. (1954).

42 The corporation's offer was accepted and the bonds are now outstanding. See Appendix infra, No. 5.

43 See Appendix infra, e.g., Nos. 7(a), 16.

44 Ibid.

45 See Appendix infra, e.g., Nos. 17, 19(a). The indenture requirement of a certain percentage, usually 20% to 25%, of the security holders' making a demand as a condition of accelerating has generally been enforced. Greene v. New York United Hotels, 236 App. Div. 647, 260 N.Y.S. 405 (1932), affd. 261 N.Y. 698, 185 N.E. 798 (1933). The condition may not be enforced when the trustee refused to act or acted in bad faith. Campbell v. Hudson & M.R. Co., 277 App. Div. 731, 102 N.Y.S. (2d) 878 (1951), affd. 302 N.Y. 902, 100 N.E. (2d) 183 (1951).

46 53 Stat. 1173 (1939), 15 U.S.C. (1952) §77qqq.

47 See Appendix infra, Nos. 6(a), 6(b).

amined subordinate the security holder to general creditors.[48] Sixteen companies, some with several different issues of income bonds,[49] gave a first or second mortgage to the bondholders.[50] Seven of the issues rank the bondholder on a par with general creditors on liquidation.[51] This rank on liquidation is probably not as important to the security holder in the companies whose indentures were examined, as are their rights in a reorganization. Here again, the rights of the income bondholder and the preferred stockholder[52] in two companies with otherwise the same capital structure and in the same financial position are very similar.[53] For a reorganization plan to be fair and equitable, the rights of the senior securities must receive full compensation before a junior security may participate in the reorganized company.[54] This absolute priority rule would protect the interest of the income bond that has accumulated.[55] The accumulated dividends on the preferred stock, however, would also be given priority on reorganization.[56] Thus, while the income bondholder, as a creditor of the company, is given the theoretical right to accelerate, a right that the preferred stockholder does not have, the possibility of a reorganization, when acceleration is necessary, reduces the significance of this distinction between the two.[57]

A preferred stockholder offered income bonds in exchange for his stock might wisely approve the exchange. With the variations already pointed out, the income bondholder will have about the

48 See Appendix infra, Nos. 1, 10, 12.

49 See Appendix infra, Nos. 6, 7, 13, 14, 19, 21.

50 See Appendix infra, e.g., Nos. 11, 17.

51 See Appendix infra, Nos. 5, 7(c), 9, 14(c), 15, 19(a), 22.

52 For simplicity, the assumption is made that the preferred stock is neither participating nor convertible. Different results would, of course, attach if the preferred had these features.

53 However, one important distinction between the two is that the income bondholder, unless subordinated, would at least share with general creditors and that the income bondholder, if secured by a mortgage, would have priority over the general creditors to the extent of the security. Another distinction is that if the preferred stock does have a voting right, it will be lost by the exchange for income bonds.

54 Northern Pacific Ry. Co. v. Boyd, 228 U.S. 482 (1913); Case v. Los Angeles Lumber Products Co., 308 U.S. 106 (1939). Dodd, "The Los Angeles Lumber Products Company Case and Its Implications," 53 HARV. L. REV. 713 (1940); 38 MICH. L. REV. 695 (1940).

55 Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific R. Co., 318 U.S. 523 (1943).

56 See Petition of Portland Electric Power Co., (9th Cir. 1947) 162 F. (2d) 618, cert. den. 332 U.S. 837 (1947).

57 1 DEWING, FINANCIAL POLICY OF CORPORATIONS, 5th ed., 234 (1953). See Frank, "Some Realistic Reflections on Some Aspects of Corporate Reorganization," 19 VA. L. REV. 541, 698 (1933).

same rights that he enjoyed as a preferred stockholder. The bondholder is more certain of a continuing income because of the fact that the payments to him are a charge before taxes, which increases the company profits through tax savings.

II. *Deductibility of Interest for Tax Purposes*

The hybrid nature of income bonds poses a difficult problem with respect to the deductibility of "interest" payments for income tax purposes. Since interest on indebtedness is deductible in computing taxable income,[58] and dividends, being merely a distribution of earnings to shareholders, are not, it is necessary to categorize a security as creating either a debtor-creditor relationship or one of company-shareholder.[59] The Internal Revenue Code is of little assistance in making this determination since it does not define indebtedness, and dividends are merely defined as distributions of property to shareholders.[60] Where there is an unconditional promise to pay interest coupled with a fixed maturity date, as in the case of the ordinary bond, there is no question but that the periodic payments are "interest" within the meaning of the code and thus deductible.[61] Because of their similarity to preferred stocks, however, the courts have considered income bonds to be a type of hybrid security which will not be classified as indebtedness unless the fact that interest payments are contingent on earnings is offset by other contractual provisions which are strong indicia of indebtedness.[62] Accordingly, opinions are generally in-

58 I.R.C., §163(a).

59 The status of a security is of prime concern to the holder as well because under the 1954 code a partial exclusion and credit is allowed for dividends received (I.R.C., §§34 and 116), whereas no such benefits accompany interest receipts. See Seidman, "What the Proposed Tax Credit on Dividends Means," 179 COMM. AND FIN. CHRON. 672 (1954). As far as the issuing corporation is concerned, a determination is necessary for purposes of the personal holding company surtax (I.R.C., §§541 and 545), and whether interest on deferred payments is deductible, for in Burton v. Bowers, (4th Cir. 1949) 172 F. (2d) 429, it was held that interest on cumulated payments acquires the same status for tax purposes as the payment itself.

60 I.R.C., §316.

61 Application of the "thin capitalization" doctrine may limit the deduction in the case of a closely-held corporation as explained in the text infra.

62 See Northern Refrigerator Line, Inc. v. Commissioner, 1 T.C. 824 at 828 (1943), where the court states: "The provision for a fixed dividend has been sometimes regarded as tending to establish the relationship as that of debtor and creditor, but where, as here, the interest is payable, not at all events, but only out of net earnings, or other funds 'available for dividends,' it is more indicative of a normal stockholding relationship." See also Crawford Drug Stores v. United States, (10th Cir. 1955) 220 F. (2d) 292. "The

troduced by declaring that the court will look through the form to the substance,[63] that the underlying intent of the parties is to govern,[64] and that each case must be decided on its own facts.[65] Unfortunately, such statements do little more than point out the problem with which the court is faced. Where income bonds are involved, the substance itself raises the problem, the bondholders do not stop to consider the technical nature of their relationship with the corporation, and it is indeed rare for a decision to rest on facts that do not appear in the case.

The courts generally agree on the main factors to be considered; however, since the significance to be accorded any particular factor varies widely and borderline cases are decided on the basis of marginal factors which other courts may consider immaterial,[66] the result has been a collection of irreconcilable decisions. In 1946 the Supreme Court reviewed the cases of *John Kelley Co. v. Commissioner* and *Talbot Mills v. Commissioner*[67] in what appeared to be an effort to settle the law. The indentures involved in these cases were substantially alike, except that interest in the *Talbot Mills* case was cumulative and in the *Kelley Co.* case it was not. The Tax Court held that payments on the cumulative issue were dividends[68] and those on the non-cumulative issue were interest.[69] On appeal to the circuit courts, the cumulative case was affirmed[70] and the non-cumulative case was

scheme to convert the preferred stock into debentures left the debentures resembling preferred stock rather than indebtedness. 'In the business world interest on indebtedness means compensation for the use or forbearance of money.' . . . The taxpayer 'hired' no money here. Its owners merely swapped papers and wound up in relatively the same position." Commissioners v. John Kelley Co., (7th Cir. 1944) 146 F. (2d) 466 at 468, revd. on other grounds 326 U.S. 521 (1946).

63 E.g., United States v. South Georgia Ry. Co., (5th Cir. 1939) 107 F. (2d) 3.

64 E.g., Bowersock Mills and Power Co. v. Commissioner, (10th Cir. 1949) 172 F. (2d) 904.

65 E.g., Commissioner v. John Kelley Co., (7th Cir. 1944) 146 F. (2d) 466, revd. 326 U.S. 521 (1946).

66 For example, in the case of Commissioner v. National Grange Mutual Liability Co., (1st Cir. 1935) 80 F. (2d) 316, the absence of voting rights was given much weight in the court's concluding that the relationship was one of debtor-creditor. In the case of Jordan Co. v. Allen, (M.D. Ga. 1949) 85 F. Supp. 437 at 443, however, which involved similar facts, the court held the security to be stock and stated: "The absence of voting and managerial rights or the presence of only extremely limited rights, however, is of little probative value, since it is common both to bonds and preferred stock."

67 326 U.S. 521 (1946), commented on in 44 MICH. L. REV. 827 (1946).

68 3 T.C. 95 (1944).

69 1 T.C. 457 (1943).

70 Talbot Mills v. Commissioner, (1st Cir. 1944) 146 F. (2d) 809, affd. 326 U.S. 521 (1946).

reversed.[71] Unfortunately, the Supreme Court, relying on *Dobson v. Commissioner*,[72] held that whether payments are interest or dividends is a question of fact to be determined finally by the Tax Court and not reviewable on appeal.[73] Consequently, the holding of the Tax Court in the non-cumulative case was reinstated. In effect, the Supreme Court's failure to resolve the conflict meant that the varying tests applied by the courts would continue.[74]

A review of the cases in which income-bond type securities have been classified for income tax purposes disclosed that the important considerations and their relative weights are the following.

Fixed Maturity Date. The vast majority of courts consider the absence of a fixed date on which security holders may demand repayment of their principal to negate indebtedness conclusively.[75] On the other hand, the existence of a maturity date, which is the general rule in the case of true income bonds, is considered by some courts to be decisive of indebtedness,[76] while most infer

[71] Commissioner v. John Kelley Co., (7th Cir. 1944) 146 F. (2d) 466, revd. 326 U.S. 521 (1946).

[72] 320 U.S. 489 (1943). The Dobson case interpreted I.R.C. (1939), §1141(a) to mean that only "clear-cut questions of law" are reviewable from the Tax Court. But see note 74 infra.

[73] Justice Rutledge, dissenting, argued that a question of law was presented because similar facts brought opposite results. He expressed his disappointment that the court would not establish a test to be applied by the Tax Court and thus bring them out of their "expert administrative fog."

[74] See 4 MERTENS, LAW OF FEDERAL INCOME TAXATION §26.10(c) (1954). Circuit court decisions are still good authority because the Tax Court continues to cite them, and many circuit courts no longer feel bound by the Dobson case, note 72 supra, because I.R.C. (1939), §1141(a) was amended in 1948 by I.R.C., §7482(a) which provides for more liberal review. See Rice, "Law, Fact, and Taxes: Review of Tax Court Decisions Under Section 1141 of the Internal Revenue Code," 51 COL. L. REV. 439 (1951).

[75] "All we now decide is that in the absence of such a provision the security cannot be a debt." Jewel Tea Co. v. United States, (2d Cir. 1937) 90 F. (2d) 451 at 453; United States v. South Georgia Ry. Co., (5th Cir. 1939) 107 F. (2d) 3. See Swoby Corp. v. Commissioner, 9 T.C. 887 (1947). The only exception of any significance is Commissioner v. National Grange Mutual Liability Co., (1st Cir. 1935) 80 F. (2d) 316, which involved a corporation which was precluded by its charter from issuing securities that would mature. Another extreme case often cited is Helvering v. Richmond, F. & P. R. Co., (4th Cir. 1937) 90 F. (2d) 971, in which payments were held to be interest even though there was no maturity date; however, interest was a fixed obligation, not contingent on earnings, and the case is generally distinguished on that basis.

[76] "The fact that ultimately he must be paid a definite sum at a fixed time marks his relationship to the corporation as that of creditor rather than shareholder. The final criterion between creditor and shareholder we believe to be the contingency of payment." Commissioner v. O.P.P. Holding Corp., (2d Cir. 1935) 76 F. (2d) 11 at 12; Commissioner v. H.P. Hood & Sons, Inc., (1st Cir. 1944) 141 F. (2d) 467; Washmont Corp. v. Hendrickson,

it is merely strong evidence of indebtedness which may be offset by other factors evidencing a shareholder's relationship.[77] An interesting problem is presented where repayment of principal is guaranteed by a third party rather than the issuing corporation. A circuit court has held that such a security is to be considered as having a fixed maturity date,[78] while previously the Tax Court held to the contrary.[79]

Rank on Liquidation. Some courts consider subordination to the claims of general creditors on liquidation to be highly indicative of a shareholder's relationship,[80] while most consider it merely another factor evidencing stock but far from conclusive.[81] In general, the courts seem to stress subordination most strongly when it is coupled with the absence of a maturity date.[82] That a security has a fixed maturity date, however, seems to outweigh any significance subordination would ordinarily be accorded.[83]

(9th Cir. 1943) 137 F. (2d) 306. In John Kelley Co. v. Commissioner, 1 T.C. 457 (1943), affd. 326 U.S. 521 (1946), the payments were held to be interest even though unearned interest was not cumulative and rights on liquidation were subordinated to the claims of general creditors.

77 Crawford Drug Stores v. United States, (10th Cir. 1955) 220 F. (2d) 292; Talbot Mills v. Commissioner, (1st Cir. 1944) 149 F. (2d) 809, affd. 326 U.S. 521 (1946); Fidelity Savings and Loan Assn. v. Burnet, (D.C. Cir. 1933) 65 F. (2d) 477. In these cases the courts held the payments were dividends although the indentures provided for a fixed maturity date. The Talbot Mills case was decided by the same court that decided the Hood case, note 76 supra, leaving the status of a maturity date in the First Circuit unclear. See Jordan Co. v. Allen, (M.D. Ga. 1949) 85 F. Supp. 437. It should be added that there is some authority to the effect that a compulsory redemption provision is not synonymous with a provision for maturity. See Haffenreffer Brewing Co. v. Commissioner, (1st Cir. 1940) 116 F. (2d) 465 at 469; Kentucky River Coal Corp. v. Lucas, (W.D. Ky. 1931) 51 F. (2d) 586 at 588, affd. (6th Cir. 1932) 63 F. (2d) 1007. In the case of United States v. Title Guarantee & Trust Co., (6th Cir. 1943) 133 F. (2d) 990, however, the Sixth Circuit seems to have reversed its position. In the Haffenreffer case the court argued that such redemption is merely the retirement of the obligation to retire rather than retirement of the debt itself. This distinction is certainly of dubious validity and seems to violate the principle that substance rather than form is to govern.

78 Bowersock Mills and Power Co. v. Commissioner, (10th Cir. 1949) 172 F. (2d) 904.

79 Northern Refrigerator Line, Inc. v. Commissioner, 1 T.C. 824 (1943).

80 See, e.g., Dayton and Michigan R. Co. v. Commissioner, (4th Cir. 1940) 112 F. (2d) 627 at 629; Crawford Drug Stores v. United States, (10th Cir. 1955) 220 F. (2d) 292; Jordan Co. v. Allen, (M.D. Ga. 1949) 85 F. Supp. 437.

81 See, e.g., Bowersock Mills and Power Co. v. Commissioner, (10th Cir. 1949) 172 F. (2d) 904; Commissioner v. H.P. Hood & Sons, Inc., (1st Cir. 1944) 141 F. (2d) 467; Washmont Corp. v. Hendrickson, (9th Cir. 1943) 137 F. (2d) 306.

82 For example, of the three leading cases cited in note 80, only the security in the Crawford case had a maturity date.

83 For example, all the securities involved in the leading cases which appear at note 81 had maturity dates. In the case of Talbot Mills v. Commissioner, (1st Cir. 1944) 146 F. (2d) 809, affd. 326 U.S. 521 (1946), the payments were held to be dividends although there was a fixed maturity date; but in deciding the case, the court emphasized factors other than subordination.

The result is that in few cases can it be said that subordination to the claims of general creditors was the determining factor.

Cumulation of Payments. Whether or not periodic payments are cumulative was not considered a significant factor until 1944 when the Seventh Circuit stated, "A consideration of cases in the Circuit Courts of Appeals and the District Courts discloses none where noncumulative payments, payable out of earnings only, have been held to be interest."[84] Although the statement quoted was true, it is quite misleading because the cases in which payments were non-cumulative involved securities that did not have a fixed maturity date or did not provide for equal rights with creditors on liquidation, and it was these factors that the courts stressed in deciding those cases.[85] On the other hand, if unearned interest is fully cumulative and payable at maturity regardless of earnings, this should offset any weight the court would ordinarily give to the fact that interest payments are contingent on earnings. In effect, the security would approach the well-recognized type of bond, similar to the government series "E" savings bond, on which interest is payable only at maturity. A few courts have recognized this fact,[86] while most have not, considering the lack of absolute periodic payments to evidence a shareholder's relationship although the stated return must eventually be paid in full.[87] Where interest is non-cumulative or, if cumulative, is payable at maturity only if earnings are adequate, the contingency of payment feature retains its effect of indicating a shareholder's relationship.[88] No judicial decisions were found in which interest was cumulative only to a limited extent, as on most of the bonds examined;[89] however, it seems reasonable to assume that

[84] Commissioner v. John Kelley Co., (7th Cir. 1944) 146 F. (2d) 466 at 468.

[85] E.g., Dayton and Michigan R. Co. v. Commissioner, (4th Cir. 1940) 112 F. (2d) 627; Kentucky River Coal Corp. v. Lucas, (W.D. Ky. 1931) 51 F. (2d) 586.

[86] "Since a debenture could very well call for no current annual payment of interest at all and provide that cumulative annual interest be paid only at maturity, the additional feature that interest be paid annually to the extent of the available net earnings does not prevent the instrument from being a debenture." Commissioner v. H.P. Hood & Sons, Inc., (1st Cir. 1944) 141 F. (2d) 467 at 470. See Washmont Corp. v. Hendrickson, (9th Cir. 1943) 137 F. (2d) 306 at 308; Sabine Royalty Corp. v. Commissioner, 17 T.C. 1071 at 1077 (1951).

[87] See, e.g., Crawford Drug Stores v. United States, (10th Cir. 1955) 220 F. (2d) 292; Burton v. Bowers, (4th Cir. 1949) 172 F. (2d) 429; Fidelity Savings and Loan Assn. v. Burnet, (D.C. Cir. 1933) 65 F. (2d) 477.

[88] E.g., Dayton and Michigan R. Co. v. Commissioner, (4th Cir. 1940) 112 F. (2d) 627; Commissioner v. Schmoll Fils Associated, (2d Cir. 1940) 110 F. (2d) 611.

[89] See note 36 supra and preceding text.

in such case the courts would treat the security as if interest was not cumulative at all.

Issuance in Exchange for Stock. Since many income bonds have been issued in exchange for preferred stock, the question has arisen whether an indebtedness can be created where no new funds are received. Again, the courts are not in accord. Some decisions contain language to the effect that the "hiring" of money is the essence of indebtedness and thus essential to its creation.[90] Most courts, however, take the position that indebtedness is merely an obligation to pay a fixed sum on a fixed date and the nature of the transaction giving rise to the obligation is immaterial.[91] Where the recipients of the bonds retain their proportionate ownership interests, as is often the case where a closely-held corporation is involved, an additional problem arises as to whether the bonds are but a dividend in disguise.[92]

Intent to Avoid Taxes. Closely allied to the problem of exchanged securities is the question of tax avoidance. Both issues are generally raised concurrently because an obvious purpose in exchanging income bonds for preferred stock is to avoid taxes by gaining an interest deduction. Where it appears that the sole purpose of the exchange is to avoid taxes, there are cases which seem to apply the so-called "business purpose" doctrine and thereby disallow the deduction.[93] On the other hand, most courts hold that the purpose of the exchange is immaterial; the only question being, has a bona fide indebtedness been created?[94]

90 "Interest, within the meaning of Section 23(b), has been defined as 'the amount which one has contracted to pay for the use of borrowed money.' . . . These notes were not issued for borrowed money. They represent no new contribution to capital. They were exchanged for outstanding preferred stock which had been issued as a stock dividend to the common stockholders." Wetterau Grocer Co. v. Commissioner, (8th Cir. 1950) 179 F. (2d) 158 at 160. See quotation from Commissioner v. John Kelley Co., note 62 supra.

91 "We think, however, that the very pattern of the tax statute recognizes that indebtedness may be created by a distribution or by a recapitalization exchange through the issuance of securities out of capital or earnings or both. . . ." Kraft Foods Co. v. Commissioner, (2d Cir. 1956) 232 F. (2d) 118 at 126, noted in 55 MICH. L. REV. 457 (1957) (interest was a fixed obligation). See Commissioner v. H.P. Hood & Sons, Inc., (1st Cir. 1944) 141 F. (2d) 467; Sabine Royalty Corp. v. Commissioner, 17 T.C. 1071 (1951).

92 See I.R.C., §302.

93 In the case of Talbot Mills v. Commissioner, (1st Cir. 1944) 146 F. (2d) 809, affd. 326 U.S. 521 (1946), the security had a fixed maturity date and "interest" was cumulative. Nevertheless, the court held the payments to be dividends stating (at 811), "The taxpayer admits that tax avoidance was an important factor in this exchange, and the Tax Court found that it was 'the only substantial purpose motivating the transaction.'" See Wetterau Grocer Co. v. Commissioner, (8th Cir. 1950) 179 F. (2d) 158.

94 "The inquiry is not what the purpose of the taxpayer is, but whether what is

Apparently both the problems of exchanged securities and tax avoidance assume significance primarily where the bonds are issued to the shareholders of a closely-held corporation, with the courts entertaining some doubt as to whether an indebtedness was ever intended.[95]

Miscellaneous Considerations. Where the court is faced with a borderline situation, it is not unusual for it to resort to marginal consideration such as nomenclature in the indenture and managerial rights. At best, such factors are considered as make-weights and do not warrant analysis in this comment.[96]

Where a corporation issues income bonds which meet the requirements of an indebtedness, there is still the possibility that the interest deduction will not be allowed in full because of the "thin capitalization" doctrine.[97] If long-term debt constitutes an unusually large part of the corporation's capitalization, under this doctrine only the interest on a reasonable amount is deductible. This judge-made limitation on indebtedness, applicable only to closely-held corporations, would seem to apply regardless of the nature of the debt. Where income bonds are involved, however, a larger proportion of indebtedness than would ordinarily be considered reasonable would be justified because there is no

claimed to be, is in fact." Kraft Foods Co. v. Commissioner, (2d Cir. 1956) 232 F. (2d) 118 at 128. See Commissioner v. H.P. Hood & Sons, Inc., (1st Cir. 1944) 141 F. (2d) 467. Although the Tax Court implies that if the sole purpose of the exchange is to avoid taxes a deduction will not be allowed, the court has so readily found a concurrent business purpose that its position seems rather to be that tax avoidance is not a significant factor, but is, at best, a make-weight. See, e.g., Sabine Royalty Corp. v. Commissioner, 17 T.C. 1071 (1951); New England Lime Co. v. Commissioner, 13 T.C. 799 (1949); John Kelley Co. v. Commissioner, 1 T.C. 457 (1943), affd. 326 U.S. 521 (1946). The Tax Court is quite critical of closely-held corporations, however, and has considered the absence of a strong business purpose to show that the parties did not intend an indebtedness. See Gooding Amusement Co. v. Commissioner, 23 T.C. 408 (1954), affd. (6th Cir. 1956) 236 F. (2d) 159.

95 For example, compare Talbot Mills v. Commissioner, (1st Cir. 1944) 146 F. (2d) 809, affd. 326 U.S. 521 (1946), with Commissioner v. H.P. Hood & Sons, Inc., (1st Cir. 1944) 141 F. (2d) 467. These cases are indistinguishable on their facts and both were decided by the First Circuit. The Hood company stock was widely held, and all the stock of the Talbot Mills company was owned by one family. A deduction was allowed in the Hood case, the court stressing that tax avoidance was not to be considered. In the Talbot Mills case the court disallowed the deduction stating (at 812), "We have been referred to no case holding that the court could not look to 'the actualities of the situation' in determining whether corporate distributions were in fact true dividends or interest on indebtedness." Compare also New England Lime Co. v. Commissioner, 13 T.C. 799 (1949), with Gooding Amusement Co. v. Commissioner, 23 T.C. 408 (1954).

96 For a review of these factors see 4 MERTENS, LAW OF FEDERAL INCOME TAXATION §26.10 et seq. (1954).

97 For an excellent treatise on this doctrine see LORE, THIN CAPITALIZATION (1958). See also 55 COL. L. REV. 1054 (1955).

danger of acceleration or other repercussions if earnings are insufficient to pay interest.

An inspection of the income bonds listed on the New York Stock Exchange, in terms of the law as it now stands, shows that the great majority of these bonds pass the more significant tests as applied by the courts. All the bonds have fixed maturity dates and all but three[98] give the holders the right to share at least equally with general creditors on liquidation. Those bonds that subordinate holders to general creditors provide that interest is fully cumulative, however, and such a provision should temper somewhat the adverse effect of subordination. Many of the bonds were issued in exchange for preferred stock[99] and all but two[100] were issued in a transaction that did not result in the corporation receiving new funds. Also, the great majority of these bonds are only partially cumulative, a limitation of three times the yearly rate being typical.[101] As mentioned above, however, language to the effect that these factors weigh heavily against indebtedness is generally confined to cases involving closely-held corporations, the court having cause to question whether an indebtedness was actually intended. Since these bonds were issued at arms-length, such factors would probably be of little or no significance. Accordingly, only the three bonds which were exchanged for preferred stock and, in addition, are subordinated to general creditors on liquidation would seem to have a somewhat questionable status.[102]

If the law is to permit deductibility of interest payments on any income bonds, the need for clarification in this area is obvious. The reluctance of the Commissioner to lay down explicit standards in his regulations or rulings and to mark a safe and certain path to tax avoidance thereby, is understandable. Many income bonds, however, do achieve tax deductions, and for this result to depend upon the circuit in which the corporation is located or the forum which hears the case is equally undesirable. If preservation of the revenue is considered important enough to warrant fostering confusion and uncertainty, the problem would seem to merit congressional treatment, closing off this possible

98 See Appendix infra, Nos. 1, 10, 12.
99 See Appendix infra, e.g., Nos. 5, 7(c).
100 See Appendix infra, Nos. 3, 18.
101 See Appendix infra, e.g., Nos. 4, 9.
102 See note 98 supra.

avenue of tax advantage for all income bonds. In the absence of such legislation, the Commissioner should establish a well-defined test to determine whether the requirement of an indebtedness has been met.

In formulating any such test, a distinction should be made between arms-length transactions and those that involve closely-held corporations. Where the securities are issued at arms-length, the decisive factor should be whether or not there is a fixed date on which the security holders may enforce repayment of their principal. This is perhaps the only consistent difference between bonds and preferred stocks, and authorities in the field of finance generally agree that a provision for maturity is the feature that distinguishes bonds from stocks.[103] Such a maturity date should appear reasonably certain to arrive prior to the time when liquidation may be expected, and, in any case, there should be a maximum term allowed which would approximate the maximum term customary for ordinary bonds issued by corporations in the same or similar business and, if determinable, in similar circumstances. The requirement that the bond be expected to mature prior to liquidation would insure against maturity dates that have no significance.[104] Of course, this limitation would not be applicable to corporations which have no foreseeable demise. The general limitation, comparing the duration of income bonds with that of ordinary bonds, would preclude abnormally distant maturities, but not interfere with general corporate practice.[105] Such requirements alone should be conclusive of indebtedness, since other provisions in the indenture are only incidental to 'be debtor-creditor

103 See 1 DEWING, FINANCIAL POLICY OF CORPORATIONS, 5th ed., 176 (1953): ". . . The first of these is the direct statement that the bond is a promise to pay a certain sum of money. This statement, more than any other, distinguishes the bond from the share of stock and indicates clearly that the bondholder is a creditor and not a partner in the corporate enterprise. It is a categorical statement. It represents the contractual obligation on the part of the corporation; and all other clauses, stipulations, and provisions of the bond itself and of the supplementary agreement are merely addenda to this primary and original obligation." See also 2 JONES, BONDS AND BOND SECURITIES, 4th ed., §601 (1935), and cases cited.

104 See Jordan Co. v. Allen, (M.D. Ga. 1949) 85 F. Supp. 437 at 445.

105 In John Kelley Co. v. Commissioner, 326 U.S. 521 at 526 (1946), the Supreme Court states that there must be "a definite maturity date in the reasonable future." See Swoby Corp. v. Commissioner, 9 T.C. 887 at 894 (1947), where the Tax Court considered a 99-year obligation to be unreasonable. The proposed test for a valid maturity provision would be more definite than the "reasonableness" test as now applied by the courts, while allowing variations in conformity with accepted business practice.

relationship and do not change its nature. For example, a creditor may choose to relinquish his usual rights on liquidation or accept a non-cumulative contingent return in exchange for a higher rate of interest than would be paid had these concessions not been made. Regardless of the agreement between the parties as to the terms of compensation and rights on liquidation, their basic relationship of debtor-creditor remains unchanged. Also, the fact that bonds are exchanged for preferred stock upon consultation with the Internal Revenue Code should be of no consequence. The question is, has an indebtedness been created, not why was it created, and the contention that the only way an indebtedness can arise is by the receipt of new funds is certainly without merit.

Where a closely-held corporation is involved, and the bonds are issued to its stockholders, the requirements should be somewhat more stringent because of the possibility of an underlying agreement that the principal will not be demanded although such right may appear on the face of the indenture. Consequently, it may be necessary to require such an additional safeguard as periodic payments into a sinking fund held by a disinterested third party for the retirement of the income bonds at maturity. Serial retirements would be an acceptable alternative, an equal number of bonds being retired over the duration of the issue.

III. *Conclusion*

The striking aspect of this study of income bonds is the dichotomy of result between sections I and II of this comment. On the one hand, an economic and historical evaluation reveals that for practical purposes income bonds are the equivalents of preferred stock. The investor holding income bonds rather than preferred stock has almost an identical investment with perhaps certain additional safeguards and advantages over the normal preferred stockholder. On the other hand, the tax treatment afforded these two transactions recognizes a substantial difference between preferred stock and the carefully drawn income bond. If taxpayers and tax lawyers in substantial numbers take advantage of this dichotomy in the future, Congress will no doubt act to destroy this difference. Until such time, this difference would seem to merit careful attention.

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APPENDIX

1. Armour and Co. (Ill.), 5% Cum. Inc. Sub. Debs., due 1984.
2. Baltimore and Ohio R. Co., Conv. 4½% Inc. Bonds, due 2010.
3. Boston and Maine R. Co., 4½% Inc. Mtge. Bonds, Series A, due 1970.
4. Chicago and Great Western Ry. Co., 4½% Gen. Inc. Mtge. Bonds, due 2038.
5. Chicago and Eastern Illinois R. Co., 5% Inc. Debs., due 2054.
6. Chicago, Indianapolis, and Louisville Ry. Co.:
   (a) First Mtge. 4% Inc. Bonds, Series A, due 1983.
   (b) Second Mtge. 4½% Inc. Bonds, Series A, due 2003.
7. Chicago, Milwaukee, St. Paul, and Pacific R. Co.:
   (a) Gen. Mtge. 4½% Inc. Bonds, Series A, due 2019.
   (b) Gen. Mtge. 4½% Conv. Inc. Bonds, Series B, due 2044.
   (c) 5% Inc. Debs., Series A, due 2055.
8. Chicago and Northwestern Ry. Co., Second Mtge. 4½% Conv. Inc. Bonds, Series A, due 1999.
9. Chicago, Rock Island, and Pacific R. Co., 40-year 4½% Inc. Debs., due 1995.
10. Curtis Publishing Co., 30-year 6% Sub. Inc. Debs., Series of 1956, due 1986.
11. Erie R. Co., Gen. Mtge. 4½% Inc. Bonds, Series A, due 2015.
12. Minneapolis-Moline Co., 6% Sub. S.F. Inc. Debs., due 1986.
13. Minneapolis, St. Paul, and Sault Ste. Marie R. Co.:
   (a) First Mtge. 4½% Cum. Inc. Bonds, Series A, due 1971.
   (b) Gen. Mtge. 4% Inc. Bonds, Series A, due 1991.
14. Missouri Pacific R. Co.:
   (a) Gen. Mtge. 4¾% Inc. Bonds, Series A, due 2020.
   (b) Gen. Mtge. 4¾% Inc. Bonds, Series B, due 2030.
   (c) 5% Inc. Debs., due 2045.
15. New York, Chicago, and St. Louis R. Co., 35-year 4½% Inc. Debs., due 1989.
16. New York, New Haven, and Hartford R. Co., Gen. Mtge. Inc. Bonds, 4½%, Series A, due 2022.
17. New York, Susquehanna, and Western R. Co., Series A, Gen. Mtge. 4½% Inc. Bonds, due 2019.
18. Peoria and Eastern Ry. Co., Inc. Mtge. 4% Noncum. Bonds, due 1990.
19. St. Louis-San Francisco Ry. Co:
   (a) 50-year Inc. 5% Debs., Series A, due 2006.
   (b) Second Mtge. Inc. 4½% Bonds, Series A, due 2022.
20. Spokane International R. Co., Inc. Mtge. 4½% Bonds, Series A, due 2013.
21. Wabash R. Co.:
   (a) Gen. 4% Inc. Bonds, Series A, due 1981.
   (b) Gen. 4¼% Inc. Bonds, Series B, due 1991.
22. Western Pacific R. Co., 30-year 5% Inc. Debs., due 1984.
23. Wisconsin Central R. Co., Gen. Mtge. 4½% Inc. Bonds, Series A, due 2029.