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CALEDONIAN RAILWAY.

THIRD PAMPHLET

BY

A PUBLIC ACCOUNTANT.

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CALEDONIAN RAILWAY.

The Report of the Committee which took upon itself the onerous charge of investigating the affairs of the Caledonian Railway Company, and the Supplementary Reports of the professional gentlemen who so ably assisted them in their inquiry, are now before the public. We have, also, been favoured with a reply in the shape of observations on the Report of the Committee from the Directors and Auditors of the Company, but these observations have already been so entirely set aside by a further statement from the Committee's Accountants, that I think they may be held as of no moment. Taken together the Report of the Committee and these accounts contain reliable data, from which an approximately correct estimate may be formed of the present financial position and future prospects of that unfortunate undertaking. At the same time they form a sad but instructive chapter in railway history. Apart from the question of the justification of the serious charges which I felt compelled to bring against the

Directors of the Caledonian Railway, I cannot but regret to find that my worst predictions are more than realized. It is a regrettable fact that Railway Boards, with all their supposed collective wisdom, are as little amenable to the lessons of experience as solitary individuals are said to be. Seventeen years ago the Caledonian Railway Company had to seek the intervention of Parliament to avert impending ruin. By the Arrangement Act, 1851, it was relieved from the pressure of the heavy burdens under which it had well nigh succumbed; its finances were subsequently gradually restored to a healthy state; its traffic was rapidly developed, and nothing but prudent management was required to enable the Caledonian Railway Company to enter on a career of lasting prosperity—unfortunately this indispensable condition was wanting. The Directors were men of ambitious views and combative disposition; and instead of devoting their sole energies to work well and profitably the valuable ground they already occupied, they looked with covetous eyes on that of their neighbours. They entered into ruinous competition with the Edinburgh and Glasgow Railway Company, and urged a desperate, protracted, and costly war against the North British Company, for possession of the barren district between Hawick and Carlisle. Defeated in their attempt to stay the progress of that Company southwards, they changed the battle-field to the north, and by acquiring the Scottish Central and Scottish North Eastern Railways on terms ruinously exorbitant, obtained, as they supposed, the control of the whole of the traffic of the north of Scotland. They succeeded for a while in their object of crippling the North British, but it was a victory more fatal than defeat, for now, like some of the doughty warriors of old, they have ingloriously fallen, crushed beneath the weight of their own armour, and are *compelled to accept peace, and surrender a portion of the advantages so dearly purchased*, by entering into a joint purse arrangement with the very enemy against whom, at an immense cost, they have battled for years! A more disastrous policy, or one more directly opposed to the teachings of experience, was never pursued by any Railway Board.

With these few prefatory remarks I will proceed to the consideration of the Report of the Committee of Investigation.

The first thing that occurs to me in reference to that important document is, that the Committee do not produce any credentials. There is nothing in the Report to show by whom or under what circumstances they were appointed. This is a serious omission. In order to command the confidence of the public, and to carry due weight with the parties immediately interested in the results, it is essential that any committee conducting an inquiry of such high importance, shall be appointed by the Shareholders at general or special meeting assembled, and that the objects and scope of the investigation shall be clearly defined. In the absence of any regular appointment and instructions from a meeting of Shareholders, it is scarcely a matter for surprise, that the Caledonian Committee should have shrunk from the labour and responsibility of a fearless, thorough, and searching investigation, and restricted their inquiries (for reasons which appear to be wholly inadequate) to the two years ending on the 31st July, 1867. The same feeling of hesitation may have operated to prevent them from giving instructions for an accurate valuation of the rolling stock, so as to show the extent of its depreciation, and the extent to which revenue had thus been relieved of its proper charges, and from accepting, in their entirety, the conclusions arrived at by the accountants whom they appointed to assist them in their inquiry.

The result is, the production of a Report which alarms us even more by what it suggests, or fails to disclose, than by the startling facts which it reveals. For the convenience of those who may be unable or unwilling to wade through a mass of figures and other matter, not so logically arranged as one could wish, I will state as concisely as I can the facts proved in the Committee's Report, showing how far they substantiate the charges made by me against the Directors of the Caledonian Railway, and the natural inferences to be drawn from the facts as to the present actual position and future prospects of the Company.

The first count against the Caledonian Directors was that of incurring Preferential obligations out of all due proportion to the amount of the unguaranteed Capital, and purchasing or leasing other undertakings on terms unfavourable to the Caledonian Shareholders. The truth of this allegation is amply confirmed by the Committee; it is shown in their Report that the working of the Port Patrick Railway has already resulted in a dead loss of £46,889, after giving credit for all the traffic brought by that undertaking over the Caledonian system. It is further stated that this loss is but "*trifling as compared with what may yet result*, from the competing lines which have been called into existence" by the "uncalled-for invasion of the territory of a friendly Company." The agreement which entails this heavy loss unfortunately has still eighteen years to run.

With respect to those costly acquisitions, the Scottish Central and Scottish North Eastern Lines, no separate accounts have been kept, and the Committee are unable for that reason to give the results of the working since these lines came into the possession of the Caledonian Company, but they state "we very much doubt if either can have been beneficial to the Caledonian proper. *The Scottish North Eastern, has, we have no doubt, entailed a heavy loss, and is another fruit of reckless competition.*"

From the foregoing facts it will appear that the practical effect of the recent amalgamations, leases, and working agreements entered into by the Directors of the Caledonian Railway has not been to conserve the interests of the Company, but to lay upon it a heavy burden of annual deficiencies, which for years to come, will, irrespective of other causes operating towards the same end, seriously depress the present undertaking and greatly diminish, if not entirely extinguish, the dividends on its original Stock.

The next charge preferred against the Caledonian Board was, that while debiting Capital with loss on shares in other lines, they credited Contingent Revenue account with the premiums realized on the issue of new shares. As to the fact there is no dispute, and the accountants show in their Report that the amount received for share premiums was £283,251, of which the large sum of £186,026 has been applied to the payment of Revenue charges and Dividends.

These gentlemen very properly observe in their Report—"We have not recognized the Premium account as a source from which amounts can be taken for the purpose of supplementing net Revenue, as in our judgment Dividends can only properly be paid from ordinary income." The Committee of Investigation do not attempt to controvert the principle thus laid down, but, instead of acting upon it, and urging the restitution by Revenue of the sums thus improperly diverted from Capital, they doubtless, with the best intentions, and with the amiable desire to make things as little unpleasant as possible, recommend that the sums be allowed to remain at the credit of Revenue—a most lame and impotent conclusion!

It will be interesting and instructive to refer for a moment to the peculiar circumstances under which a large proportion of the Premiums on Shares was obtained. For the half-year ending 31st July, 1865, a dividend at the rate of $6\frac{3}{4}$ per cent. was declared on the Caledonian Ordinary Stock, and the holders received in addition a bonus of 1 per cent., making it apparently a very valuable property. At this opportune moment, when Shareholders were congratulating themselves on the bright prospects before them, and rejoicing over the positive assurance of the Chairman that the dividend would certainly be maintained at 7 per cent. as a minimum, the Directors issued £990,000 Ordinary Stock, authorized to be raised by the Cleland and Mid-Calder, and other Acts.

In consequence of the high dividend and bonus on the existing Ordinary Stock, the new issue was eagerly taken up, and realized the handsome premium of £186,809; but it now appears from the report of the accountants, that the dividend declared could not have been earned, and that the bonus of 1 per cent. was, in point of fact, paid out of former premiums, which, as I have shown, ought to have been placed to the credit of Capital. Had the true state of the Company's affairs been known at the time, it is certain that no premiums on the new shares would have been obtained.

On "severe, but just principles," then, these high premiums, having been given on the faith of the assurance that the Caledonian was a 7 or 8 per cent. line, ought to be returned to the persons who paid them. The conduct of the Directors in reference to this transaction is indefensible, and deserves to be visited with the severest censure.

The third charge brought againt the Directors was that the cost of reconstructing bridges, which had formerly been charged (and properly so) to Revenue, had recently been debited to Capital, and that the charges to Capital for new works at stations, sidings, &c., was out of all reasonable proportion to the sums charged against Revenue in respect of the old lines and works. This allegation is fully proved by the Report of the Committee. In the course of the two years to which the accountants were unfortunately instructed by the Committee to limit their inquiries, the sum of £44,882 was found to have been improperly charged to Capital account for re-construction of bridges. Then a charge of £15,900 extra cost of renewing a portion of the Scottish North Eastern Railway has been wrongly charged in like manner. Again a sum of £7837, difference between the cost of steel and iron rails, which had been debited to Revenue up to the year 1865, was in 1867 taken from the Revenue account and charged to Capital. By these three items of expenditure alone, revenue has been improperly relieved to the extent of £68,906.

The Committee also indicates, *but does not estimate items improperly charged to Capital* for reconstruction of stations, sheds, sidings, &c.

So far the Committee, the accountants, and I may add myself, are in accord, but now arises a dissidence of opinion on a point of vital importance, which involves the question of further heavy charges against Revenue on account of permanent way. The accountants recommend that the cost of fish-plating a portion of the rails, and the extra cost of steel rails used in substitution for iron should be charged against Revenue. The Committee, on the other hand, departing from the "severe but juster principles," to which they make such pointed reference, recommend that these items should be charged to Capital account. I will state briefly why I consider the accountants to be right, and the Committee wrong on this question.

In the first place, the majority of the items were from 1861 to 1866 charged to Revenue, a clear proof that during this period the Directors considered them to be a proper Revenue charge. But, in 1867, finding it impossible to maintain the dividends at their previous figure, they decided to transfer these items to Capital, and thus ease Revenue for the time being. This extraordinary proceeding the auditors allowed. This is a crab-like policy, progessing backwards. If these items were a proper charge against Revenue in 1861, they were still more emphatically a proper charge against it in 1867, when public opinion had pronounced in favour of keeping charges to Capital within the narrowest possible limits, and widening the door to Revenue charges.

The auditors, I see, in their observations on the Report of the Committee of Inquiry, object to the "displacement of amounts." That objection would have had much greater weight had they declined to sanction the displacement of the charges from Revenue in order to carry them to Capital.

In the second place it is the practice of other large Railway Companies to charge the whole cost of reconstruction of bridges and many other improvements, and the whole, or the extra cost of steel rails used for renewals, to Revenue. From the proceedings at the half-yearly meetings of the London and North Western, North London, Midland, and North Eastern Railway Companies, held in the month of September last, I extract the following information.

London and North Western.—Mr. Moon, the Chairman, stated: "We have done certain things which practically form for us a sinking fund. For instance, we have renewed our wooden bridges, with stone and iron, having probably in the course of five years spent in that way £50,000. We have in six years spent £150,000 in replacing stations and in additional works, at the expense of Revenue. We have remade the St. Helen's canal, at a cost of £23,000, and we have renewed in a very few years the Chester and Holyhead, and the Carlisle and St. Helen's lines. We have in this way taken out of Revenue such very large sums that the whole of the property is improved as well as maintained. During the half-year we have set aside the sums that we have been in the habit of placing to the debit of revenue, though it might fairly have been argued that in an exceptional period we might have made an exceptional case of it. But we thought that this concern must not be so dealt with at exceptional periods; that it was better to let the period go by and continue, as heretofore, carrying all that we thought was necessary to the debit of Revenue. We have, therefore, nothing behind us. Our accounts are as true and straightforward as it is possible to make accounts . . . . . . The extra cost of steel rails has been put to Revenue account as against what would have been the cost of iron rails, to the extent of £14,800."

North London Railway. The Chairman stated that "The working expenses for maintenance of way and works and stations show an increase, attributable in part to a large amount of fence walling substituted for post and rail fencing . . . . . The permanent way and works have been efficiently kept up, and with the exception of about two miles, which will be renewed in the current half-year, the entire line has been re-laid with steel rails."

Midland Railway.—The Chairman observed that "The revenue of the half-year was charged with £10,000, cost of reconstruction of bridges at Tamworth, and also with residue of payments for the Appleby viaduct, and other works damaged by the floods last year."

North Eastern Railway.—Mr. H. S. Thompson, the Chairman, stated that, "The charges under the head of maintenance of way and works would have been less had it not been for a considerable outlay in rebuilding bridges, and in having substituted iron and brick for timber ones."

It will be seen at a glance that the practice of these companies is diametrically opposed to the principles laid down by the Caledonian Auditors, as to the allocation of expenditure to Capital and Revenue. It was, to say the least, an error on their part, to assert that their audit had been "carried out strictly in accordance with the existing principles applicable to railway accounts." It is quite clear that such is not the case. Seeing that the London and North Western and Caledonian Companies are, and always have been, in such close alliance as to form, for most practical purposes, but one undertaking, I should have supposed that the latter company would have made the principles, upon which they base their charges against Revenue, conform to those of the former. But what do we find? Why this: that while the London and North Western Company make large improvements and replacements at the cost of Revenue, so as to *improve* as well as *maintain* the property, and thus, as the Chairman states, practically form a sinking fund,—while they, in order to leave nothing behind them, decline to omit any sums they have been in the habit of charging to Revenue, because the traffic may have been low, or much of the other Revenue expenditure exceptional,—the Caledonian Directors have, with the sanction of their auditors, accumulated heavy arrears of Revenue charges, debited Capital with every item of expenditure for which they could possibly find a pretext, omitting even to credit Capital with the original cost of the works, for which the new works carried to that much abused account were in substitution, and have actually made a retrospective journey through the Revenue accounts to the year 1861 to bring back to Capital account items of expenditure which had for years been peaceably reposing in the bosom of Revenue. What was the object of this exhumation, and on what "existing principles" was it based? Perhaps the auditors, who object so strongly to "displacement of amounts" from Capital to Revenue, but regard the process with singular complacency when the "displacement" is from Revenue to Capital, will inform us.

The fourth, and perhaps the most important, allegation made against the Caledonian Directors was that the sums charged against Revenue for the repairs and renewals of the rolling stock were inadequate. This is amply confirmed by Mr. D. K. Clark, in his report. He states that, "The sums which have been expended during the last two or three years for repairs and renewal of rolling stock have not been sufficient;" that the charge to Revenue for repairs has "fallen very low during the last three years, from 3½d. to 2d. per train mile;" that, "no charge for replacement of engines has been made in the last three half years;" that, "but for the large addition srecently made (at cost of Capital) to engine stock, replacement of the old engines would have been indispensable;" and he further observes that if the old engines had been adapted to the work or replaced out of Revenue, the recent addition to the engine stock at the cost of Capital would have been unnecessary. Mr. Clark's report is, therefore, conclusive as to the fact of Revenue having been relieved to a very large extent during the last few years of the charge for necessary renewals, by the simple process of purchasing new rolling stock out of Capital instead of repairing or renewing old. During the eighteen months ending July, 1867, 67 new engines were added to the stock on the Caledonian line proper, at the cost of Capital, although there are now no less than 100 engines which require to be replaced at the cost of Revenue. It is clear that if the replacements had been made from time to time as they became necessary, this large expenditure for new engines, amounting probably to upwards of £160,000, might have been avoided. The Directors very naïvely state in their reply (?) to the Investigation Committee: "It must be borne in mind that this plant has thrown upon Revenue an additional charge for interest which would have been a useless burden if the plant had not been employed." May I ask, if the 100 engines requiring replacement are not a useless burden? They represent, I presume, a large amount of Capital upon which interest should be paid, although several of them have been broken up, and others "laid up idly in store," and, therefore, not earning a penny of Revenue. Ought not then the existing stock of engines to have been put in an efficient condition, by making all the necessary renewals at the expense of Revenue, before purchasing so largely out of Capital? No stronger proof could be adduced of the reckless prodigality with which the Directors have been expending the money of the Shareholders than their purchasing 67 new engines at a time when the stock was amply sufficient in number for the requirements of the line. But this is not all. Mr. Clark affirms that "the existing stock of 524 locomotive engines is fully sufficient for the present traffic, and will, if the requisite replacements are made, further suffice for a considerable increase of traffic for the next five years, bearing in mind the new traffic that will arise upon the opening of the Mid Calder, and other lines and branches now in the course of construction." Yet there are 15 new engines contracted for, to be supplied to the Company, and 10 new engines are being constructed at the Company's engine works, and although the existing stock of engines is certified by Mr. Clark to be sufficient for the traffic for at least five years to come, and although Revenue has to replace 100 engines, the Directors coolly recommend that these new engines, instead of being dealt with as replacement of existing stock, shall be *added* to the stock, and charged to Capital! The proposal is simply monstrous, but unless the new Members of the Board are imbued with sounder principles, it will doubtless be carried into effect. It is futile to expect that the auditors, with their peculiar notions of "existing principles" of audit of railway accounts will interfere, inasmuch as they allowed £16,050, which had been debited to Revenue in 1866 for six new engines, to be subsequently transfered to Capital account, while for three half years they allowed Revenue to be relieved from all charge for replacement!

With regard to the carriage and waggon stock, it appears that a considerable number of vehicles have been broken up and not replaced. There are 70 carriages and 1209 waggons short of the number in the stock list of the Scottish North Eastern section, and 23 carriages and 1657 waggons in that of the Caledonian proper. These have been paid for out of Capital, and fall to be replaced out of Revenue. The Directors cannot consistently object to this, as Sir Charles Wood (now Viscount Halifax), in whose letter they seek, but fail to find, a justification of their conduct, states that "The rolling stock and plant, after being once paid for out of Capital, *must be kept up by Revenue to its full complement.*" This missing stock ought therefore to be immediately replaced at the cost of Revenue, and this involves a charge of about £170,000. Revenue being so largely indebted to carriage and waggon replacement account, the carriage stock contracted for and now being constructed for the Mid Calder line ought unquestionably to be charged to Revenue and not to Capital.

The foregoing facts with regard to the rolling stock show what heavy arrears have to be worked up at the cost of Revenue before the stock is put into thoroughly efficient condition, and brought up "to its full complement." Having regard to the amount of those arrears, I cannot concur with Mr. Clark that an expenditure of 5d. per train mile during the last two years would have prevented their accumulation. The replacements of stock now due from Revenue account amount to not less than upwards of £370,000. It is evident, therefore, that a much larger sum than 5d. per train mile ought to have been expended on the stock to maintain it in number and value. But this question cannot be satisfactorily disposed of until a careful valuation be made of the whole of the rolling stock; then the difference between its present value and the value at which it stands in the Company's Capital account, will be the extent to which Revenue has been short charged for its maintenance and renewal. Were such valuation to be made I feel satisfied from the disclosures in Mr. Clark's report as to the amount and condition of the older portion of the rolling stock, that in my former pamphlets I have rather under-estimated than over-stated the sums that should have been charged against Revenue during the last two years for repairs and renewals.

If I am rightly informed, the Scottish Central rolling stock was valued somewhere about the year 1856, and the average depreciation was found to be 30 per cent. from its original cost. Taking into account the fact that a large proportion of the Caledonian Company's rolling stock is nearly twenty years old, that the renewals have been exceptionally small, and that a large number of the vehicles have been broken up or are missing, I have no hesitation in affirming that if it were to be valued by competent and disinterested parties, the depreciation would be found to be greater than that of the Scottish Central stock. But assuming it to be the same, for the purpose of this argument, then 30 per cent. of £2,669,787 (the amount at which the rolling stock stood in the Company's books at 31st July, 1867) is equal to £800,934. Adopting the sound principle laid down by the Chairman of the London and North Western, that works and plant should not only be *maintained but improved*, the Caledonian Company would require to expend upwards of £800,000 sterling, to bring their rolling stock up to its normal value. The permanent way and works would be found to be, though perhaps not to so large an extent proportionately to their cost, in the same position as the rolling stock, and under these circumstances there is not a shadow of justification for placing any further sums to the debit of Capital, until it is ascertained beyond doubt that the permanent way and rolling stock have been brought up to their original value, even though they may have not been improved. If the London and North Western Railway Company regulates its expenditure on these severe but just principles, the Caledonian must perforce eventually do the same.

I may here mention that Mr. Clark's estimate of 25 years as the average duration of engines appears excessive, and certainly does not apply to the older stock of the Caledonian, inasmuch as the average life of the early engines has been less than 20 years, according to his own showing. And had it not been for the large infusion of new engines during the last few years, by means of which the older engines have been relieved of a great portion of their mileage, the life of the latter would not probably have exceeded sixteen years. Assuming that the infusion of additional new engines will now be stopped, the present engines will, on the opening of the Mid Calder and other lines, have to run a considerably increased mileage and their duration measured by time, will be materially shortened—say to 17 years at the utmost. Consequently as, independently of the 100 engines now to be replaced, there are 80 engines 13 to 14 years old, it is tolerably clear that they will require to be renewed in the course of three to four years. The cost of renewals of engines will therefore bear heavily upon Revenue for some years to come.

In the foregoing remarks I have endeavoured to confine myself as closely as possible to facts. The Caledonian Shareholders will do well to weigh carefully the serious nature of these facts in their bearing upon the present position and future prospects of the Company. It has been proved that the rolling stock has not been properly maintained at the cost of Revenue, although a large infusion of new stock has taken place at the expense of Capital. It has been shown that to restore the stock to its normal value on the principle laid down by Mr. R. Moon, the Chairman of the London and North Western, a sum would be required which would not only sweep away the whole of the dividends on the Ordinary Stock for the last two years, but absorb them for two or three years to come. It has been shown that Revenue is largely indebted to Capital for sums improperly debited to the latter account for reconstruction of bridges and other works in connection with the permanent way. It has been shown that credit has been taken for every farthing that could possibly be brought in aid of Revenue, while charges against Revenue have been allowed to fall seriously into arrear. It has been shown that many items which, in a former year had been charged to Revenue, have been recently, *designedly and deliberately*, transferred to Capital. These and other facts, which have been proved in the course of this enquiry, must necessarily tend to destroy all confidence in the present Board of Directors, and the auditors who permitted so many "displacements of amounts" in the Capital and Revenue accounts. The Committee of Investigation, so far from dealing with the question in more severe and just principles than usually obtain, have been far too lenient, and, as the *Times* observes, have been timorous and hesitating in their treatment of so important an inquiry.

It is for the Shareholders now to insist that the affairs of the Caledonian Company shall at once be placed on a sound basis, so as to restore the confidence of the public to the undertaking. The internal and external policy of the Board have been alike disastrous. An immense amount of Capital has been expended and lines purchased or leased on ruinous terms, to secure advantages which are now proposed to be surrendered by entering into a joint purse agreement with the opposing Company. The first step that is necessary is an entire reconstruction of the Board. Then let there be a searching and fearless investigation into the actual position of the Company; let the rolling stock and permanent way be valued, and such additions and improvements, at the cost of Revenue, made thereon as will bring them up to their original value. Thereafter let them be maintained and improved out of Revenue, as is the practice in the London and North Western. Finally, let it have a system of Audit which is a reality and not a sham. It is simply a truism to state that the profits of a year's working cannot be be estimated until the wear and tear of rolling stock and permanent way during that year are provided for out of Revenue. It would be unnecessary to insist on this point were it not that Directors, Auditors, and speculative Shareholders, who care only for the momentary dividend and market value of the stock, have shown a strong disposition to ignore it. But it is a law which cannot be ignored with impunity. Already something like ruin of the Ordinary Shareholders is threatened by the neglect of sound and prudent principles, and *continuance of such neglect will seriously endanger the interests of the Preference Shareholders also.* All classes of holders have therefore a common interest in enforcing the adoption of the principles which I have advocated, and which are now endorsed by the most eminent authorities on railway finance. Nothing but prompt and vigorous action, on the part of the Shareholders, in the direction I have indicated can save the Caledonian Railway from drifting into a more serious position than that in which it is at present placed.

I will only add, in conclusion, that my views having been challenged by the Chairman of the Caledonian Railway Company, I have submitted the whole documents relating to this controversy to Messrs. Price, Holyland, & Waterhouse, of London, who are the professional accountants of several English Railway Companies. From their high professional standing, great experience in railway accounts, and freedom from bias, their opinion, given at length in the Appendix, is entitled to great weight, and will be accepted by the general public (if not by such of the Caledonian Shareholders as "prefer a large dividend based on a cheat to a smaller one honestly earned") as conclusive upon the subject of Caledonian dividends during the two half-years ending 31st July, 1867. And I may further observe that the opinion and estimate formed by Messrs. Price, Holyland, and Waterhouse, of the financial position of the Caledonian Company, are not made up on any ultra severe principles, but on those adopted by all sound lines.

APPENDIX.

THE following accounts and documents referring to the two half-years ending the 31st July, 1867, have been left with us:—

Reports of the Directors and Published Accounts, Statement of Accounts, 18th March and 10th September, 1867; Report of the Committee of Inquiry to the Shareholders, dated January 3rd, 1868; the Observations of the Auditors on the Report of the Accountants to the Committee of Inquiry, dated 20th January, 1868; and the Reply by the Accountants to the Committee of Inquiry on the Observations of the Auditors, dated 28th January, 1868;

with a request that after examining them, we would give our opinion on the following points:

1st.—As to how much, if any part, of the charges of Capital in respect of the Main Line during this period ought to have been debited to Revenue.

2nd.—Whether, referring to the Observations of the Auditors on the Report of the Accountants to the Committee of Inquiry, we agree with those gentlemen in stating that the principle upon which railway accounts have hitherto been based has been "to charge to Capital the cost of all additions to the line, stations, rolling stock, or other property of the Company, as well as the additional cost, over and above the first outlay, of any improvement in the renewal or substitution of permanent way or works."

3rd.—Whether 5d. per train mile, as estimated by the Committee of Inquiry, is sufficient for the maintenance and replacement of the rolling stock, and if considered insufficient, what the amount should be?

4th.—Whether Premiums received upon Stocks issued, belong to Revenue or Capital; whether they may be applied to increase a dividend; and if they belong to Revenue, how should discount allowed upon the issue of Stock be borne?

5th.—As to the amount of the surplus, if any, during the past two half-years available for dividends on the Ordinary Stock which, after all proper charges to Revenue, had been made.

It must be remembered that the following replies are founded upon such papers only as have been laid before us.

1st.—We cannot state with accuracy how much of the charges to Capital in respect of the Main Line ought to have been debited to Revenue, but the small amount charged to Revenue for maintenance of way and works and stations, shows either that the railway has not been properly maintained, or that the expenditure incurred in keeping it in repair has been carried to Capital. We are satisfied that for the two half-years under review a further sum under this head of at least £34,817 ought to have been charged to Revenue.

2nd.—We find a difficulty in saying whether we do or do not agree with the Auditors, as we are not sure of the meaning which they attach to the word "additions." If by "additions to the line" their meaning is limited to new lines, a branch or an extension for example, no doubt the cost would be a proper charge to Capital, but there are many things which might be included under the term "additions to the line" which are Revenue charges. Additions to stations can be admitted against Capital only on condition that Revenue is charged with the entire original outlay upon the buildings destroyed to make way for the alteration or enlargement, less the amount, if any, that may have been written off in the meantime for depreciation and the value of the old materials.

We feel the same doubt as to the meaning of "additions to rolling stock" as to the "additions to the line," just mentioned, and the principle of our observation above applies to these also.

We do not agree with them in thinking that the "additional cost over and above the first outlay, of any improvement in the renewal or substitution of permanent way and works," is a charge against Capital. Additional *value* may be, and probably this is what is intended by the Auditors.

3rd.—We do not think 5d. per train mile sufficient for the maintenance and replacement of the rolling stock. We think a charge of 6½d. per train mile should have been made.

4th.—Premiums received upon the issue of Stock do not belong to Revenue, and ought not to be used to augment a dividend. They are a profit on Capital. No doubt it is competent to the Shareholders to divide the profit as a *bonus*, but it is wiser to apply it to Capital expenditure. This opinion renders it unnecessary for us to answer the latter part of the inquiry, as to how the discount allowed upon the issue of Stock should be borne, a question not wholly free from difficulty.

5th.—We are of opinion that if all proper charges to Revenue had been made, not only would there not have remained any surplus available for dividends upon the Ordinary Stock of the Company, but the Revenue account would have resulted in a balance on the debit side.

(Signed)

PRICE, HOLYLAND & WATERHOUSE.

13, Gresham Street, London,
4th February, 1868.