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United Fuel Investments
Limited

and

Subsidiary Companies

Eighteenth Annual Report

31st March, 1946

EIGHTEENTH ANNUAL REPORT
OF THE DIRECTORS OF
UNITED FUEL INVESTMENTS LIMITED
FOR THE YEAR ENDED 31st MARCH, 1946

Hamilton, Ontario, 7th June, 1946.

To the Shareholders:

Information concerning the operations of United Fuel Investments Limited and its wholly owned Subsidiaries for the fiscal year ended 31st March, 1946, is submitted in this report of your Board of Directors. Incorporated herein is the Consolidated Balance Sheet of the Company and its Subsidiaries as at 31st March, 1946, with the related Profit and Loss and Surplus Accounts showing the comparative figures for the corresponding period last year and the Auditors' Report to the Shareholders.

OPERATIONS

Consolidated Net Profits of your Company and its wholly owned Subsidiaries for the year, as compared with the previous year, are as follows:

	Year ended 31st March			
	1946		1945	
Net profit for the year before provision for depreciation, reserve for inventory and taxes on income . . .		$685,409		$912,101
Less: Provision for regular depreciation on plant and equipment . . .	$248,055		$251,340	
Amortization of plants erected for war requirements		248,055	84,418	335,758
Net profit before providing for inventory reserve and taxes on income . .		$437,354		$576,343
Less: Provision for income and excess profits taxes	190,000		247,000	
Provision for future price decline in inventory values		190,000	15,000	262,000
Net profit for the year.		$247,354		$314,343

The decrease of $226,692 in net profit before providing for depreciation, reserve for inventory and taxes on income is attributable to the following:

Decrease in gross value of sales of all products produced or purchased for resale	$718,475	
Decrease in gross production cost or purchase price of all products sold	429,282	
		$289,193
Reduction in sundry income and interest earned		9,949
		$299,142

Less: Decrease in interest on funded debt and bond discount absorbed	$ 57,604	
Reduction in total general and administrative selling and gas distribution expenses	14,846	
		72,450
Net decrease in profit before providing for depreciation, reserve for inventory and taxes on income		$226,692

The net reduction of $718,475, or 10.7%, in gross value of sales was due to a decrease in volume of sales of all products, and to a decrease in the selling price per ton of coke, one of the main products of your Company. The cost of all products sold decreased only $429,282, or 8.4%, due to the reduction in volume of sales, although the unit cost of all products produced or purchased for sale was slightly less than for the previous year. As a result, gross profit on sales decreased $289,193, or 18%.

The most important raw material used in the production of coke and gas in the plants of your Company is coal, practically all of which is imported directly from the United States. Since 1940 the cost per ton of coal charged to the ovens after allowance for duty drawbacks received, has increased approximately 57% even though for the fiscal year ended 31st March, 1946, there was actually a small decrease in this cost per ton as compared with the previous fiscal year, arising from the cancellation during the year of the 10% War Exchange Tax imposed by the Dominion Government in 1940, and the retention by your Company, with the approval of the Wartime Prices and Trade Board, of that portion of the duty drawback on coal previously passed on to a few large industrial coke customers.

The effect of these steadily increasing coal costs on the earnings of your Company, during a period in which for a large portion of the time Government Orders prohibited voluntary increase in the selling prices of any of your Company's products, was so serious that applications were made to the Dominion Government for price adjustment to offset these increased costs. As a result of these applications the Dominion Coal Controller, with the approval of the Wartime Prices and Trade Board, in May, 1943, authorized a special price increase of $2.00 per ton on all coke produced and sold for industrial use. However, in October, 1944, this special price increase of $2.00 per ton was cancelled by the Dominion Coal Controller. Thus, industrial coke selling prices reverted to the level in effect in 1941 when prices were frozen by Government Order, even though after that date there had been substantial increases in the cost per ton of coal. As a result your Company was again faced with the prospect of operating at little or no profit on an annual basis.

Applications were again made to the Coal Controller and to the Wartime Prices and Trade Board, and after extensive negotiations some measure of relief was received effective in June, 1945, through your Company being authorized to retain for its own account certain duty drawbacks on coal previously passed along to industrial customers, and through the cancellation by the Dominion Government upon the recommendation of the Wartime Prices and Trade Board, of the 10% War Exchange Tax on all importations of coal. Later, that Board recognized that your Company should receive further relief and effective in December, 1945, authorized a special price increase of 75c. per ton on all coke produced and sold for industrial purposes, thus restoring only a small portion of the special price increase cancelled in October, 1944. However, this special price adjustment of 75c. per ton was in effect for less than four months of the fiscal year ended 31st March, 1946.

The total volume of gas sold during the year decreased approximately 7.5% as compared with the previous fiscal year, a reduction of 20% in the volume of sales for industrial purposes being only partially offset by an increase of 9.5% in the volume of sales to domestic and commercial customers. Although the average rate received for all gas sold during the year was approximately the same as for last year, the decrease in volume of sales together with higher production costs resulted in a reduction in revenue and gross profits from gas sales. There was also a moderate decrease in gross profit from sales of by-products and coke purchased for resale.

The decrease in interest on funded debt and bond discount absorbed resulted from the refunding operations carried out during the previous fiscal year, operations for the fiscal year ended 31st March, 1946, having received the benefit for a full year of the reduced interest rates on the refunding bond issue.

The net reduction in total general and administrative, selling and gas distribution expenses was due mainly to the cancellation after the cessation of hostilities of certain expenses attributable directly to operating under wartime conditions, such as special plant protection, and to an increase in the volume of gas appliance sales.

Provision for regular depreciation on plant and equipment for the year amounted to $248,055, a decrease of $3,285 as compared with last year. As full provision for special amortization of plants erected for war requirements had been provided as at 31st March, 1945, with the appropriation of $84,418 for this purpose from the earnings of that year, no corresponding charge was made against earnings for the fiscal year ended 31st March, 1946. Only a nominal post-war value placed on the facilities erected for war requirements is now carried in the accounts.

Inventories have been priced at the lower of cost or market and the total as thus determined has been reduced by net appropriations of $140,500 from earnings of prior years as a reserve against future decline in values. The total reserve carried for this purpose as at 31st March, 1945, was $256,000, but due to a substantial reduction in the volume of coal on hand at 31st March, 1946, as compared with the normal carry-over of coal, it was considered appropriate to reduce this reserve by $115,500, which amount, less taxes on income applicable thereto, was credited to Surplus Account as at 31st March, 1946. The reduction in coal inventories at the year end was brought about by strikes in the coal fields in the United States towards the close of the 1945 boating season, thus making it impossible for your Company to obtain the normal volume of coal importation during that year. For the fiscal year ended 31st March, 1945, an amount of $15,000 was charged against earnings as a provision for additional reserve against these inventories, but no provision was required to be charged against the earnings of the fiscal year ended 31st March, 1946, for this purpose.

Surplus Account for the year ended 31st March, 1946, has been credited with $148,960 representing the above mentioned reduction in inventory reserve requirements, coal overages and other adjustments relating to prior years, less taxes on income applicable thereto. In view of the uncertain operating conditions currently facing your Company, especially the problems pertaining to the future supply and prices of coal, your Directors considered it advisable to set aside $100,000 of this amount as a Reserve for Contingencies.

As at 31st March, 1946, the working capital of your Company, after deducting $130,000 par value of First Collateral Mortgage Serial Bonds, Series "A" due 1st December, 1946, amounted to $1,272,865 as compared with $1,071,846 at 31st March, 1945, an increase of $201,019. The following statement shows in summarized form the income from profits and other sources during the year and the disposition made of these funds.

Net earnings for the year after all charges excepting provision for taxes on income	$437,354	
Less: Provision for income and excess profits taxes including refundable portion	191,500	$245,854
Add: Charges against earnings which do not represent cash disbursements:		
Depreciation	$248,055	
Amortization of bond discount and bond issue expenses	9,876	257,931
Total funds provided from operations		$503,785
Add: Adjustments through Surplus Account relating to prior years, including coal overage and reduction in reserve for inventories, less taxes on income applicable thereto		148,960
Total		$652,745
Accounted for as follows:		
Dividends on capital stock paid or provided for	$270,000	
Cost of additions to fixed assets (net)	51,492	
Sundry items (net)	234	
	$321,726	
First Collateral Mortgage Serial Bonds Series "A" maturing 1st December, 1946	130,000	451,726
Resulting in an increase in net current assets of		$201,019
Working capital at beginning of year		1,071,846
Working capital at end of year		$1,272,865

The net increase in fixed assets after deducting plant replaced and written off amounted to $25,661. With the exception of a nominal expansion in the gas distribution system to supply additional customers from the existing mains, construction work during the year was confined to necessary plant renewals and replacements. The increase in reserve for depreciation and renewals amounted to $222,224.

On 1st December, 1945, $130,000 par value of First Collateral Mortgage 3% Serial Bonds, Series "A", matured and were retired at par.

Dividends of $270,000 were paid during the year, being four quarterly dividends of 75 cents per share, or a total of $3.00 per share, on the 6% Cumulative Preferred Class "A" shares.

FUTURE OPERATIONS

Reference has been made in this Report to the fact that the cost per ton of coal charged to the ovens has increased steadily since the outbreak of war and that for the year ended 31st March, 1946, this cost was approximately 57% greater than in 1940. Since the base period in 1941 when the selling prices of gas and coke were frozen by the Dominion Government as part of its price fixing program, there has been no change in the general rates charged for gas sold by the Company, and with the exception of the special price increases allowed on industrial coke sales for a limited period, there has been no change in the selling prices of coke. The result has been that even with the elimination of such extraordinary charges as reserves for inventories and amortization of plants erected for war purposes, and the substantial reduction in interest charges due to the refunding of the bond issues at lower interest rates in 1944, net profits from operations for the fiscal year ended 31st March, 1946, fell short of meeting the dividend requirement on the 6% Cumulative Preferred Class "A" shares by $22,646.

The largest annual expenditure which your company is required to make is for the purchase of coal imported from the United States. Strikes in the coal mines last Autumn and in April and May of this year have resulted in the Company's stock piles of coal shrinking very rapidly to the point where, at the present time, there is barely sufficient coal on hand to enable continued operation even on a reduced scale for more than one month, although a considerable quantity of coal was imported from the United States by all-rail shipment during the past winter. While operations at the mines have again been resumed, a considerable portion of the current boating season has already elapsed and in view of the current disruption in shipping schedules as a result of the strike by Canadian seamen, it appears very unlikely that the entire volume of coal required to be imported by your Company this year will be received before the close of navigation. It is therefore highly probable that substantial quantities of coal will again be required to be brought in by all-rail shipment during the coming winter. The increased costs of importing coal via all-rail instead of by boat and recent increases in coal prices at the mines as an offset against higher mining labor costs will result in another substantial increase in the cost of coal charged to the ovens in the production of coke and gas.

Owing to a steady decrease in the available natural gas reserves of the companies which supply natural gas for distribution in the various natural gas markets of your Company, the volumes of gas available from this source are steadily decreasing. To make up this deficiency in gas supply, it is becoming necessary for your Company to operate its auxiliary plant for the production of gas from liquid propane over longer periods in each year. The gas produced from liquid propane is much more costly than the natural gas formerly available, although it is being sold at the same rates as apply for natural gas.

It is therefore quite apparent that your Company must receive higher prices for the sale of its products to cover these increases in costs over which it has no control. Your Directors and Management are fully aware of the serious effect on the financial stability of your Company which would result from operating under such conditions for a prolonged period, and it is their intention to apply to the various Governmental authorities for increases in selling prices as soon as the full effect of the latest increase in the laid-down cost of coal on the Company's dock can be ascertained. The future operating results of your Company will be influenced by the extent of these increased costs and to what extent the competitive situation and price fixing authorities will allow adjustment of selling prices to recover these greater costs.

GENERAL

The plant erected and owned by the Dominion Government to produce gas and coke for war purposes on property adjacent to the coke oven plant of your Company was in continuous operation during the year. This plant is being operated and its products marketed by your Company for the Government on a cost basis without any benefit to the earnings of your Company. While it was originally intended that this plant would operate for only a limited period after the end of the war, it now appears that due to existing shortages in all solid fuels in Central Canada the Government will require the continued operation of the plant for an indefinite period.

We shall always hold in honor the memory of those members of the staff who made the supreme sacrifice while serving with the Armed Forces. A total of 85 were granted leave of absence from the Company to go on active service and we are pleased to welcome back those who have now returned to their former employment with the Company. We gratefully acknowledge their achievements while in the service of their country.

Your Directors wish to record at this time their appreciation of the loyalty and devotion to duty throughout the past year of all employees of the Company.

On behalf of the Board of Directors.

DAVID P. ROGERS,

President.

AUDITORS' REPORT TO THE SHAREHOLDERS

We have examined the consolidated balance sheet of United Fuel Investments Limited and its subsidiaries, Hamilton By Product Coke Ovens Limited, United Gas and Fuel Company of Hamilton Limited (and its subsidiary, The Wentworth Gas Company Limited) and the United Suburban Gas Company Limited, as at 31st March, 1946, and the statements of consolidated profit and loss and earned surplus for the year ended on that date. In connection therewith we reviewed the system of internal control and the accounting procedures of the companies and examined or tested accounting records but we did not make a detailed audit of the transactions. We have obtained all the information and explanations we required.

Depreciation of capital assets has been provided for on the bases approved by the consulting engineer of the companies in 1942, subject to which we report that in our opinion the accompanying consolidated balance sheet and related statements of consolidated profit and loss and earned surplus have been drawn up so as to exhibit a true and correct view of the state of the combined companies' affairs at 31st March, 1946, and of the results of their operations for the year ended on that date, according to the best of our information, the explanations given us and as shown by the books of the companies.

CLARKSON, GORDON & CO.,
Chartered Accountants.

Hamilton, Canada,
27th May, 1946.

UNITED FUEL INVESTMENTS LIMITED
AND ITS SUBSIDIARIES

Statement of Consolidated Profit and Loss for the Year ended 31st March 1946
(With comparative figures for the year 1945)

	1946		1945	
Profit from operations before charging bond interest, depreciation, etc.		$865,763		$1,150,059
Deduct:				
Interest on bonds including premium on United States funds	$170,478		$219,485	
Bond discount absorbed	9,876	180,354	18,473	237,958
		$685,409		$912,101
Provision for depreciation on the bases approved by companies' consulting engineer	$248,055		$251,340	
Amortization of plants erected for war requirements			84,418	
		248,055		335,758
Net profit before providing for inventory reserve and taxes on income		$437,354		$576,343
Provision for income and excess profits taxes	$191,500		$250,000	
Less: Refundable portion thereof	1,500		3,000	
	$190,000		$247,000	
Provision for future price decline in inventory values			15,000	
		190,000		262,000
Net profit for the year		$247,354		$314,343

Note: The expenses of the companies for the year ended 31st March, 1946, include:

Remuneration of directors (not including executive officers)	$ 2,400
Payments to counsel, solicitors and legal advisers	6,700
Remuneration of executive officers	24,000

Statement of Consolidated Earned Surplus for the Year ended 31st March 1946
(With comparative figures for the year 1945)

	1946		1945	
Balance at beginning of year		$1,019,656		$1,334,994
Add:				
Net profit for the year as above		247,354		314,343
Adjustments relating to prior years (including reduction of $115,500 in inventory reserve in 1946) and after deducting in 1946 net taxes of $50,500	$148,960		$ 31,666 –	
Less: Provided for contingencies	100,000	48,960		31,666 –
		$1,315,970		$1,617,671
Deduct:				
Dividends on 6% preferred shares	$270,000		$270,000	
Refinancing charges (including balance of bond discount) on bonds of subsidiary companies redeemed			328,015	
		270,000		598,015
Balance at end of year		$1,045,970		$1,019,656

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ASSETS

	31st March 1946	31st March 1945
PROPERTY:		
Comprising gas and coke manufacturing plants, transmission lines, distribution systems, real estate, buildings, automobiles, fixtures, franchises, rights, organization expenses, interest during construction, etc.	$11,829,563	$11,803,902
Deduct reserve for depreciation and renewals	5,420,179	5,197,955
	$ 6,409,384	$ 6,605,947
NOTE: The above assets are valued at cost with the exception of assets of United Gas and Fuel Company of Hamilton Limited, acquired prior to 31st March, 1929, aggregating $4,238,980, which are shown at the values at which they were carried in the books of that company at that date.		
PREMIUMS paid on acquisition of subsidiary companies	4,079,955	4,079,955
	$10,489,339	$10,685,902
CURRENT ASSETS:		
Cash on hand and in banks	$ 682,446	$ 463,815
Investment in marketable securities at cost and accrued interest (approximate market value 31st March, 1946, $211,715):		
Dominion of Canada 3% Victory Loan Bonds	202,480	251,814
City of Hamilton ninety-day treasury bills.		199,284
Accounts receivable less reserve	776,806	670,239
Inventories as determined and certified by the management from book records and valued at the lower of cost or market, less reserve of $140,500 in 1946 and $256,000 in 1945 for future price decline in inventories.	417,874	633,027
	$ 2,079,606	$ 2,218,179
DEFERRED AND OTHER ASSETS:		
Bond discount, commissions and expenses less amounts written off	$ 134,952	$ 144,828
Deferred charges and prepaid expenses	101,359	117,142
Stores and spare equipment	170,400	156,883
Refundable portion of taxes on income	46,500	42,500
	$ 453,211	$ 461,353
	$13,022,156	$13,365,434

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Dominion Companies Act)

SUBSIDIARIES

Balance Sheet

March 1946

LIABILITIES

	31st March 1946	31st March 1945
Capital and Surplus:		
Capital:		
Class "A" 6% cumulative preferred shares of $50 each redeemable at the option of the company or by purchase in the open market for cancellation at a price not exceeding $60:		
Authorized and issued—90,000 shares . . .	$ 4,500,000	$ 4,500,000
Class "B" non-cumulative preferred shares of $25 each purchasable in the open market by the company for cancellation at a price not exceeding $30:		
Authorized and outstanding . 69,689 shares	1,742,225	1,742,225
Common shares of no par value:		
Authorized and issued . . . 90,000 shares	50,000	50,000
Capital surplus arising from discount on redemption of Class "B" preferred shares	417,220	417,220
Consolidated earned surplus	1,045,970	1,019,656
	$ 7,755,415	$ 7,729,101
Funded Debt:		
First collateral mortgage serial and sinking fund bonds—authorized $5,500,000, whereof issued $4,500,000:		
3% Serial bonds (Series "A") due 1st December 1947 to 1950	$ 740,000	$ 870,000
4% Sinking fund bonds (Series "A") due 1st December, 1959	2,300,000	2,300,000
3¾% Serial bonds (Series "B") due 1st December, 1951, to 1956 (payable in Canadian or United States funds at the option of the holder)	1,200,000	1,200,000
	$ 4,240,000	$ 4,370,000
Reserve arising from exchange on sale of series "B" bonds in United States Funds.	$ 120,000	$ 120,000
Current Liabilities:		
Accounts payable and accrued charges including meter deposits	$ 315,419	$ 678,292
Accrued interest on bonds	55,327	56,687
Reserve for income, excess profits and other taxes . . .	238,495	213,854
Dividend payable	67,500	67,500
First collateral mortgage serial bonds (Series "A")		
—due 1st December, 1946	130,000	
—matured 1st December, 1945		130,000
	$ 806,741	$ 1,146,333
Reserve for Contingencies	$ 100,000	
	$13,022,156	$13,365,434

Approved on behalf of the Board.

DAVID P. ROGERS, *Director.*
S. B. SEVERSON, *Director.*

UNITED FUEL INVESTMENTS LIMITED

AND

SUBSIDIARY COMPANIES

Officers

D. P. Rogers	*President*
S. B. Severson	*Vice-President*
T. P. Pinckard	*General Manager of Subsidiaries*
F. Palin, C.A.	*Comptroller, Secretary and Treasurer*
W. M. Common	*Assistant Secretary and Assistant Treasurer*

Directors

H. D. Hancock	S. B. Severson
R. L. O'Brian	C. E. Weger
D. P. Rogers	T. Weir

SUBSIDIARY COMPANIES

Hamilton By Product Coke Ovens Limited—
Manufacturing coke, gas and by-products in Hamilton, Ontario.

United Gas & Fuel Company of Hamilton Limited—
Distributing manufactured and natural gas in Hamilton, Ontario.

and its wholly owned subsidiary:

The Wentworth Gas Company Limited—
Distributing natural gas in Dundas, Waterdown, Burlington and other territory adjacent to Hamilton, Ontario.

The United Suburban Gas Company Limited—
Distributing manufactured gas in Oakville, Bronte, Port Nelson and Burlington Beach, Ontario.