

Tenth
ANNUAL REPORT
1950



Southwest Airways

C O M P A N Y

SAN FRANCISCO AIRPORT
SOUTH SAN FRANCISCO, CALIFORNIA



Southwest Airways Company

*General Offices
San Francisco Airport
South San Francisco, California*

OFFICERS

LELAND HAYWARD	<i>Chairman</i>
JOHN H. CONNELLY	<i>President</i>
TED R. MITCHELL	<i>Vice-President</i>
ALWIN W. JOHNSON	<i>Treasurer</i>
HARRY S. WHITE	<i>Sales Manager</i>
WALTER ROCHE	<i>Secretary</i>
CORNELIUS H. SULLAVAN	<i>Assistant Secretary</i>
FLOYD HENDRICKSON	<i>Assistant Secretary</i>

BOARD OF DIRECTORS

BERT ALLENBERG	ALWIN W. JOHNSON
JOHN H. CONNELLY	DANIEL O'SHEA
LELAND HAYWARD	WALTER ROCHE
FLOYD HENDRICKSON	HARRY S. WHITE

AUDITORS

PRICE, WATERHOUSE & COMPANY
351 California Street, San Francisco, California

REGISTRAR AND TRANSFER AGENT

WALTER ROCHE
309 First National Bank Building, Phoenix, Arizona

PRESIDENT'S REPORT

To the Stockholders and Employees of Southwest Airways Company

In the year 1950, which was the fourth full year of operation by Southwest Airways as a Federally certificated local service air carrier, the Company continued to progress and earned a net profit of \$135,473.05, equivalent to \$.2079 a share on the outstanding capital stock, after provision for Federal income

taxes of \$92,532.50. This compares with a net profit of \$81,143.17 for the year 1949, or \$.1253 a share after Federal income taxes of \$53,078.45. A summary of the Company's operations from the inception of certificated flight operations on December 2, 1946 is set forth in the following table:

	1950	1949	1948	1947*
<i>Operating Revenues:</i>				
Passenger, express freight, charter, etc.....	\$1,269,857	\$1,148,588	\$ 962,421	\$ 710,451
Mail	<u>943,888</u>	<u>1,249,992</u>	<u>1,401,332</u>	<u>1,504,510</u>
Total operating revenues.....	\$2,213,745	\$2,398,580	\$2,363,753	\$2,214,961
 <i>Operating Expenses</i>	<u>1,968,883</u>	<u>2,263,878</u>	<u>2,283,989</u>	<u>2,172,077</u>
<i>Operating Profit</i>	\$ 244,862	\$ 134,702	\$ 79,764	\$ 42,884
Non-operating expense (net)	<u>16,856</u>	<u>481</u>	<u>15,602</u>	<u>37,403</u>
 <i>Net Profit Before Federal</i>				
<i>Income Taxes</i>	\$ 228,006	\$ 134,221	\$ 64,162	\$ 5,481
Federal income taxes	<u>92,533</u>	<u>53,078</u>	<u>36,100</u>	<u>.....</u>
<i>Net Profit After Taxes</i>	<u>\$ 135,473</u>	<u>\$ 81,143</u>	<u>\$ 28,062</u>	<u>\$ 5,481</u>

*Covers the 13 month period ending December 31, 1947.

Southwest Airways Company



OPERATING STATISTICS

	1950	1949	1948	1947*
<i>Revenue miles flown</i>	2,375,224	2,419,695	2,363,827	1,854,117
<i>Revenue passenger miles</i>	22,236,008	20,947,484	18,046,778	15,348,113
<i>Passenger load factors</i>	45.80%	41.56%	36.56%	39.73%
Number of passengers carried:				
Scheduled service	118,860	114,573	97,424	83,994
Charter service	3,111	1,345	530	1,082
Total passengers carried	121,971	115,918	97,954	85,076
<i>Mail ton miles</i>	46,406	51,136	45,892	35,146
<i>Express ton miles</i>	49,394	34,199	31,856	32,177
<i>Freight ton miles</i>	126,773	90,177	75,064	10,431
<i>Excess baggage ton miles</i>	7,495	6,746	6,142	5,142

*Covers the 13 month period ending December 31, 1947.

The above statements show the Company's consistent trend of increasing non-mail operating revenues and the lessening necessity for Government support in the form of mail pay. Operating revenue from passengers, express, freight, charter, etc., increased 10.5% in 1950 over 1949. Revenue received for transporting mail by aircraft decreased 24.5% in 1950 over 1949. Operating expenses in 1950 decreased approximately

13% over 1949, caused principally by a reduction in depreciation of flight and other equipment of \$274,805 due to certain equipment reaching a fully depreciated status, and a change in flight equipment depreciation rates effective January 1, 1950. Prior to that date, flight equipment costs were amortized over three years to a residual value of 10%. Beginning January 1, 1950 the estimated residual value was

reduced to 5% and the then book value of flight equipment was amortized over the four years ending December 31, 1953. Other factors resulting in lower costs were greater efficiency on the part of the Company's employees and the approval by the Civil Aeronautics Administration of substantial increases in the intervals of time of use before overhaul of the various aircraft components.

The Company began the year operating flight equipment consisting of nine DC-3 Douglas aircraft of 24 seats each. These nine aircraft are now undergoing conversion to 28 seats each. The Company also owned two C-47 Douglas aircraft held in reserve, which were converted in the Company's own shops in the spring and summer of 1950 to DC-3 aircraft of 27 seats each. This fleet of eleven operating aircraft will make it possible for the Company to furnish better service to the public and participate to an even greater degree in the available charter, freight and scheduled passenger business.

On January 1, 1950, the Civil Aeronautics Board reduced the Company's mail rate to an amount which yielded 40.83 cents per scheduled mile flown in 1950, as compared with 52.08 cents per mile received in 1949. This reduction in mail pay requirements manifests a very healthy trend for the Company and is brought about principally by an increase in non-mail revenues and a decrease in operating expenses which has been previously discussed. The following statement shows the extent to which the Company's break-even need per revenue aircraft mile flown has decreased in the past four years. It has been the constant aim of the Company's management to reach a self-sufficient status so that the compensation received for carrying the mail will be for services rendered without any element of subsidy. In furtherance of this policy, the Company has voluntarily petitioned the Civil Aeronautics Board to lower its mail compensation to a rate which will yield 33.5 cents per scheduled mile flown effective May 1, 1951.

PER REVENUE MILE FLOWN

	1950	1949	1948	1947*
<i>Operating revenues (exclusive</i>				
<i>of mail pay)</i>	\$.5346	\$.4747	\$.4071	\$.3832
<i>Operating expenses</i>	<u>.8289</u>	<u>.9356</u>	<u>.9662</u>	<u>1.1715</u>
<i>Amount of mail pay needed</i>				
<i>to break even</i>	<u>\$.2943</u>	<u>\$.4609</u>	<u>\$.5591</u>	<u>\$.7883</u>

**Covers the 13 month period ending December 31, 1947.*

Southwest Airways Company

Simplified Comparative Statement of INCOME and EXPENSES

	1950		1949	
	Amount	Per \$1.00 of Revenue	Amount	Per \$1.00 of Revenue
<i>Income Received from Following Sources:</i>				
Passengers	\$1,139,969	\$.5121	\$1,059,558	\$.4400
Express	18,877	.0085	14,136	.0059
Freight	43,925	.0198	36,007	.0149
Excess baggage	4,056	.0018	3,796	.0016
Charter	41,898	.0188	15,607	.0065
Incidental operating revenues...	21,132	.0095	19,484	.0081
Other income	12,207	.0055	9,448	.0039
	<u>\$1,282,064</u>	<u>\$.5760</u>	<u>\$1,158,036</u>	<u>\$.4809</u>
Mail	943,888	.4240	1,249,992	.5191
Gross Income	<u>\$2,225,952</u>	<u>\$1.0000</u>	<u>\$2,408,028</u>	<u>\$1.0000</u>
<i>Disposition of Gross Income:</i>				
Wages and salaries paid to employees	\$1,013,610	\$.4554	\$ 990,789	\$.4115
Gasoline and oil	243,729	.1095	249,126	.1035
Telephone, telegraph and teletype	78,106	.0351	68,724	.0285
Other materials, supplies, and services	215,050	.0966	283,727	.1178
Rentals and landing fees	65,323	.0293	63,771	.0265
Insurance	69,994	.0314	68,314	.0284
Travel and incidental	52,320	.0235	54,697	.0227
Advertising and publicity	83,572	.0375	65,649	.0273
Depreciation	82,256	.0369	357,061	.1483
Taxes other than Federal income taxes	72,054	.0324	70,610	.0293
Amortization of extension and development expenses	21,932	.0099	1,339	.0005
Federal income taxes	92,533	.0416	53,078	.0220
Total Expenses	<u>\$2,090,479</u>	<u>\$.9391</u>	<u>\$2,326,885</u>	<u>\$.9663</u>
Balance retained by the Company for use in the development of the business	<u>\$ 135,473</u>	<u>\$.0609</u>	<u>\$ 81,143</u>	<u>\$.0337</u>

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AS SHOWN by the certified financial statements included in this report, the Company is in excellent condition, having a working capital ratio of 2.6 to 1 and a net worth of \$1,070,952.28,

equivalent to \$1.64 a share of outstanding capital stock. The eleven operating aircraft are included therein at an average book value on December 31, 1950 of \$22,500 each and are insured for a value of \$85,000 each.

On April 10, 1950, the Company and West Coast Airlines, Inc. jointly filed a petition with the Civil Aeronautics Board proposing a merger of West Coast into Southwest. This joint petition was the result of resolutions by the Board of Directors of West Coast Airlines, Inc. on December 2, 1949 and of Southwest Airways Company on February 27, 1950, authorizing such action. Under the terms of the proposed merger agreement, Southwest will ac-

quire a maximum of $\frac{2}{3}$ out of 187,371 $\frac{1}{2}$ outstanding shares of capital stock of West Coast for \$5.25 per share and the balance of the West Coast stock will be acquired by Southwest in exchange for Southwest stock under a formula involving an adjusted book value of the respective shares of stock. Although September 1949 financial statements of both companies formed the basis on which a merger agreement was reached, it should be pointed out that the actual ratio of exchange of stock will be determined from the financial condition of each of the companies at the end of the second month preceding the date of approval of the merger by the Civil Aeronautics Board. As of December 31, 1950 this exchange would have been 2.07 shares of Southwest for 1 share of West Coast. The following condensed pro-forma balance sheets before and after merger show the financial changes that have taken place between the time immediately before the merger negotiations took place and the end of 1950.

PRO-FORMA BALANCE SHEETS

	AS OF SEPTEMBER 30, 1949			AS OF DECEMBER 31, 1950		
	Southwest	West Coast	After Merger	Southwest	West Coast	After Merger
Current assets	\$ 813,510	\$ 675,061	\$ 911,445	\$1,002,074	\$ 732,117	\$1,152,088
Equipment (net)	335,123	341,390	676,513	369,940	224,398	594,338
Other assets	107,836	109,420	217,256	131,574	65,333	196,907
Total Assets	<u>\$1,256,469</u>	<u>\$1,125,871</u>	<u>\$1,805,214</u>	<u>\$1,503,588</u>	<u>\$1,021,848</u>	<u>\$1,943,333</u>
Current Liabilities	\$ 295,191	\$ 187,958	\$ 483,149	\$ 383,536	\$ 155,458	\$ 538,994
Long term debt	145,000	145,000	75,000	75,000
Reserves	38,159	9,848	48,007	49,100	14,933	64,033
	<u>\$ 333,350</u>	<u>\$ 342,806</u>	<u>\$ 676,156</u>	<u>\$ 432,636</u>	<u>\$ 245,391</u>	<u>\$ 678,027</u>
NET WORTH:						
Capital stock	\$ 323,830	\$ 187,371	\$ 415,224	\$ 325,805	\$ 187,371	\$ 416,745
Surplus	599,289	595,694	713,834	745,147	589,086	848,561
	<u>\$ 923,119</u>	<u>\$ 783,065</u>	<u>\$1,129,058</u>	<u>\$1,070,952</u>	<u>\$ 776,457</u>	<u>\$1,265,306</u>
Total Liabilities	<u>\$1,256,469</u>	<u>\$1,125,871</u>	<u>\$1,805,214</u>	<u>\$1,503,588</u>	<u>\$1,021,848</u>	<u>\$1,943,333</u>

A public hearing on the merger was conducted by the Civil Aeronautics Board in November 1950 during which the merger was opposed by United Airlines, Inc. and Western Air Lines, Inc. It is not believed, however, that the Civil Aeronautics Board will allow such opposition to in any way deter the Board's sound development of the nation's air transport system on the West Coast. Under date of April 11, 1951 the Examiner

rendered his report on the merger hearing and recommended that the Civil Aeronautics Board approve the merger of Southwest and West Coast and transfer the certificate of public convenience and necessity of West Coast to Southwest. The oral argument will probably be held in the summer of 1951 and the Board's decision should be forthcoming shortly thereafter. If the Civil Aeronautics Board renders a decision favorable to the

merger and the transaction is consummated in the manner provided for and outlined above, Southwest Airways will emerge as the continuing operating company. It will be observed from Note C to the financial statements that there is a contingent stock option outstanding which entitles the holder to purchase 32,500 shares of the unissued common stock of the Company at \$1.50 per share. This option was granted to Mr. Nick Bez, President of West Coast Airlines, Inc. as an inducement for him to continue his activities on behalf of the

merged company. Mr. Bez has a history of long successful association in the Pacific Northwest and as one of its leading citizens is well-known throughout the area. The directors of Southwest believe that the continued interest of Mr. Bez is very important and desirable for the successful development of the merged company in the Pacific Northwest and offered the option method as being the most economical manner of assuring the continuation of his services. The following is a copy of the option agreement.

OPTION AGREEMENT

WHEREAS, SOUTHWEST AIRWAYS COMPANY, a corporation, is a certificated air carrier operating a feeder line in California and adjacent states with the northern terminus thereof at Medford, Oregon, and WEST COAST AIRLINES, INC., a corporation, is a certificated air carrier operating a feeder line in the states of Washington and Oregon with the southern terminus thereof at Medford, Oregon, and

WHEREAS, the principal stockholders of said two companies have agreed to vote their stock and use their best efforts to cause other stockholders of said two companies and their respective boards of directors to vote, in favor of a merger of said two companies, subject to Civil Aeronautics Board approval, whereby one company will operate, as a certificated air carrier, the combined routes of said two companies or such thereof as may be deemed advisable, and

WHEREAS, Nick Bez organized West Coast Airlines, Inc., and has been the President thereof throughout its corporate existence, and said Nick Bez is interested in the purchase of a substantial number of shares of the common stock of Southwest Airways Company which it is contemplated will operate the combined routes of said two air carriers as the surviving corporation resulting from the said merger, and

WHEREAS, it is to the corporate best interest of Southwest Airways Company that an option be granted to said Nick Bez on the terms herein set forth:

NOW, THEREFORE, it is mutually agreed between Southwest Airways Company and Nick Bez:

1. In consideration of the sum of One Hundred Dollars (\$100.00) in hand paid by Nick Bez to Southwest Airways Company, the receipt whereof is hereby acknowledged, Southwest Airways Company hereby grants to Nick Bez (a resident of the State of Washington), his heirs, executors, administrators, and assigns, an option to purchase 32,500 shares of the common capital stock of Southwest Airways Company at \$1.50 per share, exercisable in whole or in part at any time within a five (5) year period beginning thirty (30) days after the date the Civil Aeronautics Board approves the merger or consolidation of West Coast Airlines, Inc. and Southwest Airways Company; provided, however, that before said option may be exercised Southwest Airways Company shall have acquired a minimum of two-thirds (2/3) of the outstanding stock of West Coast Airlines, Inc. or said merger or consolidation shall have been consummated. In the event this option shall not have become exercisable, as hereinabove provided, on or before January 1, 1953 said option shall expire and terminate for all purposes as of said date.

2. It is understood that this option covers stock of the company which will operate, as a certificated air carrier, the routes now operated by Southwest Airways Company and West Coast Airlines, Inc. (except for such routes as may be eliminated but including any new

routes that may be applied for and approved by the Civil Aeronautics Board) whether said certificated air carrier operates as Southwest Airways Company or under any other name; Southwest Airways Company agrees to take such corporate action, including action by its board of directors and its stockholders, as will legally bind it or its successor (including any new company that may be formed to operate said routes) to carry out the terms of this Option Agreement.

3. Certified copy of resolution of the board of directors of Southwest Airways Company approving and ratifying the execution of this Option Agreement by its President will be delivered to said Nick Bez within thirty (30) days from the date hereof and like evidence of stockholders approval thereof will be furnished said Nick Bez following the next stockholders meeting of Southwest Airways Company.

4. If, prior to the exercise of this option, a recapitalization of Southwest Airways Company (including a split-up of its shares) is effected, the number of shares which said Nick Bez shall be entitled to purchase hereunder and the price to be paid therefor shall be adjusted following said recapitalization, so that he will not be adversely affected thereby.

5. Southwest Airways Company agrees, that it will not grant any stock options to its President or to the Chairman of its Board; stock options to other employees may be given, however, under appropriate corporate action whenever the giving of such options serves corporate purposes.

6. This agreement is the sole agreement entitling Nick Bez to purchase from Southwest Airways Company stock of Southwest Airways Company pursuant to options or warrants, and supersedes and is in place of any and all other understandings and agreements with respect thereto.

Dated this 3rd day of December, 1949.

NICK BEZ

By /s/ Nick Bez
Nick Bez, An Individual

SOUTHWEST AIRWAYS COMPANY

By /s/ John H. Connolly
President and Director

/s/ A. W. Johnson
Director

SOUTHWEST AIRWAYS COMPANY

/s/ Floyd L. Hendrickson
Director

/s/ E. Allenberg
Director

/s/ Daniel T. O'Shea
Director

/s/ Harry S. White
Director

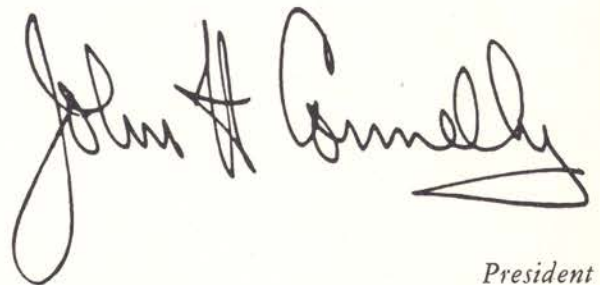
Southwest Airways Company
(AN ARIZONA CORPORATION)



As a result of the merger application mentioned above, the Civil Aeronautics Board reopened the case involving the Southwest certificate renewal and the United Airlines suspension issues in order to determine the effect of the merger on these points. A decision in this case is expected to be made by the Civil Aeronautics Board in the near future.

On December 19, 1949, the Company was awarded a certificate for local service operations between Los Angeles, California and Phoenix, Arizona via seven intermediate points. After several postponements by the Civil Aeronautics Board of the date of activation of this route, the Board on March 10, 1950 rescinded the operating certificate for this route segment because of certain legal complications which the Board

felt required reconsideration. The Board then reopened the "Additional California-Nevada Service Case" for rehearing and redetermination of the service requirements between Los Angeles and Phoenix. In this reopened case, the public hearing of which was completed in February 1951, Southwest is applying for authority to serve Santa Ana-Laguna Beach, Oceanside, San Diego, El Centro, Indio, Blythe, Palm Springs, Banning-Beaumont, San Bernardino-Riverside, Ontario-Pomona, California, and Yuma, Ajo, and Phoenix, Arizona. There are two other air carrier applicants in this case, and it is not possible at this time to determine whether the Board will authorize any new local service in this area or when the decision will be rendered.

A handwritten signature in cursive script, reading "John A. Connelly". The signature is written in dark ink and is positioned above the title "President".

President

BALANCE SHEET

Southwest Airways Company
(AN ARIZONA CORPORATION)



ASSETS

December 31

1950 1949

Current Assets:

Cash in banks and on hand	\$ 299,569.43	\$ 293,775.80
U. S. Government securities, at cost	299,473.84	300,075.23
Accounts receivable:		
U. S. Post Office Department, for carrying mail	168,705.25	115,117.36
Traffic and agents	123,339.79	68,246.62
Miscellaneous, less allowances for possible losses in collection (1950—\$1,248.58; 1949— \$1,511.46	29,238.12	20,795.92
Employees	1,323.08	1,081.07
Inventories of motor fuels, lubricants and materials and supplies, at approximate cost	80,424.77	87,510.63
	<u>\$1,002,074.28</u>	<u>\$ 886,602.63</u>

Investments in Stocks of Service

Organizations, at cost	\$ 511.00	\$ 511.00
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Property and Equipment, at cost

Flight equipment	\$1,183,974.30	\$1,008,468.26
Ground and shop equipment	107,652.49	91,591.10
Leasehold improvements	120,697.22	103,299.31
Other	94,064.48	134,592.02
	<u>\$1,506,388.49</u>	<u>\$1,337,950.69</u>
Less—Accumulated depreciation	1,136,448.33	1,056,609.54
	<u>\$ 369,940.16</u>	<u>\$ 281,341.15</u>

Deferred Charges:

Prepaid insurance and taxes	\$ 33,027.23	\$ 28,298.03
Extension and development expense	72,597.78	37,253.26
Engine overhaul in process, etc.	25,437.21	19,704.68
	<u>\$ 131,062.22</u>	<u>\$ 85,255.97</u>
	<u>\$1,503,587.66</u>	<u>\$1,253,710.75</u>

LIABILITIES

December 31

1950 1949

Current Liabilities:

Accounts payable	\$ 196,825.63	\$ 129,141.62
Taxes collected or withheld from others	37,424.94	25,161.98
Accrued expenses	41,966.09	53,804.90
Transportation sold, not yet used or refunded	13,305.27	8,672.88
Federal taxes on income (estimated—Note D)	94,013.51	53,000.00
	<u>\$ 383,535.44</u>	<u>\$ 269,781.38</u>

Reserve for Aircraft Engine Overhaul

	\$ 49,099.94	\$ 53,427.14
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Capital Stock and Surplus:

Common stock:

Authorized, 10,000,000 shares of 50c par value per share (Note C)		
Issued.		
December 31, 1949—647,660 shares		\$ 323,830.00
December 31, 1950—651,610 shares	\$ 325,805.00	
Paid-in surplus (Note C)	231,275.50	228,273.50
Earnings retained for use in the business, per accompanying statement (Note B)	513,871.78	378,398.73
	<u>\$1,070,952.28</u>	<u>\$ 930,502.23</u>
	<u>\$1,503,587.66</u>	<u>\$1,253,710.75</u>

STATEMENT *of* INCOME *and* EARNINGS
 RETAINED *for* USE *in* the BUSINESS

December 31

	1950	1949
<i>Operating revenues:</i>		
Passenger	\$1,139,969.14	\$1,059,557.84
Mail	943,888.17	1,249,992.46
Express	18,876.53	14,135.60
Freight	43,925.17	36,007.30
Charter and special revenue	67,086.39	38,887.36
Total operating revenue	<u>\$2,213,745.40</u>	<u>\$2,398,580.56</u>
<i>Operating expenses:</i>		
Flying operations	\$ 609,883.90	\$ 601,064.56
Flight equipment maintenance—direct	173,418.87	265,073.65
Depreciation—flight equipment	56,928.45	293,193.55
	<u>\$ 840,231.22</u>	<u>\$1,159,331.76</u>
Ground operations	333,900.90	334,936.72
Ground and indirect maintenance	142,953.25	124,316.64
Passenger service	90,807.50	85,629.60
Traffic and sales	261,842.13	237,491.75
Advertising and publicity	86,954.44	70,700.73
General and administrative	186,866.23	187,603.78
Depreciation—ground equipment	25,327.30	63,867.14
Total operating expense	<u>\$1,968,882.97</u>	<u>\$2,263,878.12</u>
Operating profit	<u>\$ 244,862.43</u>	<u>\$ 134,702.44</u>
<i>Other income:</i>		
Discounts earned	\$ 1,603.14	\$ 1,390.96
Interest	3,612.44	671.17
Other	6,991.98	8,435.13
	<u>\$ 12,207.56</u>	<u>\$ 10,497.26</u>
<i>Other deductions:</i>		
Interest	\$ 1,272.82	\$ 3,427.17
Extension and development	21,932.32	1,338.93
Other	5,859.30	6,211.98
	<u>\$ 29,064.44</u>	<u>\$ 10,978.08</u>
	<u>\$ 228,005.55</u>	<u>\$ 134,221.62</u>
<i>Provision for estimated federal taxes on income</i>	92,532.50	53,078.45
Net income for year	<u>\$ 135,473.05</u>	<u>\$ 81,143.17</u>
<i>Earnings retained for use in the business,</i> <i>beginning of year</i>	<u>378,398.73</u>	<u>297,255.56</u>
Earnings retained for use in the business, end of year	<u>\$ 513,871.78</u>	<u>\$ 378,398.73</u>

NOTE A The Company is operating under an amended certificate of public convenience and necessity, issued by the Civil Aeronautics Board, the authority contained in which is continued beyond the expiration date therein prescribed (November 21, 1949) by the Administrative Procedure Act pending final disposition by the Board of applications by the Company for extension of its operating authority. The Civil Aeronautics Board examiner has recommended that the Board extend the Company's certificate to September 30, 1954.

NOTE B On April 6, 1950, a joint application was filed with the Civil Aeronautics Board by the Company and West Coast Airlines, Inc., requesting approval of a plan of merger of these companies, under which plan Southwest Airways Company would be the survivor corporation. The hearing before the Civil Aeronautics Board with respect to the merger plan has been completed but a decision thereon has not as yet been rendered. Under the terms of the plan of merger, no dividends or other distributions to stockholders may be made by either party thereto without prior written consent of the other.

NOTE C Stock options have been granted to certain officers and employees of the Company; these options, which entitle the holders to purchase 19,800 shares of unissued common stock of the Company at \$1.26 per share, expire on December 31, 1952, except that an option in respect of 375 shares held by a former employee expires on April 10, 1951. Similar options on 3,950 shares were exercised during 1950 and the proceeds of \$4,977 was credited \$1,975 to capital stock account and \$3,002 to paid-in surplus. A contingent stock option is also outstanding, which entitles the holder to purchase 32,500 shares of unissued common stock of the Company at \$1.50 per share. This option may not be exercised until thirty days after the date the Civil Aeronautics Board approves the proposed merger, mentioned in Note B, and continues in effect for five years thereafter. In the event such approval is not obtained on or before January 1, 1953, this option will expire.

NOTE D The Company's federal income tax returns for the taxable periods to and including the year ended December 31, 1947 have been examined by a Revenue Agent and additional taxes proposed to be assessed have been provided for in the accounts. In the opinion of officials of the Company the liability for federal income taxes as shown in the accounts is sufficient to provide for all federal income tax liabilities applicable to all open years; however, the liabilities for these years cannot be finally determined until the related returns have been reviewed by the Bureau of Internal Revenue.

PRICE, WATERHOUSE & CO.

351 CALIFORNIA STREET
SAN FRANCISCO 4
February 21 1951

To the Board of Directors of
Southwest Airways Company

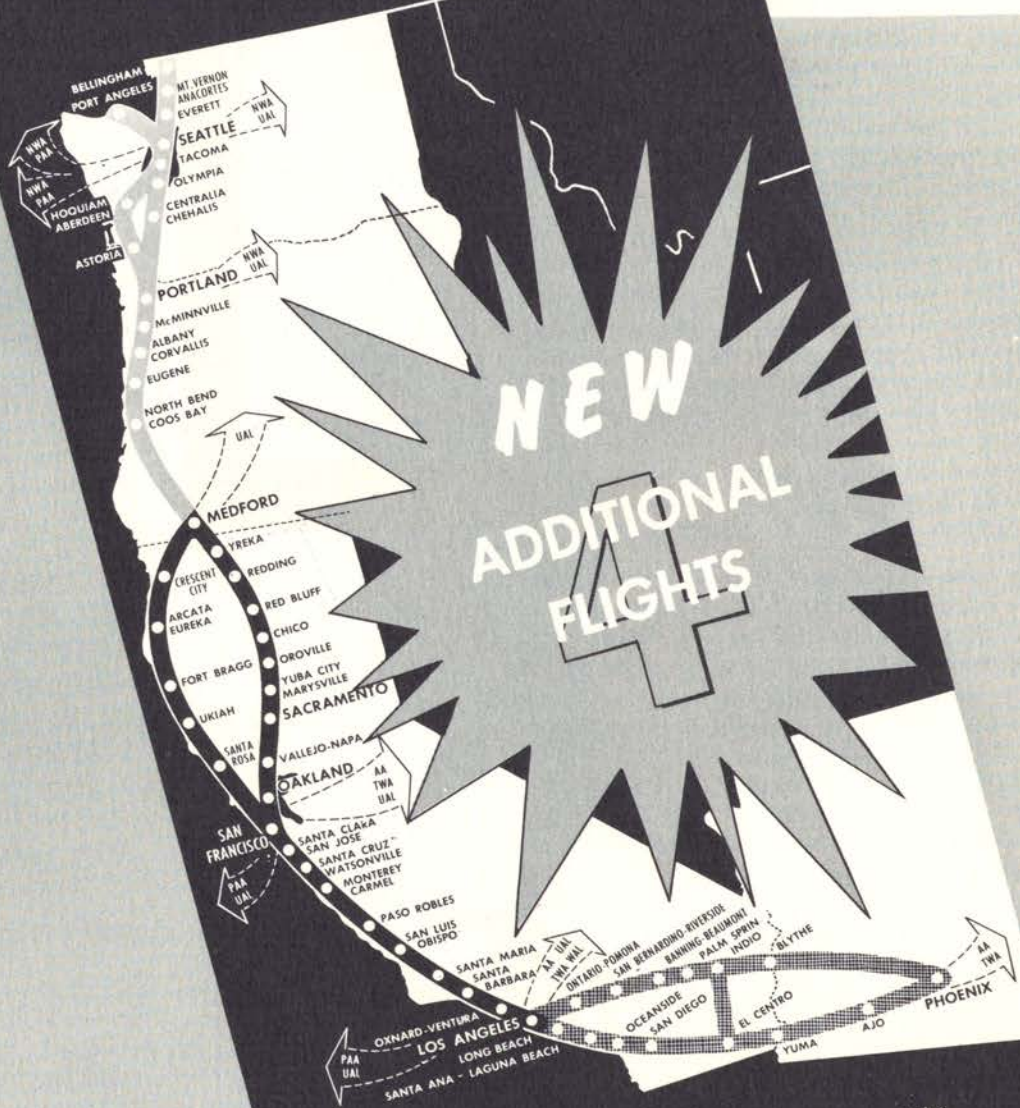
In our opinion, the accompanying financial statements, together with the explanatory notes thereto, present fairly the position of Southwest Airways Company as of December 31 1950 and the results of its operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. Our examination of such financial statements was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. It was not practicable to confirm the amount receivable from the United States Post Office Department, as to which we have satisfied ourselves by means of other auditing procedures.

Price Waterhouse & Co.

NOTE E From the commencement of flight operations in December 1946 to December 31, 1949, sufficient depreciation had been provided from income to reduce the net carrying value of flight equipment to an amount approximating residual value. The depreciation provided for flight equipment since January 1, 1950 consists primarily of the amortization of recent major air frame overhauls, conversions and current additions. Because of the foregoing, the depreciation provided during 1950 for flight equipment was \$236,000 less than the amount provided during 1949. Recognizing that the principal flight equipment was substantially depreciated, and therefore the Company required less reliance on mail pay, the Civil Aeronautics Board established a lower rate of pay for carrying mail, effective January 1, 1950; this decrease in mail rate largely accounts for the reduction of approximately \$305,000 in mail revenue for 1950 as compared with 1949.

COMPLETE TIMETABLE

Southwest Airways



LEGEND

- Service now provided by West Coast Airlines will be operated by Southwest Airways upon approval by Civil Aeronautics Board of merger of West Coast and Southwest.
- ▨ Service by Southwest Airways between Los Angeles and Phoenix pending C. A. B. action.



Aviation Safety Award

The National Safety Council presented the above award to Southwest in 1950 in recognition of the Company's continuously safe operations through 1949. A similar award was earned by the Company for the year 1950.



Southwest Airways

C O M P A N Y

