

Decision No. 9910

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA

ORIGINAL

In the matter of the application of Southwestern Home Telephone Company, a corporation, for an order authorizing said company to establish certain increased rates, tolls, rentals and charges.

Application No. 6398.

Max Thelen for applicant.
 F. A. Leonard, City Attorney, and
 A. E. Brock, President, Board of
 Trustees, for City of Redlands.
 B. N. Pratt, William Collier and
 S. H. Burton, for subscribers of
 Elsinore and vicinity.
 W. H. Panson and Burdette Raynor,
 for Hemet Chamber of Commerce.
 A. E. McDowell, for subscribers in
 Little Lake District.

BRUNDIGE, Commissioner.

O P I N I O N

Southwestern Home Telephone Company, applicant in this proceeding, owns and operates telephone exchanges serving the cities and towns of Redlands, San Bernardino County, and Banning, Beaumont, Elsinore, Hemet, Perris, San Jacinto and Temecula, Riverside County, and adjacent territory. The application as originally filed sets forth that the rates now in effect do not yield revenue sufficient to meet actual and reasonable maintenance and operating expenses, together with a reasonable depreciation annuity and to yield a fair return on the fair value of the property used and useful in the public service. The Commission is asked to make its order authoriz-

ing applicant to establish rates set forth in the application amounting to an increase of 33 1/3 % over the present rates.

Public hearings were held in Redlands on April 5th and in Los Angeles on July 1st, 1921.

At these hearings applicant filed a number of exhibits, among which are statements of claimed investment together with statements of receipts and expenditures for the year 1920 and of estimated receipts and expenditures for the year 1921 under the proposed rates, the purpose of these exhibits being to show the necessity for increasing the present rates. The investment claimed by applicant is based on an inventory prepared by it during the year 1914 to which net additions to December 31, 1920 have been added. The engineering department of the Commission has also made and presented a valuation report in which the valuation is found considerably lower than that claimed by the applicant.

At a conference held on November 26, 1921, between representatives of the applicant and of the Railroad Commission, it was agreed that the company and the Commission's engineering department should each submit a statement setting forth their different views relative to the valuation of the applicant's property. It was also agreed at this conference by reason of the fact that the company and the Commission's engineering department do not agree as to what the fair value of this property is and particularly since applicant admits that it will be unable to establish and collect rates sufficient to yield a fair return on what it considers a fair valuation of its property that it would submit modified schedules in lieu of those originally set out in its application.

The statements and modified schedules have since been submitted and the matter is now ready for decision.

The valuation found by the engineering department of the Commission and shown by the valuation report previously referred to was \$382,297.00. This valuation is on an historical reproduction cost undepreciated. After conference with representatives of the company, the Commission's engineering department has made corrections to the original figure resulting from certain additions and deductions, bringing the original valuation up to \$392,148.00 as shown by the engineering department's statement above referred to. The company's statement of comparable items shows a valuation of \$491,735.51 to which is added an item of \$12,761.00 for materials and supplies and a further item of \$7,000.00 for working capital, making a total of \$511,496.51, which is the amount now claimed by applicant as a proper rate base. In comparison the items appearing in these two statements are as follows:

	<u>Statement of Engr. Dept.</u>	<u>Statement of Company</u>
Physical Property	\$ 374,442.00	\$ 418,860.86
Development Expenses	3,883.00	60,612.00
Franchises, Contracts and Rights of Way	1,062.00	12,262.65
Materials and Supplies	12,761.00	12,761.00
Working Capital	—	7,000.00
Totals, -	\$ 392,148.00	\$ 511,496.51

The amounts shown in the statements of the engineering department are below those of the company in the items and to the extent following:

Physical Property	\$ 44,418.86
Development Expenses	56,729.00
Franchises, Contracts and Rights of Way	11,200.65
Working Capital	7,000.00
Total, -	\$119,348.51

This difference in valuation of physical property arises chiefly from the fact that the company's appraisal is based on unit costs representing average prices of labor and material prevailing in 1914, the year during which its plant was inventoried, while those applied by the Commission's engineers are average historical costs obtained in most cases from the company's voucher records.

The amount claimed by the company for development expense, according to its statement, is the amount which has been carried on its books. The amount allowed in the engineering department's statement for this item is 1% of the total of physical property, franchises, contracts and rights of way, and materials and supplies.

The amount claimed by the company for franchises, contracts and rights of way, as its statement shows, is also the amount appearing on its books for these items. It appears on the statement of the Commission's engineers that there are two items included in the company's claim as follows: one item of \$1,000.00, covering a contract for the joint occupancy of poles entered into during the year 1914 and growing out of a controversy between the applicant and the Southern Sierras Power Company, concerning the use of certain streets for the location of their respective lines; the other, an item of \$10,200.00, covering a contract with The Pacific Telephone and Telegraph Company for the purchase of property from The Pacific Company by the applicant and for the interexchange of service between the contracting parties. In each of these two transactions the expenses involved are capitalized by the company in its statement, and in connection with the latter transaction, there appears an issue of \$10,000.00 par value of bonds to Mr. C.D. Rolie

for his services in this transaction, this amount being included as a capital charge in the company's claim. The sum claimed by the company for these two contracts \$11,200.00 is not included in the statement of the Commission's engineers.

The amount claimed by the company for working capital, \$7,000.00, is an amount which it claims represents substantially one month's operating expenses to which it urges it is entitled for working capital. A statement of the Commission's engineers disallows this item on the theory that since the company collects its rates in advance and the revenues thus collected being in excess of its monthly operating expenses it is not entitled to any claim for working capital.

I do not consider it necessary for the Commission to come to a decision in this proceeding on the merits of the disputed items of the valuation. It may be stated, however, that the valuation of this property was made by the Commission's engineering department under the same methods and following the same general rules as have been adopted and approved by the Commission in all public utility valuations for rate making purposes. There is no doubt, I believe, that the Commission would disallow, if the matter had to be decided, the capitalized value of the contract with The Pacific Telephone and Telegraph Company (since the expenses arising from that contract to applicant are allowed in operating expenses) and would also disallow, for rate making purposes, the item of development expense. These matters do not appear to be of controlling importance, however, because as will be shown hereunder the rates proposed will produce for applicant a fair return on a reasonable investment or valuation figure.

The rates at present in effect and those which the applicant now desires to make effective, in so far only as increases in present rates now being sought are involved, are as follows:

	<u>Business Service</u>		<u>Residence Service</u>	
	<u>Monthly Rate</u>		<u>Monthly Rate</u>	
	<u>Present</u>	<u>Proposed</u>	<u>Present</u>	<u>Proposed</u>
	<u>Wall Set</u>	<u>Wall Set</u>	<u>Wall Set</u>	<u>Wall Set</u>
Redlands Exchange				
1-Party Line	\$4.25	\$5.25	\$3.25	\$4.00
2-Party Line	3.75	4.50	2.50	3.00
4-Party Line	3.75	4.50	2.50	3.00
8-Party Line	3.75	4.50	2.50	3.00
Suburban Line	--	--	3.50	4.00
Employees	--	--	1.50	1.75
San Jacinto and Hemet Exchanges				
1-Party Line	\$3.25	\$4.00	\$2.75	\$3.00
4-Party Line	2.75	3.50	(2.25)	(2.50)
8-Party Line (Block 2)	2.75	3.50	(Block 1)	(Block 1)
" " " (" 3)	3.00	3.75	2.25	2.50
" " " (" 4)	3.25	4.00	2.50	2.75
" " " (" 5)	3.50	4.25	2.75	3.00
" " " (" 6)	3.75	4.50	3.00	3.25
Mountain Lines				
(Oak Grove & Idylwild)	\$3.75	\$4.50	\$3.25	\$3.50
Winchester Line	3.25	4.00	2.75	3.00
Employees	--	--	1.50	1.75
Perris Exchange				
1-Party Line	\$3.25	\$3.75	\$2.75	\$3.00
4-Party Line	2.75	3.25	2.25	2.50
8-Party Line (Block 2)	2.75	3.25	2.25	2.50
" " " (" 3)	3.00	3.50	2.50	2.75
" " " (" 4)	3.25	3.75	2.75	3.00
Suburban Line (Block 5)	--	--	2.75	3.00
Employees	--	--	1.50	1.75
Elsinore Exchange				
1-Party Line	\$3.25	\$3.75	\$2.75	\$3.00
4-Party Line	2.75	3.25	2.25	2.50
8-Party Line (Block 2)	2.75	3.25	2.25	2.50
" " " (" 3)	3.00	3.50	2.50	2.75
" " " (" 4)	3.25	3.75	2.75	3.00
Employees	--	--	1.50	1.75

For desk sets in place of wall sets add 25 cents per month to each of the rates quoted above.

The rates quoted above are gross monthly rates. Discounts from each of the above rates for advance payment are al-

lowed as follows:

For monthly payments made on or before the 10th day of the current month, \$0.25.

For quarterly payments in advance on or before the 10th day of the first month of the quarter for which payment is made, \$1.00.

If paid annually in advance, \$4.50.

Applicant has presented with its proposed schedule of modified rates shown above an estimate of the increase in gross revenues which it would derive for these rates over actual gross revenues for the year 1920, - this estimate being based on the stations actually in service on November 1, 1921. The amount of revenue increase shown by this estimate after deducting $1\frac{1}{2}\%$ for temporary loss of subscribers and for regrading of subscribers following the proposed increase in rates is \$14,514.00. It does not, however, take into account any increase in revenue through possible growth of the business. Undoubtedly there should be some allowance made for the purposes for which this $1\frac{1}{2}\%$ has been deducted but consideration should also be given to such increases in revenue as may result from a growth in business. Conditions are such in the territory in which applicant operates that in our opinion the growth in business to be expected will be limited, and this view is supported by applicant's experience in former years. It seems reasonable to assume, however, that the growth in business will at least be sufficient to offset the temporary loss of $1\frac{1}{2}\%$ for which applicant has made allowance in its estimate. On this basis the amount of revenue increase resulting from the proposed rates would be \$16,059.00.

The actual gross revenues and operating expenses exclusive of depreciation reported by the company for the year 1920 were \$111,918.36 and \$74,261.92 respectively. During the four months of the year from September 1 to December 31, 1920, operators' salaries were higher than during the first eight months of the year. This item of operating expense will therefore be greater in 1921 than it was in 1920. The amount paid out for taxes in 1921 is also greater than the amount paid out during 1920. Estimated operating expenses for 1921, taking 1920 expenses as a basis after allowing for necessary increases in operators' salaries and taxes and after certain deductions (consisting of an adjustment in charges to accidents and damages and to automobile hire) to which applicant has agreed have been made will amount to \$74,190.65. After allowing one-half of 1% of gross revenues for uncollectible revenues and adding to operating expenses $3\frac{3}{10}\%$ of the value of the depreciable property found by the Commission's engineers for depreciation annuity, this addition of \$16,059.00 for gross revenues would leave a net income of \$40,245.83. This amount would be equivalent to a return slightly in excess of 10% on the valuation found by the Commission's engineers, plus \$7,000.00 for working capital, or $7\frac{7}{10}\%$ on the company's valuation.

On the basis above referred to, as to operating expenses and depreciation, the rates hereinafter suggested should yield a return of 8.24% on the valuation found by the Commission's engineers, had the Commission allowed the company's claim for \$7,000.00 for working capital, or 6.4% on the company's valuation. Under the circumstances in this case, it is our opinion that rates which will yield this amount of net return are reasonable.

The Rates Suggested Are as Follows:

	Business Service Monthly Rate <u>Wall Set</u>	Residence Service Monthly Rate <u>Wall Set</u>
Redlands Exchange		
1-Party Line	\$5.00	\$3.75
2-Party Line	4.25	2.75
4-Party Line	4.25	2.75
8-Party Line	4.25	2.75
Suburban Line	--	3.75
Employees	--	1.75
San Jacinto and Hemet Exchanges		
1-Party Line	\$3.75	\$2.75
		(Block 1)
4-Party Line	3.25	(2.25)
8-Party Line (Block 2)	3.25	2.25
" " " (" 3)	3.50	2.50
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Mountain Lines		
(Oak Grove & Idylwild)	\$4.25	\$3.25
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Employees	--	1.75
Perris Exchange		
1-Party Line	\$3.50	\$2.75
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Suburban Line (Block 5)	--	2.75
Employees	--	1.75
Elsinore Exchange		
1-Party Line	\$3.50	\$2.75
4-Party Line	3.00	2.25
8-Party Line (Block 2)	3.00	2.25
" " " (" 3)	3.25	2.50
" " " (" 4)	3.50	2.75
Employees	--	1.75

For desk sets in place of wall sets add 25 cents per month to each of the rates quoted above.

The following order is recommended:

O R D E R

Southwestern Home Telephone Company having applied to the Railroad Commission for an order authorizing said company to establish certain increased rates, tolls, rentals and charges; public hearings having been held; the case having been submitted, and the matter being now ready for decision,

IT IS HEREBY ORDERED that Southwestern Home Telephone Company be and it is hereby authorized to publish and file with this Commission within thirty (30) days from the date of this order and to make effective on and after January 1, 1922 the schedule of rates set forth in the opinion preceding this order as suggested rates, subject to the conditions following:

1. The rates herein authorized shall be subject to the same discounts for advance payment as are at present in effect.
2. All of the rates and all of the rules and regulations affecting rates now in effect other than those provided for in the schedule herein authorized shall be continued in effect until or unless otherwise authorized by the Commission.
3. Efficient and adequate telephone service shall at all times be provided to all subscribers.

The foregoing opinion and order are hereby approved and ordered filed as the opinion and order of the Railroad Commission of the State of California.

Dated at San Francisco, California, this 21st day of December, 1921.

H. B. Benedict
H. B. Benedict
Irving Martin
Charles H. Knicker
H. B. Benedict
Commissioners.