Decision No. 38514

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Investigation and Suspension by the Commission on its own motion of reduced rates published by The Atchison, Topeka and Santa Fe Railway Company, Southern Pacific Company and Pacific Freight Tariff Bureau, J. P. Haynes, Agent, for the transportation of liquors, alcoholic, carloads, between San Francisco, Oakland and other points on the one hand and Los Angeles and other points on the other hand.

ORIGINAL

Case No. 4473

CRAEMER, COMMISSIONER:

Appearances

James E. Lyons, for Southern Pacific Company and Pacific Freight Tariff Bureau.
G. E. Duffy and George T. Hurst, for The Atchison, Topeka and Santa Fe Railway Company.
Edward M. Berol, for Truck Owners Association of California.
Carl R. Schulz, for The Kent Lines, Inc.

O P I N I O N

This is an investigation instituted by the Commission on its own motion for the purpose of inquiring into the lawfulness and propriety of certain reduced rates published by The Atchison, Topeka and Santa Fe Railway Company, Southern Pacific Company and Pacific Freight Tariff Bureau (hereinafter termed the rail lines) for the transportation of shipments of alcoholic liquor in rail carload service between railheads in San Francisco and Oakland on

the one hand and railheads in Los Angeles and certain adjacent points on the other hand.[1] These rates were suspended by the Commission upon consideration of petitions filed by The Truck Owners Association of California, a nonprofit corporation composed of highway carriers engaged in transporting property over the public highways of the state, and by The Kent Lines, Inc., a radial highway common carrier and highway contract carrier operating between the metropolitan areas of San Francisco and Los Angeles, alleging that said rates were unjust, unreasonable, insufficient and discriminatory, and in violation of Sections 13, 13½, 19, 32 and 32½ of the Public Utilities Act.

Public hearings were held at San Francisco on April 17, and May 1, 1940. At the outset, respondents took the position that it was not incumbent upon the rail lines to justify the suspended rates initially and that the burden of proving those rates unlawful was upon the parties who sought the suspension. It was agreed, however, that the rail lines would proceed first with the introduction of evidence.

The applicable rates for the transportation of alcoholic liquor in carload service by railroad between railheads in San Francisco and Oakland on the one hand and railheads in Los Angeles on the other hand, are 35 cents,[2] minimum weight 40,000 pounds. The suspended rates are 28 cents, minimum weight 30,000 pounds. The minimum highway carrier rates for transportation of alcoholic liquor in pickup and delivery service between these points are 37 cents,

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[1] The reduced rates involved are published in Item No. 5980-D, Atchison, Topeka and Santa Fe Railway Company Tariff No. 12375-O, C.R.C. No. 690; Item 5886-C, Southern Pacific Company Tariff No. 730-D, C.R.C. No. 3353; and Item No. 10715-C, Pacific Freight Tariff Bureau Tariff No. 30-N, J. P. Haynes, Agent, C.R.C. No. 592 (L. F. Potter series).

[2] Rates are stated in cents per 100 pounds.

minimum weight 30,000 pounds, these rates having been established by this Commission as minimum for this transportation by Decision No. 31606, of December 27, 1938, as amended, in Case No. 4246, in re - Rates of All Common and Highway Carriers. For transportation between railheads, however, the aforesaid order permits highway carriers to meet the rail carload rate, subject to certain added charges for services performed by highway carriers which are not rendered in carload rail service.[3] The rail pickup and delivery rate for the transportation involved is 52½ cents, minimum weight 20,000 pounds, and is not here sought to be disturbed. Said Decision No. 31606, as amended, permitted rail carriers, including respondents, to publish rates for pickup and delivery service equivalent to the rates established for corresponding service by highway carriers, but respondents have not taken advantage of that permission.

While the reduced rates were published to apply in both directions, the evidence dealt almost exclusively with southbound traffic having its origin at San Francisco. An assistant general freight agent of the Southern Pacific Company stated that two distillers located at San Francisco, namely, Schenley Distilleries, Inc., and Hiram Walker & Sons Western, Inc., each ship approximately 30,000 pounds of alcoholic liquor into Los Angeles daily. Although both of these plants are located on railroad spur tracks, he said, and

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[3] Carload rail service ordinarily includes spotting the car at the shipper's place of business for loading and the consignee's place of business for unloading. The shipper, however, is required to load and the consignee to unload the car at their own expense. Forty-eight hours free time is ordinarily allowed for loading and a like time for unloading. When observing the rail rate, highway carriers are permitted under existing orders to load and unload the shipment without additional charge, provided the property is not brought from or carried to a point more than twenty-five feet distant from the carriers' equipment. For other accessorial services not performed by rail carriers, highway carriers are required to assess an additional charge of $1.00 per man per hour.

although a considerable portion of the traffic is destined to railhead points, only eight shipments were made via the Southern Pacific Company during the year 1939. The balance was transported by highway carriers, with the exception of a small number of cars which moved by another rail carrier.. The small volume of traffic moving by rail, the witness asserted, was attributable mainly to the slower service afforded by rail carriers as compared to truck service, to the fact that highway carriers rendered split delivery service on occasion, and to the fact that highway carriers permitted the painting of advertising signs on their equipment. Another contributing factor, he stated, was that loading facilities at the shipper's plants were so arranged that it was inconvenient and more costly to the shippers to use rail transportation. The witness estimated the difference in the value of the service which his company could give as compared to the service of highway carriers to be at least 5 cents per 100 pounds.

Respondent's witness stated further that consideration had first been given to the publication of a pickup and delivery rate equal to or lower than that maintained by highway carriers, but that the shippers had declined to promise rail carriers any traffic under a pickup and delivery rate. The 28-cent rate was decided upon in consideration of estimates that the cost of picking up shipments at the shipper's places of business and bringing them to the rail depot in truck equipment, of delivering them in truck equipment from the destination depot, and of handling them over the freight platform at origin and destination, amounted to approximately 13 cents per 100 pounds. He asserted, moreover, that the rails could have as well afforded to establish a rate of 24 cents per 100 pounds for carload service, which would have been the equivalent of a rate of 37 cents for pickup and delivery service, the margin between the two rates being represented by the 13 cents per 100 pounds handling cost. The proposed rate of 28 cents in-

stead of 24 cents, the witness testified, was decided upon for the reason that a rate of that volume was already in effect for transportation of wine and brandy from the intermediate points of San Jose and Stockton to Los Angeles, which respondents did not desire to break down by the publication of lower rates from a more distant point. Assertedly, the shippers had agreed to divert to the rails a substantial amount of tonnage if the 28-cent rate were established.

Another factor influencing the 28-cent rate was said to be that the rate being charged for draying alcoholic liquor from team tracks in Los Angeles to consignees was 9 cents, which, when added to the proposed 28-cent rate, would produce a total rate equal to the through truck rate. The witness stated, however, that he had no expectation that the 28-cent rate would actually attract any material amount of the traffic destined to off-rail points.

Exhibits were introduced by the Southern Pacific Company's witness, purporting to show that the proposed rate would produce earnings comparing favorably with earnings returned on various other commodities transported between San Francisco and Los Angeles in carload lots. However, no showing was made as to the similarity of the commodities compared to those here in issue, from the standpoint of value, ease of handling, or transportation conditions.

An assistant general freight agent of The Atchison, Topeka and Santa Fe Railway Company confirmed the foregoing testimony. He stated that during the year 1939 his company received only four carloads of alcoholic liquor from San Francisco to Los Angeles.

A cost engineer in the employ of the Southern Pacific Company introduced an exhibit designed to show the estimated cost of transporting alcoholic liquor in carload rail service between San

Francisco and Los Angeles, based upon the so-called "Eight Point Formula." Briefly, the witness used as a starting point the freight proportion of the operating expenses incurred by the Southern Pacific Company, Pacific Lines, (embracing territory Portland and south and El Paso and west) for the year 1939. He deducted from this amount an amount based on the per cent of operating expenses assumed to be applicable to various accounts which were considered not to vary with the volume of traffic handled. These unvariable expenses were deducted from the total to obtain the direct or variable expenses. The direct expenses were then apportioned to eight work units, based upon statistical analysis and judgment.[4] The direct expense of hauling alcoholic liquor between San Francisco and Los Angeles was then estimated by considering the average size of trains moving over the districts involved and the number of carloads of alcoholic liquor which would be handled in an average size train. Indirect expenses were allocated to this particular traffic on what the witness termed a "pro rata" basis; that is, on the assumption that each unit of traffic handled, regardless of type or kind, would pay the same proportion of these expenses. The direct costs estimated by this witness were 13.13 cents per 100 pounds for a net load of 30,000 pounds and 11.94 cents per 100 pounds for an estimated average weight load of 33,750 pounds. The direct costs plus a pro rata share of the indirect expenses, but excluding taxes and return on investment, were said to be 17.65 cents per 100 pounds and 16.05 cents per 100 pounds for 30,000 pound and 33,750-pound loads, respectively.

The San Francisco plant of Schenley Distilleries, Inc. is

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[4] The work units used were designated as "yard engine hours," "locomotive miles," "locomotive ton miles," "train miles," "gross ton miles," "net ton miles," "car miles" and "revenue carloads."

served by the State Belt Railroad, and the Los Angeles warehouse of Hiram Walker & Sons is located on spur track facilities served by the Santa Fe. The cost witness acknowledged that the figures shown did not include the State Belt Railroad's switching charge of $4.00 per car or the division of revenue accruing to the Santa Fe for handling shipments in terminal switching service at Los Angeles of 1½ cents per 100 pounds, subject to a minimum charge of $6.20 per car. Moreover, he was unable on cross-examination to give an estimate of the proportion of taxes which should be borne by the traffic here involved and conceded that no allowance had been made for the failure of passenger operations to pay their share of operating and overhead expenses.

Respondents' cost witness admitted that the allocation of overhead expenses made by him did not necessarily reflect the proportion of all expenses other than direct expenses which were necessary to be borne by the traffic if the rail operation in the aggregate were to be profitable. As a matter of fact, he said, rates two or three hundred per cent in excess of direct costs obtained by use of the formula employed by him would still be insufficient to produce a fully compensatory operation.

Testimony concerning the relative cost to the shipper of loading and unloading a rail car as compared with the cost of loading and unloading a truck was also given by the cost engineer. He estimated the rail loading cost to be $10.75 per car, plus $1.00 for material, although he stated that another estimate based upon a warehouse tariff loading charge produced a cost of $9.22 per car for loading. The rail car unloading cost was estimated as $7.38 per car, based on an average of three lots observed. Truck cost of loading comparable shipments was said to be $4.50 per car. The difference was said to be in excess of 2 cents per 100 pounds in favor

of truck loading, but less than 5 cents per 100 pounds for both loading and unloading. Concededly, these estimates did not take into consideration the fact that, as testified by other witnesses, employees were used in loading rail cars when they were not needed for other work.

Witnesses controlling the local transportation policies of each of the interested shippers testified in support of the proposed rail rate reduction. They explained that truck transportation had been employed almost exclusively in the past due to advantages in economy and flexibility which it offered as compared with railroad service, but stated that if the suspended rates became effective they would rearrange their distribution and allot the rail lines a share of the business moving to destination points served with spur track facilities. According to their testimony, the absence of adequate loading facilities at both of the distilleries had materially handicapped the rail lines. The Schenley representative testified, however, that the proposed rate reduction would make it economically feasible to utilize employees working on night shifts at the Schenley plant for the purpose of loading rail cars without increasing the cost of transportation now experienced by that company. This plan of loading, he stated, would relieve present congestion, although it would increase the loading costs.

In opposition to the proposed reduced rates, a witness for The Truck Owners Association asserted that the proposed rate would not create additional traffic for the rail lines but would only result in depleting existing revenues of both rail and truck transportation. He pointed out that under the provisions of Highway Carriers' Tariff No. 2 highway carriers are permitted to meet rail rates for performing similar transportation services, and that truck operators engaged in hauling liquor shipments had advised that they

would be compelled to reduce their rates if the suspended rate items became effective. The rail lines, he asserted, would be then subject to the same competitive disadvantages which they had testified exist at the present time. The witness also pointed out that such rate would affect adversely the revenue of highway carriers for transportation to off-rail destination points where the rail lines obtained no traffic. In this respect, he called attention to the fact that highway carriers were authorized to combine rail and highway carrier rates for transportation from and to off-rail points and stated that, whereas shipments were currently moving under a rate of 37 cents, minimum weight 30,000 pounds, a combination rate of 32½ cents (28 cents plus the established minimum 4th class rate of 4½ cents) would be available in the event the 28-cent rate became effective for transportation between railhead points.

Protestants' witness asserted, further, that while cost of performing the service undoubtedly was an important factor in determining a reasonable rate for either rail or highway transportation, other factors ordinarily entering into the fixation of rates should likewise be considered. He pointed out that the rails had heretofore substantially reduced alcoholic liquor rates in an effort to attract traffic. Exhibits were submitted tracing the rail rate reductions. They disclose that in January, 1933, a class rate of 84½ cents, minimum weight 30,000 pounds, was in effect for the transportation of alcoholic liquor between the points involved, and that through changes in classification rating and the publication of commodity rates reflecting drastic reductions, the present level of rates was reached. It was also contended by protestants that the proposed rate would produce car mile earnings considerably less than alcoholic liquor could reasonably bear, and which were substantially less than those obtained for transportation from San Francisco and

Los Angeles to various intrastate and interstate destination points. Existing carload rates for varying lengths of haul, generally less than 500 miles, were shown to yield earnings ranging from 30.0 cents to 64.3 cents per car mile, as compared with earnings of 18.0 cents per car mile under the proposed rate.

A certified public accountant called by protestants submitted revenue and income data covering the years 1937, 1938 and 1939, for each of the shippers involved, showing that their earnings had been substantial during each of these years. He also compared wholesale prices of alcoholic liquors with those covering a variety of grocery items accorded comparable classification ratings, the comparisons assertedly showing that alcoholic liquor had a substantially higher value per 100 pounds and, hence, could afford to bear a proportionately larger amount for transportation charges. He did not show the volume of rates under which the grocery items were moving.

The accountant witness also introduced exhibits showing the investment, net railway operating income and rate of return of the Southern Pacific Lines for the year 1925 to 1939, inclusive; the net income or deficit after fixed charges; the earnings per share of stock and the dividend appropriations; and the average rate per ton per mile received on the Southern Pacific system for the years 1925 to 1938.[5]

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[5] Annual figures set forth below are taken from these exhibits:

	1925	1930	1935	1938 *(Deficit)	1939
Rate of Return on Investment	3.75%	2.85%	1.35%	0.97%	1.93%
Net income After Fixed Charges	$35,657,410	$30,684,103	$2,360,199	*$6,829,008	$6,134,574
Earnings per Share of Stock	$9.58	$8.24	$0.62	*$1.81	$1.63
Average Rate per Ton Mile	$0.0138	$0.0132	$0.0111	$0.0110	-

Conclusions

The ultimate issue to be determined in this proceeding is whether or not the suspended rates are in violation of law in any respect. The statutory provisions said by protestants to be particularly relevant are Sections 13, 13½, 19, 32 and 32½ of the Public Utilities Act. It will perhaps be helpful in arriving at a conclusion in this matter to discuss briefly the pertinent portions of these sections.

Sections 13 and 19 have been contained in the Public Utilities Act since its enactment. The former provides that all charges made, demanded or received by any public utility shall be "just and reasonable." A rate may be unreasonable because it is too low as well as because it is too high. (Interstate Commerce Commission vs. C. N. O. & T. P. Ry. Co., 167 U.S. 479, 511.) Whether or not a rate is unreasonably low has been held to depend to a great extent upon whether or not it tends to cast an undue burden on other traffic and whether or not its general effect would be harmful to the public interest. (Anchor Coal Company vs. U. S., 25 Fed. (2nd) 462; Ex Lake Iron Ore, 123 I.C.C. 503.) Section 19 provides that no public utility shall, as to rates, charges, service facilities or in any other respect make or grant any preference or advantage to any corporation or person, or subject any corporation or person to any prejudice or disadvantage. It states, further, that no public utility shall establish or maintain any unreasonable difference as to rates, charges, service, facilities or in any other respect, either as between localities or as between classes of service. Not all differences in rates constitute the discrimination forbidden

by the statute. To be unlawful under this section, the discrimination must be undue, taking into consideration all of the surrounding facts and circumstances. (Application of Southern Pacific Company, et al., for Long and Short Haul Relief, 10 C.R.C. 354, 356.)

Concurrently with the enactment of the Highway Carriers' Act in 1935, Sections 13½ and 32½ were added to the Public Utilities Act. Section 13½ appears particularly applicable to the situation here presented and is quoted in full for ready reference:

> "Nothing herein contained shall be construed to prohibit any common carrier from establishing and charging a lower than a maximum reasonable rate for the transportation of property when the needs of commerce or public interest require. However, no common carrier subject to the jurisdiction of the California Railroad Commission may establish a rate less than a maximum reasonable rate for the transportation of property for the purpose of meeting the competitive charges of other carriers or the cost of other means of transportation which shall be less than the charges of competing carriers or the cost of transportation which might be incurred through other means of transportation, except upon such showing as may be required by the commission and a finding by it that said rate is justified by transportation conditions; but in determining the extent of said competition the commission shall make due and reasonable allowance for added or accessorial service performed by one carrier or agency of transportation which is not contemporaneously performed by the competing agency of transportation."

It will be seen that, under Section 13½, a showing before the Commission and a finding by it that the rate is "justified by transportation conditions" are conditions precedent to the lawful establishment by a common carrier of any rate which is (a) less than a maximum reasonable rate, (b) established for the purpose of meeting the competitive charges of other carriers or the cost of other means of transportation, and (c) less than the charges of competing carriers or the cost of transportation which might be incurred through other means of transportation. In determining "the extent of said competition," the Commission is directed to make due and reasonable allowance for added or accessorial services performed by one carrier or agency of transportation which are not performed by the other.

Whether or not a proposed reduced rate is "justified by transportation conditions," within the contemplation of Section 13½, has been held to depend upon whether or not its effect would redound to the best interest of the general public. In Southern Pacific Company vs. Railroad Commission, 13 Cal. (2nd) 89, the California Supreme Court said, with reference to Section 13½ of the Public Utilities Act:

> "In the language of the statute, the Railroad Commission is charged with the particular duty of 'finding' whether a proposed rate 'is justified by transportation conditions'; that is to say, among other things, weighing and considering each and all of the several and various pertinent facts and elements that should furnish a foundation for a 'finding' or conclusion as to whether the effect of the proposed rate will redound to the best interest of the general public."

Section 32½ was also added to the Public Utilities Act at the time of enactment of the Highway Carriers' Act and, like Section 13½, relates to the relationship between rates of different forms of transport. The section directs the Commission to prescribe such rates as will provide an equality of transportation rates for transportation of property between all competing agencies of transportation, whenever it finds, after hearing, that any rate is lower than a "reasonable or sufficient" rate and is not justified by actual competitive transportation rates of competing carriers or the cost of other means of transportation.

The portion of Section 32 which appears to have application here is paragraph (d) thereof, which was added to the section in 1937. It directs the Commission in any proceeding involving rates of more than one type or class of carriers, to consider all such types or classes of carriers, and, pursuant to the provisions of the Public Utilities Act and the Highway Carriers' Act, to fix as minimum rates applicable to all such types or class of carriers the "lowest of the lawful rates so determined" for any such type or class of carrier. In Southern Pacific Company vs. Railroad Commission, supra, the

Court held that the phrase "lowest of the lawful rates so determined" referred to rates approved by the Commission as not violative of other provisions of the Public Utilities Act.

Summarizing the statutory provisions, under ordinary circumstances reduced rates may be approved only in the event they are not unreasonably low within the contemplation of Section 13; not unduly discriminatory within the meaning of Section 19; not lower than reasonable and sufficient rates under Section 32½; and such that they provide an equality of transportation rates between competing agencies of transportation. Moreover, under Section 32(d) rates higher than "lowest lawful rates" for any of the types or classes of carriers involved should not be required to be maintained. In addition, by virtue of Section 13½, a showing must be made sufficient to support a finding by the Commission that the reductions are "justified by transportation conditions." Viewed in broad perspective, the rate-making provisions of the Public Utilities Act, in addition to insuring against the exaction by common carriers of exorbitant or discriminatory charges, give recognition to the fact that the public itself has a vital interest in the prescrvation of adequate and stable systems of transportation by rail, water and highway and that it is a proper function of regulation to prevent the several forms of transport from engaging in internecine rate wars, contrary to the public interest.

Although the statutory policy of this state is clearly against the continuation of destructive rate cutting practices, it is plainly not intended that this Commission should prevent the railroads from according the public the benefit of reduced rates when they have shown that they can operate more economically than other carriers; that the Commission should base rail rates upon truck costs; or that it should fix minimum rates for all carriers based

upon the costs of the highest cost agency of transportation. Neither truck nor rail carriers are entitled to have an "umbrella" held over them if it appears that their services do not fill an essential public need.

Let us now consider the application of the foregoing general principles and policies to the specific situation here presented.

The record in this proceeding clearly shows that the proposed rates are far less than maximum reasonable rates. Moreover, in view of the fact that those rates are substantially lower than the minimum rates established by this Commission for truck transportation based upon extensive truck cost studies, and are lower than the rates maintained by water carriers, it may reasonably be concluded that the proposed rail rates are "less than the charges of competing carriers or the cost of transportation which might be incurred through other means of transportation." Under the terms of Section 13½, hereinbefore quoted, a rate lower than a maximum reasonable rate and lower than the rates of competing carriers may nevertheless be lawful if the difference properly reflects the cost and value of added and accessorial services performed by one carrier and not by the other. In the instant case, the proposed rail carload rate entitles the shipper to exclusive use of the car but does not include the services of loading and unloading. It does allow 48 hours for loading and a like time for unloading, so that the services can be performed by employees of the shipper and consignee at their convenience. The truck rate, on the other hand, includes the services of the driver in performing or assisting in the performance of loading or unloading, subject to an additional charge of $2.00 per hour for time consumed in excess of twenty minutes per ton. Respondents' cost engineer estimated that the difference in cost to

the shipper of loading or unloading a rail car as compared to the cost of loading or unloading a truck with the driver's assistance amounted to slightly more than two cents per 100 pounds in favor of truck loading or unloading. A differential between rail and truck rates of 4 cents per 100 pounds appears to give ample recognition to this factor. Another accessorial service performed by highway carriers was said to be the carrying of advertising, but no estimate of the cost or value of this service was given. Neither was the greater speed and flexibility of truck service evaluated. Respondent's traffic witness himself evaluated the rail disadvantage from a service standpoint, including the factors of loading, unloading, advertising and speed in transit, to be "at least 5 cents a hundred pounds." Giving due and reasonable consideration to all added and accessorial services performed by truck carriers and not by rail carriers, it cannot be said on this record that the difference of 9 cents between the minimum truck rate and the proposed rail rate is justified by competitive conditions.

Nor is there any suggestion in this record to indicate that a reduction in the present rail rates would fill any commercial need of the particular shippers involved or would redound to the direct benefit of the general public by reason of any reduction in the price of alcoholic liquors. The commodity involved appears to be moving freely by truck under the rates now in effect. There is no claim that traffic not now moving via some form of for-hire transport would commence to move under the reduced rates. The reduced rates appear to have been designed solely in the interest and for the benefit of respondent rail carriers, in reliance upon promises of the interested shippers that they would reciprocate by shipping a portion of the traffic by rail.

If, then, the proposed rate has not been shown to be justified by differences in rail and truck service, will not directly ben-

efit the general public, and if the reduction is not required to meet the needs of commerce, should the suspended rates nevertheless be found to be "justified by transportation conditions?" As pointed out in the opening of this discussion, it is manifestly not the legislative intent that this Commission should "hold an umbrella" over any form of transport - that it should prevent one form of transport from establishing "the lowest lawful rates" merely because other forms of transport would suffer thereby. When, however, rates lower than necessary to provide a reasonable equality of competitive opportunity with other forms of transport are sought to be established, it is the duty of this Commission to see that such rates will, in fact, be fully compensatory to the carrier and that they will not unduly burden other traffic.

Although our conclusions are based upon a transportation condition to which we will later refer, we believe it advisable to comment upon the rather extensive cost study which respondents presented and their theory of making rates within what they consider the zone of their "managerial discretion" lest they be led to the erroneous conclusion that we have placed our stamp of approval thereon.

Without attempting to point out some of the infirmities of respondents' cost study, we will assume that the figures developed reasonably approximate the direct expenses attributable to the transportation in question, plus a pro rata proportion of the indirect expenses exclusive of taxes, return on investment and passenger deficiencies.

During the past several years, California rail carriers have introduced in proceedings before the Commission numerous cost studies, similar to the one here presented, purporting to demonstrate the compensatory nature of proposed reduced rates for traffic of

various kinds. In each instance the cost of performing the service has been represented as being substantially lower than the sought rates, despite the fact that the sought rates reflected drastic reductions in the rates previously in effect. If these estimated costs were accepted at their face value, California rail carriers should be in a highly prosperous condition. On the other hand, it is a generally accepted fact, which we think respondents will not dispute, that California rail carriers generally have a pressing need for additional revenue from some source. It will be recalled that as late as 1937 California railroads petitioned the Commission for authority to effect a horizontal increase in their rates of 15 per cent (Application No. 21603), alleging in justification their precarious financial condition and their dire need for additional revenue.[6]

This anomalous situation in which the prevailing rail rates are well above the estimated costs, whereas the rail rate structure as a whole is returning inadequate revenue, appears to be explainable only by the fact that respondents have not transmuted those costs into a proper "price structure," the latter phrase being synonymous with "rate structure." They proceed upon the theory that once having determined the cost of moving the traffic, any rate yielding revenue in excess thereof is compensatory, when in truth it may be far from compensatory, in that it fails to pay its fair share of the cost of doing business.

Fundamentally the railroads are not different from other businesses. They manufacture and sell transportation. If they are to survive they must apply the same sound business principles to

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[6] With minor exceptions, Decision No. 30784 of April 11, 1938, allowed an increase of 10 per cent on all commodities other than products of agriculture, on which only 5 per cent increase was allowed.

their venture as any prudent business man would to his. Necessarily, if they are to obtain the over-all "cost of doing business," they must have thousands of prices or rates, extending over a wide range, determined by the character of the traffic to be moved. Many of these rates do and should contribute substantial amounts over the average cost of moving the traffic. But often during the stress of competition and because of their inability to obtain the traffic, respondents in desperation have resorted to price cutting to regain or hold the traffic on those commodities which should bear more than the full cost of performing the service.

And so it is in this case. Respondents, as they have in many other proceedings before this Commission, proceed upon the theory that they have the inherent right to use their managerial discretion in establishing freight rates if those rates yield something over and above the cost of moving the particular traffic in question. In fact, they have asked us to accept the premise that the minimum level for any rate, and its lawfulness, is fixed if the cost of moving that particular traffic is obtained regardless of what the character of the commodity may be.

The premise rests upon shifting sands. While we do not minimize the value of using costs in determining rates, it is only one of many factors to be considered in arriving at reasonable rates. Rate making is not an exact science. There are many elements which may be considered in determining a reasonable rate, including, among others, the value of the service to the shipper, what the traffic will bear, density of traffic, risk of loss or damage, bulkiness and weight of the commodity, its susceptibility to heavy loading, comparison with other rates and cost of service. No hard and fast rules can be applied in determining the weight which should be given each of the elements or factors usually and ordinarily considered in the

establishment of reasonable rates. (Davis vs. West Jersey Express Co., 16 I.C.C. 214, 216; In re Wool, Hides and Pelts, 25 I.C.C. 675, 677; Marley Paper Mfg. Co. vs. Akron C. & Y. R. Co., 163 I.C.C. 103, 107; United Paper Board Co. vs. Boston & A. R., 171 I.C.C. 627, 631; Carthage Pulp & Board Co. vs. Penn R. Co., 177 I.C.C. 217, 221).

Nor do we believe the statute requires us to give controlling weight to the cost of service. It is significant that Section 32(d) directs the Commission to establish the "lowest lawful rate" which comprehends the consideration of many other elements of rate making. Surely if the legislature intended the Commission to measure the lawfulness of rates by the cost of service alone, it could have done so in unmistakable terms.

The value of costs in rate making is demonstrable only when it is used as a base point to guide management or regulatory agencies in arriving at a reasonable level to be charged for the product transported. From time immemorial many commodities in order to move freely, or at all, have been hauled at less than full cost. Often the passenger traffic has failed to stand its full share of the cost of doing business. But even with their deficiencies, this traffic contributes to the over-all successful operation of the railroad as long as it contributes something in excess of the out-of-pocket costs. And likewise, from time immemorial, other commodities when they were able, have contributed more than the full costs of moving the traffic, indeed in some cases contributing many times the full costs.

The principles of rate making which have been followed practically since the inception of the railroads are rather elemental. One simple illustration will suffice. Let us assume that a railroad is handling a thousand tons of freight each day consisting of five commodities. The average full cost (including a return on

the investment) of moving the traffic is $3.00 per ton. But 400 tons of the one thousand tons consist of a low grade commodity which will not move at a rate in excess of $2.00 per ton. The second commodity consisting of 400 tons will not move at a rate in excess of $2.50 per ton, while the third commodity of somewhat higher value consisting of 100 tons will not move at a rate in excess of $3.00 per ton. But the other commodities, consisting in the aggregate of 100 tons, are of such high value that the volume of the freight rate, if not extortionate, has no bearing on their ability to move. Thus the first commodity contributes to the $3,000 per day cost of doing business $800, the second contributes $1,000 per day, the third $300 per day and the last $900 or $9 per ton and three times the full cost. And yet, after having given due consideration to all the elements of rate making, all the rates referred to above may well be "just and reasonable" within the meaning of Section 13 of the Public Utilities Act.

While the principles of rate making set forth above are elemental, their practical application is difficult because of the thousands of commodities transported, the fluctuation and the volume of movement, and numerous other factors that make the determining of just and reasonable rates by mere formulas or by mathematical computation impossible. Thus it must appear obvious that the determination of proper rates, after all proper elements are considered, rests largely upon an informed judgment. Initially the judgment is that of the management but this judgment may be supplanted by the judgment of the Commission if any provisions of the statute have been or will be violated.

We would think the proposed rates inherently unlawful in all respects were it not clearly apparent, under the particular circumstances herein, that present transportation conditions do not afford the respondents an equality of opportunity

to compete for the alcoholic liquor traffic now moving by for-hire carriers. It cannot be gainsaid that the philosophy of the legislation as contained in the Public Utilities Act and the Highway Carriers' Act contemplates that each agency of transportation shall have equal opportunity to compete for traffic which they can handle within their proper sphere. This record amply demonstrates that, in so far as this traffic is concerned, such an equality of opportunity does not exist. Out of a total of approximately 700 cars of alcoholic liquors transported between Los Angeles and San Francisco during 1939, the major part of which moved from rail spur to rail spur, only 12 cars were hauled by the railroads. Although in Case No. 4246 we attempted to place the trucks and rails on a plane of "equal opportunity" it appears from the record here that at least in this instance the desired equality may not have been attained. However, the ultimate remedy does not lie in permitting the rails to place in effect and maintain indefinitely the proposed rates, but does lie in evaluating the differences in the services of the different forms of transportation more completely than has heretofore been done. Accordingly, a hearing will be immediately scheduled in Case No. 4246, a continued proceeding involving the establishment of rates, rules and regulations of all common carriers as defined in the Public Utilities Act and all highway carriers as defined in the Highway Carriers' Act, for the purpose of considering these matters.

Under these circumstances and until more complete equality of opportunity has been provided, and for this reason alone, I am of the opinion and I hereby find that the proposed rates are justified by transportation conditions. The order of suspension should be vacated.

I recommend the following form of order:

O R D E R

Public hearings having been held in the above entitled proceeding, and based upon the evidence received at the hearings and upon the conclusions and findings set forth in the preceding opinion,

IT IS HEREBY ORDERED that the Commission's order of suspension and investigation of November 28, 1939, as amended, in the above entitled proceeding, suspending the operation of Item No. 5980-D of The Atchison, Topeka and Santa Fe Railway Company Tariff No. 12375-O, C.R.C. No. 690; Item No. 5886-C of Southern Pacific Company Tariff No. 730-D, C.R.C. No. 3353; and Item No. 10715-C of Pacific Freight Tariff Bureau Tariff No. 30-N of J. P. Haynes, Agent, C.R.C. No. 592 (of L. F. Potter series), be and it is hereby vacated and set aside and this proceeding discontinued.

Dated at San Francisco, California, this 17th day of September, 1940.

Commissioners.