C.4709 - RLC

Decision No. 36890

ORIGINAL

BEFORE THE RAILROAD COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Investigation upon the Commission's own motion into the reasonableness of the rates and charges, and into the sufficiency and adequacy of the operations, service, and facilities of San Diego Electric Railway Company.) Case No.4709

MORRISON, HOHFELD, FOERSTER, SHUMAN & CLARK, by FORREST A. COBB, for San Diego Electric Railway Company

J. F. DU PAUL, City Attorney, H. B. DANIEL, Assistant City Attorney, and WALTER W. COOPER, City Manager, for the City of San Diego

W. H. JENNINGS, for the City of La Mesa

LIEUTENANT J. E. SPELLMAN and LIEUTENANT (jg) J. K. GIBSON, U. S. NAVY, representing the Commandant, 11th Naval District, San Diego

HAVENNER, Commissioner:

INTERIM OPINION AND ORDER

This investigation, dealing with the rates and service of San Diego Electric Railway Company, was instituted by the Commission on its own motion on January 26, 1944, following a preliminary study by the Commission's staff which showed that this carrier's earnings during 1943 were excessive.

The matter was set for hearing on February 10, 1944, at San Diego, in the interest of securing for the patrons of this company some immediate relief in advance of the completion of the detailed study of the operating results. This plan for an early hearing was in keeping with the attitude expressed by Walter W. Cooper, city manager of San Diego.

At the hearing the company showed, through its Exhibit No. 2, that for the year 1943 it had earned a return of approximately 11.5% on the depreciated rate base of $4,201,000. This return is after allowance of all operating expenses including depreciation on the straight-line basis of $737,000, and including $1,450,000 of excess profits taxes, computed at the 90% gross rate, as well as full allowance for normal income tax and surtax. Based upon this excessive return, the company proposed an interim fare reduction which would save its patrons an estimated $437,000 per year. This reduction would become effective immediately and upon a trial basis, pending future development of the operating results. The proposed reductions consist of a change in the token fare from four for 30¢ to four for 25¢, extending the use of tokens to all zones, and extending the zone limits on three bus lines.(1)

Exhibit No. 2 shows also the estimated results that would obtain for the year 1944 on two bases, one employing the present fares and the other the proposed fares. In the case of the estimate employing present fares, the company concludes that the return on its investment would be 7.05%. There is included in the operating expenses an item of $976,000 for excess profits tax, computed at a gross rate of 95%. It will be noted that in all of the Company's estimates no credit allowance is made for the excess profits tax post-war refund which under the present law amounts to ten per cent.

Also included in operating expenses is an item of $200,000 for deferred maintenance. With respect to this item, it is the company's contention that it is in a position to spend this extra amount of money during 1944 in meeting deferred maintenance which has accumulated in prior years.

In the case of the company's estimate employing the proposed changes in the fare structure, the estimated return for the 1944

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(1) Proposed Reductions as shown by Exhibit No. 1:

"1. Reduce the token fare from seven and one-half cents (four for thirty cents) to six and one-quarter cents (four for twenty-five cents); tokens to be sold only in multiples of four.

2. The token fare will apply (a) between any two points which are within either the Inner or Outer Zones, and (b) between any two points in any two contiguous fare zones outside of Inner Zone. Not more than one token may be used on any one continuous one-way trip.

3. Extend the outer boundary of Outer Zone as follows:

(a) Route L: From Rosecrans Street and Elliott Street to Rosecrans Street and Lowell Street,
(b) Route O: From Chatsworth Boulevard and Ibsen Street to Chatsworth Boulevard and Zola Street,
(c) Route R: From Rosecrans Street and Midway Drive to West Point Loma Boulevard and Midway Drive.

4. Discontinue the twenty-five cent Round Trip fare between La Jolla and the following points:

(a) Chatsworth Boulevard and Zola Street
(b) Del Mar Street and Sunset Cliffs Boulevard, and
(c) West Point Loma Boulevard and Montalvo Street."

operation amounts to 6.55%. This estimate includes an item of $583,000 as excess profits tax at the 95% rate, together with the allowance of $200,000 for deferred maintenance.

Commission's Research Engineer Mors introduced a statement as Exhibit No. 4 showing the results of his study on this carrier's operation for the years 1943 and 1944, under the same fare structures as those employed by the company in its Exhibit No. 2. Exhibit No. 4 shows that for the year 1943 the return on the depreciated rate base amounted to 15%, after providing for excess profits tax of $1,305,000, computed at the net tax rate of 81%, and full allowance for normal income tax and surtax. With respect to the estimated results of the 1944 operations, this exhibit shows that with the present fares in effect the earnings would provide a return of 9.6% on the depreciated rate base, after allowing for an express profits tax of $937,000, computed on 85½% net rate. In the case of the estimate employing the proposed reduced fares, the return is computed at 8.2% after allowance for excess profits tax of $583,000 at the 85½% rate.

It should be noted that of the $437,000 proposed reduction in gross revenue all except about $21,000 is absorbed by reductions in taxes based on income (principally the excess profits tax) according to the company's calculation wherein the gross excess profits tax is included in operating expenses. In the Commission staff's calculation, in which the net excess profits tax is included in operating expenses, all except $60,000 of the proposed reduction is offset by tax decreases.

A comparison of the company's and the Commission staff's estimates for the year 1944 under the reduced fares is shown in the following tabulation:

Item	Company's Estimate (Ex. No.2)	Commission Staff's Estimate (Ex. No.4)
Undepreciated Rate Base*	$ 9,719,000	$ 9,719,000
Deduction for Depreciation and Amortization	5,549,000	5,549,000
Depreciated Rate Base	4,170,000	4,170,000
Operating Revenue	7,753,000	7,753,000
Operating Expenses (including straight line depreciation)	6,197,000	6,126,000
Taxes	1,282,847[a]	1,285,600[b]
Total Expense	$ 7,479,847	$ 7,411,600
Net Operating Income	273,153	341,400
Rate of Return on Depreciated Rate Base	6.55%	8.2%

*Comprises book investment as of January 1, 1944, in road and equipment, materials and supplies, and construction work in progress (which for the purposes of this study was assumed to be all operative). No allowance for working cash capital is included.

a. Includes $583,075 of excess profits tax computed at gross rate of 95%.

b. Includes $583,400 of excess profits tax computed at net rate of 85½%.

Mr. T. C. Stein, Principal Accountant of the Commission's Department of Finance and Accounts, introduced in evidence as Exhibit No. 3 a statement showing results of his study taken from the company's records, setting forth comparative income accounts and comparative balance sheets for the period January 1, 1938, to November 30, 1943.

The city manager of San Diego stated that in his opinion the patrons of this carrier should be afforded the reduced fares proposed by the company immediately and that, rather than wait for a complete investigation which might justify further reductions, it would be more desirable to accept the company's offer on an interim basis, with the understanding that the matter would be investigated further in the near future, looking toward the establishment of an equitable rate based upon a complete survey.

A review of this record leads to the conclusion that it is in the public interest to accept the company's offer as an initial step toward reducing rates. In doing so, however, it should be definitely understood that the Commission does not consider this a final rate or one that should rest for any period of time, but rather the matter should be continued for further taking of testimony as soon as the necessary studies can be made. To this end, the Commission's staff will be instructed to proceed with their studies in cooperation with the city and the company, with the objective of providing the public adequate service at the lowest reasonable rates under prevailing conditions.

No opposition developed to the company's proposed plan of fare reduction, notwithstanding the fact that the public had general knowledge of this hearing. Investigation thus far has shown that this company has performed a good mass transportation service, both rail and bus, under unusual and difficult wartime conditions. This is apparent from its reasonably successful handling of a growth from 33,557,000 passengers in 1940 to approximately 130,000,000 in 1943, with almost a complete absence of criticism from the public. Credit is due to both the company and its management and an alert and cooperative city administration.

Large new investments have been made in motor coaches and in other construction. The book investment in road and equipment increased from $6,839,000 at the end of 1940 to $9,443,000 as of January 1, 1944. In addition, the depreciation allowances have been accumulated and kept for the purpose for which they have been set aside, namely, to protect the continuance of the service and the investment in the property.

We are also impressed by the fact that the company is able to keep practically all of its equipment in servicable condition. There is no appreciable manpower shortage on this system with respect to the operation of the available equipment, in contrast to the situation in other mass transportation companies in this State. The arrangements made by the company for the operation and maintenance of its equipment indicate an exceptional exercise of foresight and ingenuity.

It should be understood that this action on the part of the Commission is in no way to be interpreted as passing upon the question of the taxes involved herein, particularly excess profits tax, nor upon the item of deferred maintenance. These are the two primary items having the greatest effect upon the allowable earnings of this carrier which may be considered as undetermined.

The following form of order is recommended:

O R D E R

Public hearing having been had, and the matter being now ready for the issuance of an interim order based upon the foregoing opinion;

IT IS HEREBY ORDERED that San Diego Electric Railway Company may establish revised rates in accordance with the foregoing opinion, as specifically set forth in the margin as footnote (1), on two (2) days' notice to the Commission and the public.

This 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 18th day of February 1944.

Richard Sachse
Justus F. Craemer
Franck R. Havenner
Francis [illegible]

Commissioners