

ORIGINAL

Decision No. 47543

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
Key System Transit Lines, a corpor-
ation, for an order pursuant to
Section 454 of the Public Utilities
Code authorizing the establishment
of increases and adjustments in rates
and fares for the transportation of
passengers between points in the
Counties of Alameda and Contra Costa
and the City and County of San
Francisco, in the State of California.)

Application No. 33113

OPINION ON REHEARING

Key System Transit Lines operates a unified transportation system consisting of interurban rail lines and passenger stage lines for the movement of passengers by local service within and between communities in the East Bay area and in the Counties of Alameda and Contra Costa and by transbay service between points in these counties and San Francisco. By Decision No. 47432 of July 8, 1952, in this proceeding, the company was authorized to increase its local and ¹ transbay fares. The Executive Committee of the Joint Investigation of Key System Transit Lines, Railway Equipment and Realty Company, Ltd., and related companies, by petition filed July 16, 1952, sought ² rehearing of the matter. A number of objections relative to Decision No. 47432, as hereinafter dealt with, were set forth in the petition. By order dated July 22, 1952, the Commission granted a rehearing which was restricted to oral argument of the issues raised upon the

¹ No increase was authorized in local fares for the transportation of school children.

² The Committee in question is comprised of representatives of the Cities of Alameda, Albany, Berkeley, El Cerrito, Emeryville, Hayward, Oakland, Piedmont, Richmond, San Leandro and San Pablo and the County of Alameda.

record as made.³ The oral argument was held at San Francisco on July 24, 1952.

In its petition and at the oral argument, petitioner urged, in substance, that the Commission erred (1) in allowing in the operating expenses sums covering the amortization of unrecovered investment in abandoned operating properties and interest thereon and to provide for removal of tracks, incidental street repairs, and maintenance of local rail lines, (2) in denying a motion to determine whether profits were realized from the sale of real properties used in connection with the abandoned rail facilities when, it was urged, the profits should be used in offsetting the remainder of the amounts allowed for amortization of unrecovered investment, (3) in issuing a decision in the passenger fare proceeding in question before the investigation of the utility in Case No. 5259 had been completed; (4) in denying the motion of the Commission's staff for time to prepare an alternate fare structure, and (5) in allowing Key System what is claimed to be more than a fair rate of return.

Petitioner is well aware of the fact that the amortization of unrecovered investment in the properties in question was authorized as extraordinary expense for rate-making purposes following an investigation of the matter and a finding by the Commission that such treatment of the abandoned facilities was reasonable and equitable, and of the further fact that the Commission on two occasions thereafter rejected contentions similar to those now made. No substantial reasons have been made to appear which would warrant a different conclusion at this time.

³ The order granting the rehearing contained a finding by the Commission that public necessity required the hearing of oral argument on the date in question.

It was contended further that the denial of petitioner's request for an investigation by the Commission to determine whether any profits had been realized by the company from the sale of the real properties used in connection with the abandoned rail facilities was in error and resulted in failure to reduce or offset the remainder of the amount allowed for amortization by the amount of any such profits. The amortization in question was authorized in connection with the substitution of bus for the then existing rail service. In Decision No. 42298 of December 7, 1948, in Application No. 29434, the Commission said "The record clearly indicated that with the abandonment of the street railway lines the resulting operating economies would reduce the company's need for additional revenue by a sum much in excess of the amount included in the operating expenses incident to the abandonment of those rail lines."⁴ This leaves no room for doubt that the Commission amply safeguarded the public interest at the time it authorized the amortization of the unrecovered investment in the abandoned rail facilities. No error was committed in denying the motion in question.

Petitioner's contentions relative to Case No. 5259 and its objections to the denial of the motion for the preparation of an alternate fare structure likewise have been considered carefully. The Commission finds the questions raised to be without merit.

We turn now to the objection made to the rate of return of 7.69 percent that was allowed Key System under Decision No. 47432, supra. Petitioner pointed out that the company was allowed a rate of return of only 5.31 percent in the previous fare increase proceeding (Decision No. 45205 of December 29, 1950, in Application No. 31179), hereinafter referred to as the 1950 proceeding. Petitioner apparently misunderstands the basic elements which generally accounted

⁴ See also Decision No. 42200 of November 4, 1948, in Application No. 29434.

for the difference in question. In the 1950 proceeding, the Commission said in its findings "We are not convinced, however, in view of the conflicts shown on this record, that the full measure of relief sought by applicant in the fares for local service should be granted" and also "While the record as thus far developed is adequate to justify the increases herein authorized, it is not adequate for the purpose of determining certain questions presented in this proceeding." These findings when read together with the others shown in the decision definitely point in the direction that the rate of return of 5.31 percent granted in the 1950 proceeding was on the low side of the zone of reasonableness.

The estimated operating results produced by the fare structure authorized in the instant proceeding are consistent with those in the decisions rendered in past fare increase proceedings involving Key System. In Decision No. 42200 of November 4, 1948, in Application No. 29434, increased fares were authorized designed to produce an operating ratio of 94.2 percent after provision for income taxes and in the 1950 proceeding the operating ratio was 95.19 percent. In the instant proceeding, it is 94.68 percent.

The rate of return represents the earnings remaining after taxes expressed as a percentage of the depreciated rate base. Fluctuations in the rate of return are not always attributable entirely to changes in the net earnings. For example, when the rate base remains constant as a result of periodic replacements of operating equipment and there is no difference in the earnings, no change will occur in the rate of return for one year as compared with another. However, in the absence of the equipment replacements, as is the case in the instant proceeding, the amount of the rate base steadily declines generally as a result of the recovery of the investment through

depreciation charges. The rate base declines rapidly when, as in the case of Key System, motor vehicle equipment having a relatively short service life is involved. Even though the earnings remained constant, the rate of return in one year would be greater than that in another year because of the difference in the rate base. In the instant proceeding, the rate of return was calculated on a rate base of \$9,983,400 as compared with the rate base of \$12,220,700 on which the return of 5.31 percent in the 1950 proceeding was developed. The lower rate base in question resulted both from adjustments made as a result of the thorough investigation conducted by the Commission in Case No. 5259 and in other proceedings referred to in Decision No. 47432, supra, and the diminishing effect of the depreciation charges accrued since the 1950 proceeding. Counsel for petitioner stated at the oral argument that no objection was being raised to the lower rate base.

Before dealing with the rate of return that was allowed in the instant proceeding, it should be explained that it is the practice of applicants and the Commission's staff to introduce in evidence at the public hearings in fare increase proceedings studies of the carriers' earning position, including forecasts of the results of operation anticipated for a future 12-month period usually designated as a test year. The forecasts provide the Commission with data showing the effect on an annual basis of changes in traffic volume and operating expenses which occur at various times and were not in effect throughout the preceding 12-month operation. The development of the forecasts necessarily involves the exercise of judgment relative to what will occur in the future test period based upon the experience of the past. The Commission's conclusions are developed from these financial data and the other evidence of record.

In allowing a rate of return of 7.69 percent and a corresponding operating ratio of 94.68 percent after provision for income taxes in the instant proceeding, the Commission endeavored to provide earnings for Key System which it considered fair and reasonable and which would assure the maintenance of adequate and dependable service to the public. A review of the record in connection with the 1950 fare increase shows that although the Commission fixed fares designed to yield a return of 5.31 percent for the test year involved the estimated results of operation under those fares in the test year in the instant proceeding show a rate of return of 1.89 percent for the transbay operations, a loss on the local service and a loss for the combined operations. The Commission considered that it was not in the public interest to perpetuate this unfavorable earning position. It undertook to authorize in the instant proceeding an increased fare structure designed to afford the company a more favorable opportunity to achieve reasonable earnings under the conditions portrayed in the record.

The record in this proceeding indicates that if Key System were required to continue the present fares during the test year it would suffer an operating loss amounting to \$134,776. This loss is attributable in large measure to increases in the wages of employees amounting to more than \$600,000 per year granted on January 13 and June 1, 1952, as a result of required collective bargaining processes. These advances were the latest of a series of upward adjustments that have been made in the wages in the past several years. Petitioner and the public generally must understand that the Commission has no control whatsoever over wage rates that result from collective bargaining processes. They must understand

also that if adequate necessary transportation service is to be provided the company must have revenues sufficient to meet the higher wages and its other operating expenses to say nothing of a return on its investment.

The Commission repeatedly has said in rate proceedings that operating ratios, rate bases, rates of return and other pertinent data are valuable indices of earning requirements. The Commission has said also that in reaching its conclusions in such matters it considers all available data without limitation or restriction to any single method or formula. The paramount issue involved is that the final result be reasonable. It is clear that, under the circumstances, the rate of return of 7.69 percent allowed in the instant proceeding when viewed in connection with an operating ratio of 94.68 percent after provision for income taxes is within the zone of reasonableness. It is very doubtful, however, that Key System will realize these operating results under the increased fares in the immediate future. The record indicates that the company now is operating at a loss. Since the increased fares involved herein would be in effect for a period of less than 5 months in the year 1952, the company probably will not be able to recover all of the operating expenses incurred for the year. Moreover, in the face of the continued inflationary trend it appears unlikely that it will realize in the year 1953 the full earnings estimated under the increased fares.

Petitioner contends that excess profits tax liability is involved under the authorized fare structure. This

liability for excess profits tax was based on revenues and expenses for the test year as computed for rate-making purposes. Under this theory no provision was made for inclusion in operating expenses of the amounts claimed by the company for tax purposes to cover an allowance of approximately \$176,000 for accelerated amortization of its investment in bridge rail facilities, to cover the shorter lives assigned to certain depreciable assets and the resultant higher depreciation charge of about \$65,000 and to cover depreciation of approximately \$36,500 on the 21 articulated units which have been classified as nonoperative property. If consideration is given to deductions claimed by the company for tax purposes which have not been allowed as expenses in this proceeding, to the fact that the new fares will be in effect for a period of less than five months in 1952 and to the continuing inflationary trend, it is our opinion that the company will not incur a liability for excess profits tax during 1952 or 1953 under the fares herein authorized.

The Commission has carefully considered all of the arguments advanced and the points made by petitioner and it is of the opinion and hereby finds that it has not been demonstrated that any error has been committed. Decision No. 47432, supra, will be affirmed. In view of the evident need for additional revenue, Key System will be authorized to establish the fare structure therein set forth upon not less than three (3) days' notice to the Commission and to the public.

The company has requested that it be authorized to amend its tariffs on less than statutory notice to provide rules governing the use and redemption of commutation tickets purchased by passengers

before the effectiveness of the increased fares. It is proposed that 20-ride commutation tickets sold prior to the effective date of the higher fares would continue to be honored for a period of 12 days after the effectiveness of the new fares. It is proposed also to provide that 20-ride commutation tickets sold prior to the fare increase will be redeemed at the fare paid when no part of the ticket has been used or at a pro rata of the fare paid, calculated to the nearest cent, when any portion of the ticket has been used. The proposal appears to be reasonable and will be authorized.

ORDER ON REHEARING

A rehearing restricted to oral argument of the issues raised upon the record as made having been held and the Commission being fully advised in the premises,

IT IS HEREBY ORDERED that Decision No. 47432 of July 8, 1952, in Application No. 33113, be and it is hereby affirmed; and that Key System Transit Lines be and it is hereby authorized to establish, within sixty (60) days after the effective date of this order on rehearing on not less than three (3) days' notice to the Commission and the public, the increased passenger fares authorized by the said Decision No. 47432.

IT IS HEREBY FURTHER ORDERED that Key System Transit Lines be and it is hereby authorized to amend its Tariff Cal.P.U.C. No. 11, within sixty (60) days after the effective date of this order on not less than three (3) days' notice to the Commission and to the public,

to provide that 20-ride tickets sold during the period from July 12, 1952, to and including the day prior to the date of the effectiveness of the increased fares herein authorized, will be honored for a period of 12 days after the authorized fares take effect, the 12 days to include the date on which the increased fares become effective, and to provide for redemption of 20-ride tickets outstanding after the 12-day period in question on the basis of the fare paid when no portion of the ticket has been used and on the basis of a pro rata of the fare paid, calculated to the nearest cent, for the unused portion of the ticket when some use of the ticket has been made.

IT IS HEREBY FURTHER ORDERED that, in addition to the required filing and posting of tariffs, applicant shall give notice to the public by posting in its busses and terminals a printed explanation of the increased fares and of the honoring limits and redemption bases as authorized herein. Such notices shall be posted not less than three (3) days before the effective date of the fare changes and shall remain posted for a period of not less than twenty (20) days after said effective date.

This order on rehearing shall become effective five (5) days after the date hereof.

Dated at San Francisco, California, this 5th day of August, 1952.

[Signature]
President
[Signature]
[Signature]
[Signature]

Commissioners
Commissioner [Name] did not participate in the disposition of this proceeding.