

**ORIGINAL**

Decision No. 47650

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the matter of the Application )  
of GILROY TELEPHONE COMPANY, a )  
corporation, for an order )  
authorizing increases and changes )  
in rates for exchange telephone )  
service. )

Application No. 33303  
(Amended)

Appearances for Applicant: Donald A. Strahl  
and F. V. Rhodes.

Protestants: James E. Drew for Citizens and  
Business Men of Gilroy; Sidney S. Johnson  
for City of Gilroy.

Interested Parties: Frank V. Rhodes for  
California Independent Telephone Association;  
J. J. Deuel and Eldon Dye for California Farm  
Bureau Federation.

Other Appearances: Harold J. McCarthy for the  
Commission's staff.

O P I N I O N

Gilroy Telephone Company, engaged in the business of furnishing telephone service in the City of Gilroy and surrounding territory in Santa Clara County, filed the above-entitled application on April 10, 1952 for authority to increase telephone rates to yield additional annual revenue of \$32,313 from exchange service at the level of business as of December 31, 1951. On June 6, 1952, it filed an amendment to the application asking that this revenue proposal be increased to \$39,392 because of pay increases to be made effective on July 1, 1952, in accordance with a revised union wage contract with the Communication Workers of America.

Public Hearings

After due notice public hearings were held on this application before Examiner M. W. Edwards at Gilroy on June 9, 1952

and on July 21, 1952. During the first day of hearing the applicant's principal witness presented testimony and was cross-examined thereon, and statements were presented by the protestants and interested parties. During the second day of hearing the applicant filed a revised computation of the proposed increase in rates as Exhibit No. 1, which reduced the requested over-all annual increase to \$39,390 and presented testimony in substantiation of an increase in the manager's salary. Also, on the second day the Commission's staff presented a report on the results of operation of Gilroy Telephone Company for the year 1951 recorded and adjusted, and for the year 1952 estimated, as Exhibit No. 2 in the proceeding. Following cross-examination of the staff's witness and further cross-examination of the company's principal witness the matter was submitted for Commission decision subject to later filing of wage increase evidence as Exhibit No. 3 in this proceeding.

Postwar Increases

During the postwar period, since 1946, of increased prices, wages and taxes, applicant has been before the Commission once previously seeking an increase in telephone rates. On October 10, 1950 it filed Application No. 31836 asking authority to increase certain telephone rates and charges by \$27,993 annually, but at the public hearings on February 14 and 15, 1951, amended its request to a total increase of \$37,625 annually on the basis of services furnished as of December 1, 1950. By Decision No. 45468, dated March 20, 1951 applicant was authorized revised rates, now in effect, which were estimated to increase gross revenues for local service by approximately \$34,500 annually calculated to give a rate of return of 6.5% on a rate base of \$287,700. However, applicant alleged at the second day of hearing

on the instant application that the rate schedules specified by the Commission did not yield an increase of the estimated \$34,500, which is partly the reason for this second requested postwar increase. The applicant did not state how much added revenues the prior rate increase did produce.

The staff witness brought out the fact that when the previous decision was rendered the company was in the process of conversion of privately owned farmer lines and replacing the switchboard. The staff's estimate was predicated on the basis of a normal year and it was because of the delay of the applicant in conversion of these farmer lines that the full increase as estimated had not been realized.

#### Applicant's Operations

Gilroy Telephone Company furnishes exchange service locally and toll service through connection with facilities of The Pacific Telephone and Telegraph Company. Telegraph service is not offered by the company. Since preparation of the Commission staff's report on this company for the prior rate increase application in 1951, the Gilroy switchboard and associated central office equipment has been replaced. Suburban service has been provided all former farmer line subscribers except for 10 stations on two remaining farmer lines. Suburban lines are limited to a maximum of eight parties. Full selective ringing is provided on all company-owned lines by means of four nonharmonic frequencies derived from vibrator-type ringing machines.

The company's exchange is served by a Kellogg nine-position, manual common battery switchboard with a capacity of 4,200 lines. As of May 31, 1952 the company served 2,586 stations, which includes three stations furnished the City of Gilroy at no charge, in accordance with franchise requirements. As of June 1,

1952 there were 44 employees on the company's pay roll; 3 assigned to the general office, 4 to commercial, 12 to plant and 25 to traffic.

Position of Applicant

The applicant at this time seeks an approximate 39% increase in revenues. Applicant states that it has largely completed the rural program undertaken in 1951 and is now engaged in rebuilding its plant within the City of Gilroy. The rebuilding program will be completed in 1953. Materials are either on hand or on order for most of this program. Construction personnel have been trained and properly equipped, and warehouse and garage space has been provided for materials and equipment. To continue this program and bring it to a successful completion applicant alleges that it must secure additional capital funds in the very near future.

Subscriber Interest

Subscribers and their representatives were present at each day of public hearing. Statements were received in opposition to the increase, and the representatives cross-examined the company's and staff's witnesses. The City Attorney of Gilroy stated that the city is not formally opposing a reasonable increase and that it would rely on the Commission to allow no greater increase than the company was lawfully entitled to.

A local businessman presented a petition signed by some 300 persons protesting the granting of any increase in addition to that granted in 1951 and urging the Commission to investigate the application very carefully. In response to cross-examination by this representative of both the company and the Commission staff

witnesses as to the need for additional revenue, the record reveals the following:

1. The company previously was not granted its full requested increase.
2. A wage increase of approximately \$7,000 on an annual basis, made effective on April 1, 1951, was not considered in the last decision.
3. There was delay in conversion of farmer line stations to suburban service.
4. Investment per station on the average has increased from \$125.86 in 1950 to an estimated \$149.85 for 1952, thus diluting the rate of return.
5. Tax rates have increased.
6. While stations were being converted it was impossible to estimate accurately revenues and expenses.

The representative for the California Farm Bureau Federation cross-examined the staff witness with regard to the adequacy of service. The staff witness replied that an inspection of the lines indicated that the plant is in good condition, with no brush or trees contacting the open wires, and that calls were being handled promptly by switchboard operators with no delays in completing local calls. This representative indicated that the farm bureau had received some requests for improved types of service by certain outlying subscribers. The company has offered to investigate and report on these requests.

#### Evidence of Earnings

Applicant's Exhibit D (revised) attached to the amendment to the application showed that in 1951 the operating revenues of \$147,449.85 were sufficient to cover all operating expenses, taxes, depreciation and amortization expenses, and provide a net operating revenue of \$1,216.75. Such net revenue is equivalent to 0.44% return on an average depreciated rate base of \$275,165.51. For the same year the staff's study showed a rate of return of 0.48%

on an average depreciated rate base of \$256,000. However, after adjusting the 1951 revenues for the May 1, 1951 rate increase to reflect a full year and adjusting 1951 expenses for a wage increase granted non-supervisory traffic and commercial employees April 1, 1951 to a full year basis, the rate of return would have been 2.63%.

Both the applicant and the Commission's staff presented estimates of earnings of the Gilroy Telephone Company for the year 1952. The estimates, which are summarized below, were prepared on the basis of present and proposed rates:

ESTIMATED EARNINGS IN 1952

Item	Company		Staff	
	Exhibit D Revised	Exhibit No. 2	Exhibit D Revised	Exhibit No. 2
	Present	Proposed	Present	Proposed
	Rates	Rates	Rates	Rates
Operating Revenue	\$172,813	\$211,322	\$174,700	\$213,750
<u>Operating Expenses</u>				
Maintenance and Operation	141,345	147,792	147,600	147,600
Taxes	13,761	25,624	13,825	28,650
Depreciation	15,730	15,730	13,800	13,800
Total Expenses	170,836	189,146	175,225	190,050
Net Revenue	1,977	22,176	(525)	23,700
Rate Base (Depreciated)	359,926	359,926	331,000	331,000
Rate of Return	0.55%	6.18%	(0.16)%	7.16%

(Red Figure)

The company did not take any exception to the revenue and expense estimates shown by the staff which included the proposed wage increases, but it did question the lower rate base figure.

The staff engineer recommended that the company compute accruals to the depreciation reserve upon the basis of spreading the original cost of the plant, less estimated net salvage and depreciation reserve, over the estimated remaining life of the property. Such change will be required by the order herein.

Toll Revenues

Toll service revenues of the applicant consist of that portion of the total toll billing retained by applicant under the terms of a traffic agreement with The Pacific Telephone and Telegraph Company. Witness for the applicant, under cross-examination stated that the latest revision in the basis of toll revenue settlement under the traffic agreement was made effective June 21, 1947. He stated further that there have been no changes made in the traffic agreement to reflect recent increases in wages, taxes, and other costs of the applicant. The fact that this problem is currently under study by the independent telephone industry and the Bell System on a nationwide basis, does not relieve the applicant herein of its responsibility to its telephone users to negotiate with The Pacific Telephone and Telegraph Company to the end that the traffic agreement will reflect applicant's current costs of handling toll traffic.

Rate Base

The staff's rate base consisted of weighted average plant in service plus materials and supplies and working cash, less contributions of plant and depreciation reserve. The staff engineer had treated the future \$20,000 trade-in allowance on the secondhand Kellogg switchboard recently installed as a donation of plant and had deducted the said \$20,000 from the rate base. His reasoning was that the company had not been required by Kellogg Company to advance any cash to cover the future trade-in allowance and is not required to pay any interest on it; therefore, the stockholders have no investment in this portion and are not entitled to a return on it. The company brought out the fact that this amount will have to be paid in five years unless new Kellogg dial equipment is installed and that in reality it is

a deferred obligation of the company which will become real unless Kellogg dial equipment is purchased to replace the manual board.

In reviewing this problem it is apparent that from the ratepayer's standpoint there are two ways this matter equitably could be treated: (1) as equivalent to a donation of plant or (2) add the switchboard trade-in allowance of \$20,000 to the rate base and adjust the rate of return for the fact that no interest is required on this portion of the plant. For the purpose of this proceeding the former method, which was used by the staff, will be adopted in this order.

#### Wage Increase

In the amended application it is stated that the revised contract with the Communication Workers of America became effective on June 1, 1952, and that it provided a wage increase of 10 cents per hour for all accounting, commercial, and traffic non-supervisory employees to become effective on July 1, 1952. It estimated that on the basis of the number of employees needed during the year 1952 the new wage schedules would result in an increase of cost of operation of approximately \$6,600 per year. The applicant also requested an expense allowance for an annual \$2,100 increase in the manager's salary.

Applicant was granted permission to file an exhibit when approval by the Wage Stabilization Board of the wage increase was obtained. Realizing that there might be considerable delay in obtaining the Wage Stabilization Board's approval of the full 10-cent increase, the applicant's Board of Directors met on July 24, 1952 and authorized the immediate payment of 6 cents per hour increase which could be done under Regulations 6 and 8 of the board without waiting for approval. It also authorized an increase in the manager's salary effective October 1, 1952.

A copy of the minutes of the Board of Directors of the Gilroy Telephone Company of July 24, 1952, together with a sample copy of the wage agreement were submitted by letter dated July 25, 1952 and will be received and constitute applicant's Exhibit No. 3. At this time wage and salary increases of \$6,000 per year will be reflected in operating expenses.

#### Financing

Applicant has financed plant construction principally through the medium of common stocks. As of December 31, 1951 there were 21,771 shares of \$10 par value stock outstanding for which it had received \$284,260. In addition it had borrowed \$25,000 from the Bank of America on an unsecured note at 4½% interest rate and plans additional borrowings on notes for the remainder of the year. Applicant estimated its 1952 cash interest and dividend requirement at \$19,647.40.

#### INTEREST AND DIVIDEND REQUIREMENT 1952

\$25,000 Note for 12 Months	at 4.5% rate	\$ 1,125.00
30,000 Note for 6 Months	at 4.5% rate	675.00
20,000 Note for 3 Months	at 4.5% rate	225.00
March Dividend	21,915 shares at 20 cents	4,383.00
June Dividend	21,941 shares at 20 cents	4,388.20
September Estimated	22,128 shares at 20 cents	4,425.60
December Estimated	22,128 shares at 20 cents	4,425.60
Total		<u>19,647.40</u>

Applicant's witness did not request an increase based on a fair rate of return on the rate base, but asked sufficient increase to cover all interest and dividend requirements plus some reasonable allowance for surplus.

#### Conclusion on Earnings

Relatively high dividends were paid in the postwar years until 1949 while service was not maintained at a satisfactory level. The company appointed a new manager in 1950 and the record shows that service has been improved and the plant is in process of rehabilitation and expansion. The company is to be

commended for this step. At the same time, the public has been called upon to pay higher rates, in part, because of the company's failure in the prior years to maintain the plant while paying high dividends. Further increases will be authorized herein which are the minimum necessary to enable the company to carry forward its rehabilitation and expansion program.

For the purposes of this order we find that a rate of return of 6.25% is fair and reasonable for the 1952 level of operations when applied to a rate base of \$331,000. Adopting the staff's expense figures and adjusting them in the amount of \$2,700 for wage increases not yet authorized, we find that at this time an annual increase in revenue of \$29,900 is warranted on the 1952 level of business. Such increase amounts to approximately 76% of applicant's requested increase [and would provide an estimated operating revenue of \$204,400 for the year 1952 if the authorized rates were in effect for the entire year.] Rate changes will be authorized as described in the section that follows.

#### Authorized Rates

A comparison of the present rates for the basic classifications of exchange service with the rates requested by the applicant and those authorized in the order herein follows:

Class and Grade of Service	Present Rate	Company		Authorized Rate	Increase
		Proposed Rate	Rate		
<u>Residence</u>					
1-party	\$3.50	\$4.75	\$4.60	\$1.10	
2-party	3.00	4.25	3.80	.80	
4-party	2.50	3.75	3.25	.75	
Suburban	2.75	4.00	3.55	.80	
Extension	1.00	1.25	1.25	.25	
<u>Business</u>					
1-party	5.25	7.00	7.00	1.75	
2-party	4.25	6.00	5.90	1.65	
Suburban	3.75	5.00	5.00	1.25	
Extension	1.25	1.75	1.75	.50	

In addition to the increases in the basic exchange rates, the applicant also requests increases in monthly rates for PBX trunks and stations and semipublic service, and the elimination of the discount of 25 cents per month for service furnished with a wall set station. These requests appear reasonable and will be authorized.

Applicant also has requested that the rate for local messages placed from pay stations be increased from 5 cents to 10 cents. This class of service should bear a portion of the increase and the applicant's request will be authorized.

Conclusion

After reviewing all of the evidence of record, the statements by subscribers' representatives and counsel for City of Gilroy, and giving full weight to the service, operating, and financial problem of this utility, it is our conclusion that an order should be issued at this time increasing the rates in accordance with the findings herein.

O R D E R

Gilroy Telephone Company having applied to this Commission for an order authorizing an increase in rates and charges, public hearings having been held, and the matter having been submitted for decision;

IT IS HEREBY FOUND AS A FACT that the increases in rates and charges authorized herein are justified and that present rates,

in so far as they differ from those herein prescribed for the future, are unjust and unreasonable; therefore,

IT IS HEREBY ORDERED that applicant is authorized to file in quadruplicate with this Commission after the effective date of this order, in conformity with the Commission's General Order No. 96, rates, charges, and conditions revised as set forth in Exhibit A attached hereto, and, on not less than five (5) days' notice to the Commission and to the public, to make said rates effective for service furnished on and after October 1, 1952.

IT IS HEREBY FURTHER ORDERED that applicant shall review annually the accruals to depreciation reserve which shall be based upon spreading the original cost of the plant, less estimated net salvage, and less depreciation reserve, over the estimated remaining life of the property; and the results of these reviews shall be submitted annually to the Commission.

The effective date of this order shall be twenty (20) days after the date hereof.

Dated at San Francisco, California, this 2<sup>nd</sup> day of September, 1952.

A. J. Donohoe  
President.  
Justice F. Caserio  
Francis H. Patton  
John E. Mitchell  
Commissioners.

## EXHIBIT A

## RATES

The presently effective rates, charges and conditions are changed only as specifically set forth in this exhibit.

Schedule No. A-1, Individual and Party Line Service

	<u>Wall, Desk or Hand Set Station</u>	
	<u>Rate per Month</u>	
	<u>Residence</u>	<u>Business</u>
	<u>Service</u>	<u>Service</u>
Each individual line primary station	\$4.60	\$7.00
Each two-party line primary station	3.80	5.90
Each four-party line primary station	3.25	—
Each extension station	1.25	1.75

Delete the following condition: "Wall set stations installed prior to May 1, 1951 - 25¢ less per month."

Schedule No. A-5, Suburban Service

	<u>Wall, Desk or Hand Set Station</u>	
	<u>Rate per Month</u>	
	<u>Residence</u>	<u>Business</u>
	<u>Service</u>	<u>Service</u>
Each suburban ten-party line primary station	\$3.55	\$5.00
Each extension station	1.25	1.75

Delete the following condition: "Wall set stations installed prior to May 1, 1951 - 25¢ less per month."

Schedule No. A-7, Private Branch Exchange Service

	<u>Rate per Month</u>
<b>Trunk Line Rate:</b>	
Each central office trunk line	\$10.50
<b>Station Rate:</b>	
Each station not located in hotel guest room	1.75
Each station located in hotel guest room	1.25

Delete the following conditions: "Wall set stations installed prior to May 1, 1951 - 25¢ less per month."

Schedule No. A-13, Public Telephone Service

	<u>Rate</u>
Each exchange message	\$0.10

Schedule No. A-13(a), Semipublic Coin-Box Service

	<u>Wall Set or Wall Hand Set</u>		
	<u>Rate per</u>	<u>Each Exch.</u>	<u>Min. Chg.</u>
	<u>Month</u>	<u>Message</u>	<u>per Day</u>
Each individual line coin-box station	\$1.25*	\$0.10	\$0.20
Each extension station without coin box	1.25	—	—

\* In addition to minimum charge per day.