

ORIGINAL

Decision No. 54215

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of certain railroads and )  
 connecting highway common carriers for )  
 authority to increase local and joint )  
 freight rates and charges (1956). )

Application No. 37697

E. E. Bennett, Charles W. Burkett, Jr., Robert F. Garing, Clair MacLeod, R. L. McMichael, Frederick G. Pfrommer, and E. L. Van Dellen; for applicants.

J. C. Kaspar and Arlo D. Poe, for California Trucking Associations; intervenor in support of applicants.

Sidney H. Bierly, Eugene R. Booker, H. G. Feraud, R. P. McCarthy, F. F. Miller, L. E. Osborne, Mrs. Grace McDonald, and John H. Telfer; for various shipper and labor organizations, protestants.

Larry Ambrose, Frank E. Ashton, W. Y. Bell, Carl F. Breidenstein, Bert Buzzini, J. J. Deuel, W. R. Donovan, Wallace K. Downey, Joseph T. Enright, Gene Feise, B. R. Garcia, Waldo A. Gillette, William G. Higgins, Thomas B. Kircher, Harold A. Lincoln, T. A. L. Loretz, Joseph R. McNicoll, Charles C. Miller, F. F. Miller, S. A. Moore, W. G. O'Barr, O'Melvony & Myers, by Lauren M. Wright, A. E. Patton, Robert J. Puppo, Jim Quintrall, Eugene R. Rhodes, Harry H. Ross, Philip J. Ryan, James C. Uhler, J. G. Vollmar, and Reginald F. Walker; for various shippers and other interests, interested parties.

H. F. Wiggins, John L. Pearson and R. A. Lane; for the Commission's staff.

## O P I N I O N

By this application, as amended, California rail lines and certain connecting highway carriers seek authority to establish increased freight rates and charges.

Public hearing was held at San Francisco on April 12 and 13, and July 11, 13 and 17, 1956, and at Los Angeles on May 23, 24 and 25, 1956, before Commissioner Matthew J. Dooley and Examiner Carter R. Bishop. Following the conclusion of the July 17 hearing a statement of position and a motion to dismiss were filed by a protestant and by counsel for the Commission's staff, respectively, followed by applicants' written replies thereto. On August 6, 1956, the matter was taken under submission.

The latest adjustment in the general level of rail freight rates applicable on California intrastate traffic was made pursuant to authority granted by Decision No. 49290, of November 3, 1953, 53 Cal. P.U.C. 4.<sup>1</sup> That decision permitted a general increase of 15 per cent, subject to specified exceptions and to certain maximum

---

1

By Decision No. 48107 of December 22, 1952, in Application No. 32219 (First Supplemental), this Commission had found not justified the request of the California lines for authority to establish the same rate increases on intrastate traffic as were authorized by the Interstate Commerce Commission on April 11, 1952, for interstate traffic in western and southern territories and interterritorially (Ex Parte No. 175, Increased Freight Rates, 1951). Thereafter, the Interstate Commerce Commission, pursuant to an investigation instituted under Section 13(4) of the Interstate Commerce Act, found, inter alia, that California intrastate rates cast an undue burden upon interstate commerce and that they would, for the future, cause undue, unreasonable and unjust discrimination against said commerce. (Decision of October 5, 1953, in Docket No. 31219; California Intrastate Railroad Freight Rates and Charges; 289 I.C.C. 767.) The Commission further found that, in order to remove said burden and discrimination, the California intrastate rates should be subject to the same respective increases as were maintained on like interstate traffic between points in California and adjoining states under the authorization in the above-mentioned decision in Ex Parte No. 175. Accordingly, the increases in question were then authorized by this Commission's Decision No. 49290, mentioned in the text, supra.

increase limitations. The 15 per cent increase superseded a six per cent interim increase theretofore authorized by Decision No. 45672, 51 Cal. P.U.C. 341 (1951).

Applicants now seek a further general rate increase of six per cent. An increase of the same percentage was authorized by the Interstate Commerce Commission on March 2, 1956, for interstate traffic, on a nation-wide basis. The carriers had sought an increase of seven per cent. The six per cent increase in interstate rates, which became effective on [redacted] subject to designated exceptions and [redacted].

Applicants [redacted] increase sought herein be made subject to [redacted] exceptions and other provisions as [redacted] including interstate adjustment. In addition, [redacted] increases shall not apply to class and commodity [redacted] Pacific Southcoast Freight Bureau Tariff No. [redacted] on refined petroleum products in tank cars, nor to [redacted] rates, charges and provisions applicable to the transportation of carload shipments in so-called trailer-on-flat car service. The principal rate witness for applicants explained that all of the rates embraced by these additional exceptions, exclusive of those on refined petroleum products in tank cars, are now subject to other proceedings before this Commission in which applicants are seeking authority to apply increases thereon. All of these additional exceptions, he said, involve rates which applicants, for competitive reasons, have kept on the same levels as those maintained by the highway carriers for the same movements.

*CORRECTION*

# CORRECTION

THIS DOCUMENT  
HAS BEEN REPHOTOGRAPHED  
TO ASSURE LEGIBILITY

increase limitations. The 15 per cent increase superseded a six per cent interim increase theretofore authorized by Decision No. 45672, 51 Cal. P.U.C. 341 (1951).

Applicants now seek a further general rate increase of six per cent. An increase of the same percentage was authorized by the Interstate Commerce Commission on March 2, 1956, for interstate traffic, on a nation-wide basis. The carriers had sought an increase of seven per cent. The six per cent increase in interstate rates, which became effective on March 7, 1956, was made subject to designated exceptions and to maximum increase limitations.

Applicants propose that the six per cent increase sought herein be made subject to the same exceptions, limitations and other provisions as those entailed in the corresponding interstate adjustment. In addition, they propose that said increases shall not apply to class and commodity rates named in Pacific Southcoast Freight Bureau Tariff No. 255-F, nor to rates on refined petroleum products in tank cars, nor to certain rates, charges and provisions applicable to the transportation of carload shipments in so-called trailer-on-flat car service. The principal rate witness for applicants explained that all of the rates embraced by these additional exceptions, exclusive of those on refined petroleum products in tank cars, are now subject to other proceedings before this Commission in which applicants are seeking authority to apply increases thereon. All of these additional exceptions, he said, involve rates which applicants, for competitive reasons, have kept on the same levels as those maintained by the highway carriers for the same movements.

Applicants furthermore do not intend to apply the six per cent increase to certain carload commodity rates which historically have been maintained on the same levels as those of the corresponding highway carrier rates. The rail and truck rates in question were subjected to interim increases in 1955 and again in 1956 pursuant to Decisions Nos. 51688 and 52971, respectively (Petitions Nos. 62 and 74 in Case No. 5432).<sup>2</sup> However, petitioners do not want the proposed intrastate authority so restricted. While they have no intention of applying double increases to these commodity rates, the rate witness stated, applicants have no assurance that the temporary surcharge now applicable will be made permanent, and in event of its expiration wish to be able then to apply to these commodity rates such increases as may issue from this proceeding.

Applicants submitted estimates of intrastate freight revenues for a 12-month period, predicated upon tonnage and revenues for the year 1955. These estimates embrace eleven of the 36 applicant railroads.<sup>3</sup> Aggregate 1955 California intrastate traffic for the eleven lines amounted to 35,777,951 tons. Revenue from this tonnage totaled \$87,982,797. Applicants estimated that, had the

---

2

The increases in question, which are stated as surcharges, are published to expire with May 1, 1957, unless sooner canceled, changed or extended by order of the Commission. The ultimate disposition of those increases depends upon a general review of statewide minimum rates now in progress.

3

The 11 rail lines are: The Atchison, Topeka and Santa Fe Railway Company, Great Northern Railway Company, Holton Inter-Urban Railway Company, Northwestern Pacific Railroad Company, Pacific Electric Railway Company, Petaluma and Santa Rosa Railroad Company, San Diego and Arizona Eastern Railway Company, Southern Pacific Company, Union Pacific Railroad Company, Visalia Electric Railroad Company and The Western Pacific Railroad Company.

increases sought herein been in effect during the year 1955, the California intrastate revenues for the eleven roads would have amounted to \$92,456,663. Applicants anticipated a continuance of the 1955 volume of traffic and thus estimated that the proposed rate increases, if authorized, would produce \$4,473,866 in additional annual revenue for the eleven roads as a group.

A breakdown of the foregoing figures is set forth in Table I below:

Table I

Tonnage and Revenues for 1955, also Estimates of Revenues Under Proposed Rates for a 12-Month Period, for California Intrastate Traffic of Six Principal Lines and Totals

| Road                          | 1955       |              | Estimated Revenue at Proposed Rates | Additional  |
|-------------------------------|------------|--------------|-------------------------------------|-------------|
|                               | Tons       | Revenue      |                                     |             |
| Southern Pacific <sup>4</sup> | 19,852,391 | \$51,690,702 | \$54,241,199                        | \$2,550,497 |
| Santa Fe                      | 5,774,575  | 18,849,050   | 19,847,035                          | 997,985     |
| Northwestern Pacific          | 3,016,468  | 9,016,769    | 9,515,360                           | 498,591     |
| Pacific Electric              | 3,691,728  | 3,173,250    | 3,320,276                           | 147,026     |
| Union Pacific                 | 1,389,381  | 2,101,126    | 2,210,451                           | 109,325     |
| Western Pacific               | 1,130,415  | 1,658,046    | 1,745,220                           | 87,174      |
| Other 5 Roads                 | 922,993    | 1,493,854    | 1,577,122                           | 83,268      |
| Totals                        | 35,777,951 | \$87,982,797 | \$92,456,663                        | \$4,473,866 |

Estimates of California interstate revenues were also submitted. These related to revenues assigned to the California portions of hauls between that and other states, and to revenues derived from interstate traffic as to which the rail movement is entirely within California (so-called port traffic). These figures showed that, for the above-mentioned eleven roads and for the year 1955, a total of \$293,147,423 was assigned to or received from such traffic. Had the six per cent increase authorized in 1956 for interstate traffic

<sup>4</sup>"Southern Pacific" as used in this decision refers to Southern Pacific (Pacific Lines) and leased lines.

been applicable during the period in question, applicants estimate that the California interstate revenues would have amounted to \$308,476,573, or an increase of \$15,329,150 annually.

Applicants did not submit any estimates of the expenses involved in handling California intrastate traffic. Their witnesses testified extensively to the asserted impracticability of developing such estimates on a reliable basis. These witnesses, both operating and accounting, stated that the primary unit of production of rail transportation is the train, that trains generally are made up of cars some of which are moving in intrastate, and others in interstate, commerce and that expenses are incurred and recorded only in relation to trains as composite units. Testimony of similar import was given with respect to switching operations, station service, maintenance of way and structures, and other expenses. The witnesses were of the opinion that no separation of intrastate expenses from those incurred in connection with interstate traffic could be made on an actual basis and that no separation could be made on an arbitrary basis that would be reliable.

Evidence was adduced by applicants' witnesses, however, designed to show that conditions incident to the intrastate transportation of freight in California are not more favorable than those which are incident to interstate transportation in this State and in adjoining states. The evidence included, inter alia, comparisons of terrain, of feet of ascents per mile, of degrees of curvature per mile, and of the frequency of ascending grades which exceed one per cent in steepness. The average California intrastate length of haul, according to the record, is considerably less than is the average length of haul, within California, for interstate traffic. In view of this fact, the witnesses stated, the cost per mile for originating



or terminating California intrastate traffic at a specific location exceeds that for comparable interstate hauls, since terminal costs must be spread over a shorter trip in the case of the intrastate movements. Other evidence also was offered purporting to show that the cost of intrastate rail freight operation in California is at least equal to, if not greater than, the cost of rendering comparable interstate transportation services.

Applicants introduced evidence concerning over-all operating expenses. These figures were included in exhibits which showed the total system revenues and expenses of the seven principal California lines for the years 1948-1955 inclusive. The exhibits also showed the total freight and total passenger revenues separately, but no segregation of operating expenses as between freight and passenger traffic was made. Additionally, applicants introduced operating results for the year 1955, adjusted to give effect, for the full year, to the six per cent increase in freight rates authorized early in 1956 for interstate traffic, and assuming its application to intrastate traffic in all states served by the carriers included in the showing. The adjusted figures also gave effect, on a full year's basis, to increases in wages and other operating expenses, including taxes, which the carriers experienced in 1955 and in 1956 prior to the hearings in this proceeding. Predicated on applicants' assumption that the volume of traffic which they enjoyed in 1955 would continue on substantially the same levels during 1956, these adjusted revenue and expense data reflect their best estimate of operating results under the six per cent increase, for the seven carriers shown. The actual operating results

for the three years 1953-1955, inclusive, and the adjusted 1955 results are shown in Table II, below.

Table II  
Over-all Operating Results of Seven  
Principal Lines and Totals

| <u>Line</u>             | <u>Year</u> | <u>Revenues</u> | <u>Expenses</u> | <u>Net Operating<br/>Income</u> |
|-------------------------|-------------|-----------------|-----------------|---------------------------------|
| Southern<br>Pacific     | 1953        | \$546,126,794   | \$499,020,607   | \$47,106,187                    |
|                         | 1954        | 498,864,505     | 456,729,722     | 42,134,783                      |
|                         | 1955        | 529,717,935     | 480,192,830     | 49,525,105                      |
|                         | 1955        | 554,091,473     | 505,521,790     | 48,569,683                      |
|                         | (Adj.)      |                 |                 |                                 |
| Santa Fe                | 1953        | 613,531,000     | 538,422,000     | 75,109,000                      |
|                         | 1954        | 532,292,000     | 468,302,000     | 63,990,000                      |
|                         | 1955        | 578,034,000     | 504,261,000     | 73,773,000                      |
|                         | 1955        | 604,123,776     | 529,756,094     | 74,367,682                      |
|                         | (Adj.)      |                 |                 |                                 |
| Northwestern<br>Pacific | 1953        | 13,040,686      | 12,371,874      | 668,812                         |
|                         | 1954        | 13,318,625      | 12,359,704      | 958,921                         |
|                         | 1955        | 14,272,233      | 14,289,245      | (17,012)                        |
|                         | 1955        | #               | #               | #                               |
|                         | (Adj.)      |                 |                 |                                 |
| Pacific<br>Electric     | 1953        | 27,330,231      | 27,085,258      | 244,973                         |
|                         | 1954        | 12,672,119*     | 12,834,435*     | (162,316)                       |
|                         | 1955        | 15,608,636      | 14,393,561      | 1,215,075                       |
|                         | 1955        | 16,232,973      | 15,113,128      | 1,119,845                       |
|                         | (Adj.)      |                 |                 |                                 |
| Union<br>Pacific        | 1953        | 530,024,300     | 501,164,374     | 28,859,926                      |
|                         | 1954        | 481,786,451     | 452,224,901     | 29,561,550                      |
|                         | 1955        | 509,362,476     | 465,622,984     | 43,739,492                      |
|                         | 1955        | 532,498,852     | 489,301,198     | 43,197,654                      |
|                         | (Adj.)      |                 |                 |                                 |
| Western<br>Pacific      | 1953        | 59,244,506      | 50,718,470      | 8,526,036                       |
|                         | 1954        | 48,118,749      | 42,452,119      | 5,666,630                       |
|                         | 1955        | 53,749,777      | 46,441,621      | 7,308,156                       |
|                         | 1955        | 56,349,777      | 48,795,621      | 7,554,156                       |
|                         | (Adj.)      |                 |                 |                                 |
| Great<br>Northern       | 1953        | 268,034,981     | 240,504,325     | 27,530,656                      |
|                         | 1954        | 250,254,361     | 226,028,113     | 24,226,248                      |
|                         | 1955        | 267,095,219     | 236,940,777     | 30,154,442                      |
|                         | 1955        | 279,616,219     | 249,908,777     | 29,707,442                      |
|                         | (Adj.)      |                 |                 |                                 |

(Adj.) Adjusted for increased revenues under I.C.C. Ex Parte 196, including all proposed intrastate increases, and for increases in operating expenses which have been experienced since the beginning of 1955.

( ) Indicates loss.

# Not of record.

\* Passenger operations discontinued in 1953.

Applicants included in their presentation total investment figures for each of the seven principal roads. As in the case of the expenses, the carriers asserted that they could not make a reliable determination of assets properly assignable to their California intrastate traffic. Their witnesses asserted that the problem of assigning the investment in fixed property and equipment to intrastate service is even more complicated than that of segregating the expenses. This is so, they said, because all the property and equipment are used in common by both interstate and intrastate traffic, and because the units of use are not as well defined as in the case of expense separations. However, the investment would necessarily be segregated first between freight and passenger services, then between interstate and intrastate traffic. It was the opinion of applicants' witnesses that no separation of investment could be made on an actual basis, and that any separation made on an arbitrary basis would be unreliable.

The investment data offered by applicants show the average investment for each of the years 1948-1955, inclusive, on two different bases. The first basis reflects the figures developed by the Interstate Commerce Commission; the second reflects the carriers' book records. Both bases include materials, supplies and cash and, in both, deductions of accrued depreciation and amortization have been made.<sup>5</sup> Using the net operating income figures shown in Table II, applicants calculated their system rates of return, under both investment bases, for each of the years involved. In Table III are shown the investment totals and the corresponding rates of return, under both bases, of the seven principal applicants, for the years 1953-1955, inclusive. Estimated rates of return as

<sup>5</sup>

It is the view of applicants as expressed by their accounting witnesses that the so-called I.C.C. elements of value do not reflect the true cost of carrier properties for the determination of rates of return and that the carriers' book values are more representative for that purpose.

reflected by the adjusted 1955 revenue and expense figures are also shown.

Table III

Investment and Rate of Return of Seven  
Principal Roads and Totals

| Line                    | Year  | Investment     |                  | Rate of Return<br>(Per Cent) |         |
|-------------------------|---|----------------|------------------|------------------------------|---------|
|                         |   | I.C.C.         | Company          | I.C.C.                       | Company |
| Southern<br>Pacific     | 1953  | \$ 989,197,166 | \$1,352,752,570  | 4.76                         | 3.48    |
|                         | 1954  | 1,021,083,466  | 1,381,527,157    | 4.13                         | 3.05    |
|                         | 1955  | 1,033,146,083  | 1,392,817,019    | 4.79                         | 3.56    |
|                         | 1955<br>(Adj.)  | 1,033,146,083  | 1,392,817,019    | 4.75                         | 3.49    |
| Santa Fe                | 1953  | 1,173,559,000  | 1,283,138,000    | 6.40                         | 5.85    |
|                         | 1954  | 1,191,639,000  | 1,308,643,000    | 5.37                         | 4.89    |
|                         | 1955  | 1,200,575,000  | 1,317,944,000    | 6.14                         | 5.60    |
|                         | 1955<br>(Adj.)  | 1,200,575,000  | 1,317,944,000    | 6.19                         | 5.64    |
| Northwestern<br>Pacific | 1953  | 34,934,405     | 58,307,246       | 1.91                         | 1.15    |
|                         | 1954  | 35,906,499     | 58,051,524       | 2.67                         | 1.65    |
|                         | 1955  | 36,648,326     | 57,973,853       | -                            | -       |
|                         | 1955<br>(Adj.)  | 36,648,326     | 57,973,853       | #                            | #       |
| Pacific<br>Electric     | 1953  | (1)            | 60,687,634       | (1)                          | .40     |
|                         | 1954  | (1)            | 52,865,879       | (1)                          | -       |
|                         | 1955  | (1)            | 51,455,569       | (1)                          | 2.36    |
|                         | 1955<br>(Adj.)  | (1)            | 51,455,569       | (1)                          | 2.18    |
| Union<br>Pacific        | 1953  | 897,417,387    | 1,117,089,068    | 3.22                         | 2.58    |
|                         | 1954  | 937,534,850    | 1,167,806,006    | 3.15                         | 2.53    |
|                         | 1955  | 975,412,099    | 1,211,526,241    | 4.48                         | 3.61    |
|                         | 1955<br>(Adj.)  | 975,412,099    | 1,211,526,241    | 4.43                         | 3.57    |
| Western<br>Pacific      | 1953  | 134,597,363    | 148,246,868      | 6.33                         | 5.75    |
|                         | 1954  | 141,866,302    | 155,393,331      | 3.99                         | 3.65    |
|                         | 1955  | 148,102,338    | 161,580,778      | 4.93                         | 4.52    |
|                         | 1955<br>(Adj.)  | 148,102,338    | 161,580,778      | 5.10                         | 4.68    |
| Great<br>Northern       | 1953  | 621,000,600    | 671,511,602      | 4.43                         | 4.10    |
|                         | 1954  | 622,544,893    | 677,951,530      | 3.89                         | 3.57    |
|                         | 1955  | 633,474,388    | 689,113,438      | 4.76                         | 4.38    |
|                         | 1955<br>(Adj.)  | 633,474,388    | 689,113,438      | 4.69                         | 4.31    |
| Totals                  | 1953(2)   | 3,850,705,921  | 4,691,732,988    | (2)4.88                      | 4.01    |
|                         | 1954(2)   | 3,950,575,010  | 4,802,238,427    | (2)4.22                      | 3.46    |
|                         | 1955(2)   | 4,027,358,234  | 4,882,410,898    | (2)5.08                      | 4.21    |
|                         | 1955(3)<br>(Adj.)   | 3,990,709,908  | (4)4,824,437,045 | (3)5.10                      | 4.24(4) |
| (Adj.)                  | Refers to rates of return based on net railway income produced by adjusted 1955 revenue and expense figures as shown in Table II. |                |                  |                              |         |
| #                       | No adjusted revenue and expense figures for Northwestern Pacific Railroad Company are included in the record.                     |                |                  |                              |         |
| (1)                     | Pacific Electric Railway Company investment figures on basis of I.C.C. valuation are not of record.                               |                |                  |                              |         |
| (2)                     | Exclusive of Pacific Electric Railway.  |                |                  |                              |         |
| (3)                     | Exclusive of Pacific Electric Railway Company and Northwestern Pacific Railroad Company.  |                |                  |                              |         |
| (4)                     | Exclusive of Northwestern Pacific Railroad Company.   |                |                  |                              |         |

The record discloses that the net railway operating income figures shown in Table II reflect the inclusion, in tax accruals chargeable to operating expense, of income taxes on nonoperating income. This practice, the accounting witness stated, conforms to the income statement arrangement prescribed by the Interstate Commerce Commission. The Santa Fe witness stated that exclusion of the tax item in question from that carrier's operating expenses, and making other necessary adjustments, would change the 1955 net railway operating income figure from \$73,773,000 to \$72,226,000. No corresponding figures for other years were given, nor were any disclosed for the other applicants whose net railway operating income is of record.

The accounting witnesses testified that the net railway operating figures as shown in Table II and the rates of return as set forth in Table III are greater than they normally would be because of the federal income tax credit resulting from the use of accelerated amortization. The witnesses explained that, under the provisions of the Internal Revenue Act, the rail lines are permitted, for income tax purposes, to amortize, over a period of five years, a portion of certain capital expenditures which have been certified by the federal government as being in the interest of national defense. The effect of these provisions is to increase, for tax purposes, depreciation expense, with a corresponding reduction in income taxes and an increase in net railway operating income. The witnesses pointed out, however, that under I.C.C. rules, the carriers are permitted to charge to operating expenses only the normal depreciation expense. Hence, the records of the companies do not reflect the additional amortization expense allowed by the Internal Revenue Department for income tax purposes.<sup>6</sup> Assuming that income

6

Normal depreciation periods vary, depending upon the particular facility. The record indicates that the normal depreciation period for a typical diesel-electric locomotive is 20 years.

tax rates do not decline, the witnesses stated, the savings in income taxes experienced during the period of accelerated amortization will have to be made up in the form of greater income tax payments in the later years, when normal depreciation still to be charged to operating expense will not be allowed as a deduction from taxable income. They asserted, therefore, that under accelerated depreciation there is no actual tax saving, but only a deferment, and that, consequently, the net operating revenue figures and rates of return shown in their exhibits for all years since 1949<sup>7</sup> are overstated. It was explained that the carriers have taken advantage of the accelerated amortization provisions in order to make available additional funds with which to augment their rolling stock and other facilities.<sup>8</sup>

In Table IV below are shown, for the years 1951-1955, inclusive, the net operating revenues of Southern Pacific Transportation System and rates of return of that system and of the Santa Fe, as recorded, and as those items would be if accelerated amortization had not been utilized. These are the only comparisons of this nature contained in the record. No similar showing was made for the rest of the applicants.

---

<sup>7</sup> January 1, 1950, is the effective date of the present I.C.C. rule under which normal depreciation accounting is required for assets on which accelerated amortization for tax purposes has been applied.

<sup>8</sup> The accounting witnesses admitted that if the carriers, instead of securing additional funds through accelerated amortization, had borrowed the money with which to buy new equipment, they would have incurred interest expense.

Table IV

Comparison of Net Railway Operating  
Income and Rates of Return With and Without  
Accelerated Depreciation

|   | <u>Net Railway Operating<br/>Income</u>      |   | <u>Rate of Return<br/>(On Carrier Valuation)</u>            |  |
|---|--|---|---|--|
|   | <u>With<br/>Accelerated<br/>Depreciation</u> | <u>Without<br/>Accelerated<br/>Depreciation</u> | <u>With<br/>Accelerated<br/>Depreciation<br/>(Per Cent)</u> | <u>Without<br/>Accelerated<br/>Depreciation<br/>(Per Cent)</u> |
| Southern Pacific Transportation System* |  |   |   |  |
| 1951                                    | \$45,382,000                                 | \$42,119,000                                    | 3.63  | 3.37   |
| 1952                                    | 58,096,000                                   | 51,694,000                                      | 4.44  | 3.94   |
| 1953                                    | 47,106,000                                   | 36,710,000                                      | 3.48  | 2.71   |
| 1954                                    | 42,135,000                                   | 28,542,000                                      | 3.05  | 2.07   |
| 1955                                    | 49,525,000                                   | 35,172,000                                      | 3.56  | 2.53   |
| Santa Fe                                |  |   |   |  |
| 1951                                    | #  | #   | 4.58  | 4.45   |
| 1952                                    | #  | #   | 6.12  | 5.78   |
| 1953                                    | #  | #   | 6.01  | 5.47   |
| 1954                                    | #  | #   | 4.45  | 3.76   |
| 1955                                    | 73,773,000                                   | 62,739,000                                      | 5.52  | 4.76   |

\* Comprised of Southern Pacific Company (Pacific Lines), its leased lines and Texas and New Orleans Railroad Company.

# The adjustment to income for these years was not shown.

Applicants claim that the increased revenues which they anticipate under the six per cent rate increase authorized by the I.C.C. on interstate freight traffic and the proposed increases on intrastate traffic will, in the main, be more than offset by the increases in operating expenses which they have experienced since the beginning of 1955. Thus, it will be seen from a review of the adjusted 1955 figures that, of the seven carriers for which estimated operating results are shown, only the Santa Fe and Western Pacific forecast more favorable operating results than were experienced in 1955. The estimated increase in net railway operating income for both of these carriers is relatively slight.

The record discloses, however, that the forecasts of operating results do not take into account additional revenue which the carriers are receiving as a result of increases granted in proceedings other than I.C.C. Ex Parte No. 196 and related intrastate applications. A witness for Southern Pacific estimated that, on an annual basis, his company would receive additional revenues amounting to \$534,835 as a result of this Commission's Decisions Nos. 51688 of July 17, 1955, and 52971 of April 24, 1956, in Case No. 5432, hereinbefore mentioned.<sup>9</sup> Of this amount, the witness said, \$122,265 is included in 1955 revenues. The balance of \$412,570 is not included in Southern Pacific's forecast of revenues as shown in Table II. A Santa Fe witness estimated that the additional revenue which that line would receive annually, pursuant to Decision No. 52971 only, would approximate \$79,000. This amount is not included in the Table II forecast. No estimate corresponding to the foregoing was made for the other applicants. Moreover, the rail forecasts did not give effect to the increases authorized in passenger fares in Interstate Commerce Commission Ex Parte No. 202, decision of April 30, 1956 (interstate) and by this Commission's Decision No. 52995 of May 1, 1956, in Applications Nos. 36802 and 36900 (certain California intrastate fares of Santa Fe and Southern Pacific).<sup>10</sup>

With reference to estimates of operating expenses the record indicates that applicants did not give effect to reductions in fuel costs brought about by a new method under development by at least one of the applicants whereby a lower grade of fuel is

---

9

According to this witness, of the amount stated \$5,000 would represent increases which overlap those sought in the application herein.

10

It should be noted also that a further interim increase of one per cent in truck competitive rates of applicants herein is being sought in Third Supplemental Petition No. 74, in Case No. 5432. That matter is now under submission.



used in diesel-electric locomotives when the latter are operating at the higher speeds. However, a rail witness pointed out that the expense forecasts also do not include increases in locomotive fuel prices which have taken place in 1956.

Applicants introduced a series of exhibits which showed on a system basis that the average hourly wage of all employees of the principal California lines had substantially increased since July 31, 1952, the last year prior to 1956 in which there was a general nation-wide increase in freight rates. By certain mathematical procedures applicants developed data purporting to show the estimated annual pay roll increase resulting from wage increases granted between the 1952 date and December 31, 1955. This increase in the case of Southern Pacific, for example, was shown as \$37,441,242, of which \$19,192,381 was assigned to California operations. However, other exhibits of applicants show that during the past four years the average number of rail employees of the major California lines has steadily declined and that their total annual employee compensation chargeable to operating expenses has also declined.<sup>11</sup> Revenue ton miles hauled by these carriers during the above-mentioned period either remained at approximately the same level or increased. The year 1954 was an exception, when a temporary fall-off in traffic was experienced coincident with the general business recession of that year. The decline in the number of persons employed, in the face of a constant or increasing volume of traffic, the carrier witnesses explained, was due to increased operating efficiency, which has been constantly improved by the purchase of more diesel-electric locomotives and the installation of centralized traffic

---

11

An exception is Southern Pacific, whose employee compensation, after declining in 1953 and again in 1954, rose in 1955 to a level slightly higher than that of 1952.

control, as well as by other means. However, applicants' estimate of expenses gave no effect to any further improvement along this line in the future.

An economist employed by applicants presented an exhibit in which were compared, by numerous tables and graphs, the economic growth of California, the western states as a group, and the nation. According to this document, California has progressed more rapidly in recent years than the rest of the country in such matters as population growth, employment of nonagricultural workers, income payments to individuals, and volume of rail traffic.

Applicants do not anticipate that granting of the rate increases sought herein would result in any substantial diversion of rail traffic to other forms of transportation. The principal rate witness testified that this view was supported by experience with previous general rate increases, in which it was found that the carriers' revenues were augmented approximately by the amounts that had been forecast. This witness also stated that, if the increases are authorized, the rail traffic officials will be alert to make downward adjustments in individual rates where it is found that such action is necessary to hold the traffic to the rails.

In prior general increase decisions the Commission has admonished the rail lines to make every effort to remove maladjustments which had resulted from rate reductions to meet unregulated highway competition. Referring to this directive the rate witness mentioned several instances in which applicants herein have secured, or are seeking, authority under Section 454 of the Public Utilities Code to increase specific rates which it was felt were on depressed levels. He stated, however, that experience has shown that efforts to increase individual rates have met with strenuous opposition from the shippers affected and that such increases, if accomplished at all,

can be made effective only after lengthy negotiations and sometimes formal proceedings.

Evidence was introduced also by members of the Commission's staff. One of the exhibits of record is a study of certain economic factors affecting rail freight rates in California, which had been prepared by a staff rate witness, and concerning which he testified. From an analysis of the tables contained in the exhibit the witness found that the ton-mile revenue derived from rail operations within California is considerably greater than that for the nation as a whole; that although in recent years the trend has been upward in the cost, to the California farmer, for goods and services, the prices received by the farmer for his products have steadily declined; that while the California production of agricultural commodities and livestock has increased, the rail carriers for the most part have not secured traffic in proportion to this increase.

The rate witness had found also that the California rail lines had not increased their traffic, particularly that of manufactured goods, commensurate with the great expansion of industry and trade which this State and the country as a whole have exhibited in recent years; and that the California lines are not participating equally with other forms of for-hire transportation in the benefits of that expansion. He pointed to certain reductions in rates which applicants have made since the last general increase in state-wide rail rates, and raised the question as to whether the advance sought herein might cause traffic to move less freely.

Evidence relative to estimated operating results, financial condition and operating efficiency of four of the principal applicants herein was adduced on behalf of the Commission's staff through one of its transportation engineers. This witness had calculated system operating results for the first five months of 1956

and had projected these data to cover a 12-month period. His figures showed the results on three bases, viz.: (a) unadjusted, (b) adjusted to eliminate the additional revenue received on interstate traffic under I.C.C. Ex Parte 196, and (c) adjusted to show the effect for a full year of that increase in rates, including all corresponding increases sought or granted on intrastate traffic. The estimated net operating income and rates of return (on I.C.C. valuation) as thus calculated for the carriers in question are set forth in Table V below.

Table V  
Operating Results for  
First Five Months of 1956 - Annualized

| <u>Carrier</u>   | <u>Unadjusted</u> | <u>Adjusted<br/>to Eliminate<br/>Ex Parte 196<br/>Increase</u> | <u>Adjusted<br/>to Include Ex Parte<br/>196 Increase for<br/>Full Year</u> |
|------------------|-------------------|--|--|
| Southern Pacific |                   |  |  |
| Net Ry.Op.Income | \$33,335,231      | \$27,120,770   | \$39,836,953   |
| Rate of Return   | 3.18%             | 2.59%  | 3.80%  |
| Santa Fe         |                   |  |  |
| Net Ry.Op.Income | \$49,468,265      | \$43,174,843   | \$56,354,497   |
| Rate of Return   | 4.12%             | 3.60%  | 4.69%  |
| Union Pacific    |                   |  |  |
| Net Ry.Op.Income | \$41,127,502      | \$34,857,350   | \$46,856,701   |
| Rate of Return   | 4.22%             | 3.57%  | 4.80%  |
| Western Pacific  |                   |  |  |
| Net Ry.Op.Income | \$ 5,446,515      | \$ 4,718,538   | \$ 6,029,352   |
| Rate of Return   | 3.68%             | 3.19%  | 4.07%  |

In developing the foregoing estimates, which relate to freight and passenger services combined, the staff engineer used the recorded book figures of operating expenses. In annualizing the expenses, the record shows, he did not give effect to certain increased cost factors which became effective in 1956. Income taxes were calculated on the basis of normal depreciation rates, and excluded the effect of accelerated depreciation.

With the exception of the Union Pacific estimate, the staff witness' forecast of operating results is somewhat less favorable than that of the carrier witnesses. However, in making the comparison the different treatment accorded some of the expense and tax items in the staff and carrier estimates must be kept in mind. The staff estimate was based on the first five months of 1956, while applicants bottomed their forecasts on the 1955 experience.

In a separate series of exhibits the staff engineer developed for each of the years 1951-1955, inclusive, and for each of these same four lines, the total freight operating expense per thousand revenue ton miles, and the average hourly compensation of all employees, including those in freight and passenger service. The results of that analysis are summarized in Table VI, below.

Table VI

Total Freight Service Operating<sup>#</sup> Expense  
per 1,000 Revenue Ton Miles and Average  
Hourly Compensation of All Employees

| <u>Line</u>         | <u>1951</u> | <u>1952</u> | <u>1953</u> | <u>1954</u> | <u>1955</u> |
|---------------------|-------------|-------------|-------------|-------------|-------------|
| Southern Pacific    |             |             |             |             |             |
| Operating Expense   | \$11.61     | \$12.03     | \$12.43     | \$11.33     | \$11.51     |
| Hourly Compensation | 1.80        | 1.91        | 1.94        | 1.99        | 2.01        |
| Santa Fe            |             |             |             |             |             |
| Operating Expense   | 11.22       | 12.36       | 12.49       | 11.57       | 11.39       |
| Hourly Compensation | 1.77        | 1.87        | 1.91        | 1.98        | 1.99        |
| Union Pacific       |             |             |             |             |             |
| Operating Expense   | 10.39       | 10.99       | 11.11       | 10.51       | 10.29       |
| Hourly Compensation | 1.78        | 1.89        | 1.92        | 1.98        | 1.96        |
| Western Pacific     |             |             |             |             |             |
| Operating Expense   | 10.58       | 11.02       | 10.90       | 10.82       | 10.62       |
| Hourly Compensation | 1.84        | 1.96        | 1.99        | 2.06        | 2.10        |

# Includes tax accruals and net equipment and joint facility rents.

The staff witness pointed out that while average hourly compensation of all employees of the four roads studied had reflected an upward trend during the period in question, freight operating

expenses per thousand revenue ton miles were, in 1955, approximately the same as, or slightly lower than, they were in 1951. This latter situation he attributed to the increased operating efficiency of the carriers.

The engineer adduced evidence also relative to average market prices of common stocks, to earnings price ratios, and to actual or contemplated stock splits, of the four roads included in his study. These data, in his opinion, reflect a favorable position of the railroads in the investors' eyes and demonstrate the high degree of financial health of those carriers.

Relative to the problem of separating intrastate expenses and investments, the engineer testified concerning, and adopted as his own, the views set forth in a study which was made a part of the record in I.C.C. Docket No. 31219, supra. The study in question, which was assigned Exhibit No. 112 in the interstate proceeding, was prepared by a supervising transportation engineer then employed by this Commission. It purported to contain a practicable scheme, set forth in general outline, for the accomplishment of such separations. The study was incorporated in the record herein as Exhibit No. 65, and at request of applicants there was also made a part of this record, as Exhibit No. 68, a transcript of the testimony of a rail accounting witness in the above-mentioned interstate matter in which that witness stated why the aforementioned separations plan was, in his opinion, unworkable.

California Trucking Associations, Inc., a state-wide nonprofit organization of highway carriers, supported the granting of the sought increases. A witness for the association pointed out

that most of the intrastate rail carload commodity rates are not subject to the Commission's minimum rate orders and that such rates may be observed by highway carriers in lieu of the established minimum rates for the same transportation when lower charges result thereby. The witness testified that because of the competitive situation the highway carriers are compelled to meet the rail rates and that the association members, as a group, derive as much revenue from the rail rates, applied under the alternative provisions, as from all other rates. He asserted that the rail rates which the highway carriers are forced to meet are depressed and that increases therein are justified. In the opinion of the witness, there would be no substantial diversion of traffic from rails to trucks if the sought increases were granted.

Shipper representatives directed attention to the continuing decline in rail movement and the trend toward proprietary trucking operations which they had observed in connection with the commodities in which they were interested. They asserted that these trends had been encouraged by the series of horizontal rate increases which the rail lines have been granted since World War II. These witnesses felt that applicants, in order to regain the lost traffic, should not seek increases but should reduce their rates.

Other shipper representatives testified that the depressed condition of agriculture requires that no increases be made in rates which affect the economy of the farmers.<sup>12</sup> Moreover, they asserted, the granting of the sought increases would give further impetus to current inflationary tendencies. Still others alleged that

---

12

Applicants herein propose maximum increases or "hold-downs" on fresh fruits, vegetables and melons and on certain fertilizer materials. Rates on grain, grain products and related articles and on livestock would be increased by five per cent.

applicants had failed to make the necessary justification of their proposal, since they did not offer evidence of intrastate operating expenses and investment.

The representative of a shipper of gypsum, plaster and plasterboard, whose plant is located at Arden, Nevada, a point near the California line, testified that rates applicable from that plant to California markets have been increased under I.C.C. Ex Parte No. 196. Since the rates from competing California mills to those same markets have not been increased correspondingly, his client, the witness said, has been placed at a disadvantage in that it is compelled to absorb the difference in rates thus created. While he did not advocate an increase in California rates, per se, he urged that the former equality of rates on plaster as between the California and Nevada producing points be restored as expeditiously as possible. His purposes would be served, he said, if the Ex Parte No. 196 increases were removed from the Arden rates.

As hereinbefore mentioned, counsel for the Commission's staff moved that the application herein be denied and the proceeding dismissed. In support thereof he argued, inter alia, that applicants had failed to adduce any evidence concerning 25 of the 36 rail applicants or relative to any of the ten highway carriers included in the application; that the carriers had failed to make separate showings of intrastate expenses and investment, relying instead upon a showing of "system" operating results; and that they had defaulted in their survey of so-called low-spot rates. The motion was supported by counsel for various shipper interests.

#### Conclusions

Section 454 of the Public Utilities Code and similar provisions of the Constitution of the State of California prohibit



any increase in rates by common carriers and other public utilities "except upon a showing before the Commission and a finding by the Commission that such increase is justified." It is in the light of these provisions that the Commission must decide whether the relief sought herein should be authorized. Various criteria may be employed to assist us in reaching the proper conclusion. In the following paragraphs some of these will be considered.

As hereinbefore stated, applicants brought into the record figures reflecting California intrastate freight revenues received in 1955 by the major applicants, together with estimates, based on 1955 tonnage, of the additional revenues to be received under the sought increases. However, no attempt was made to show what the actual or estimated intrastate operating expenses were for that period, nor were any estimates made of what the intrastate expenses would amount to had the various increases in wages and other operating expenses, which have taken place since the beginning of 1955, been in effect throughout that year. In the absence of these expense figures we are unable to determine what the net railway operating income position of the carriers in question was as to California intrastate traffic, for the last full calendar year, to say nothing of earlier periods. Similarly, in view of the above-mentioned lack, it is impossible to estimate what the operating results might be in the handling of said intrastate traffic under the proposed rates. The foregoing observations apply also to applicants' failure to offer evidence as to their intrastate operative properties.

The record includes, of course, system operating results, for several years back, as well as estimated system results for the future. However, those figures offer us no reliable indication of the revenue and expense position of applicants as to the transportation here in issue. Moreover, even in the system data no breakdown

was made of expenses, and of net railway operating revenues, as between freight and passenger operations.

The record indicates that the increases in wages and in the cost of fuel, material and supplies, as well as in other operating costs, which have taken place in other states have been experienced equally in California. While there is evidence in the record purporting to show that railway unit operating costs are at least as high in California as in the nation as a whole, there is also evidence that rail revenues per unit of transportation service are, likewise, at least as high in California as elsewhere. Since, moreover, evidence as to the actual operating expenses incurred in the handling of applicants' California intrastate traffic is absent, the net effect of the revenues and expenses assignable to that traffic is not disclosed. Thus, the aforementioned evidence relating to increased operating costs in California is of no assistance in determining whether or not said intrastate traffic is bearing its fair share of the transportation burden.

Operating ratio is one basis commonly utilized, along with others, as a measure of the reasonableness of operating results. Applicants included operating ratios in their exhibits, but here again the ratios relate to system operations, both freight and passenger. Additionally, they were calculated excluding substantial expense items of taxes, and equipment and joint facility rents. This is in accord with the procedure set up in the I.C.C. annual report. There is no testimony, however, in the record as to the reasonableness of the operating ratios as shown for railroad operations. Under the circumstances, the operating ratios of record are of no value for the purposes of this proceeding.

Rate of return is also an important measure of the adequacy of operating results. Applicants, as noted earlier herein, showed the rates of return of the major applicants for their over-all freight and passenger operations for 1955 and several years prior thereto, as well as estimates of what the corresponding rates of return would be under the sought increases. These were shown as computed on both the rate bases developed by the Interstate Commerce Commission and by those predicated on the carriers' book records. As in the case of intrastate operating expenses, no attempt was made to develop rates of return on California intrastate operations. This would require, of course, the calculation of an intrastate rate base.

While the over-all rates of return are helpful in appraising the adequacy of the net railway operating revenues of each of the applicants studied, as a system, and the trends in recent years of such revenues, they are of no assistance to a determination of the issues involved herein which relate exclusively to intrastate rates.

As previously stated, applicants strongly contend that reliable separations of intrastate operating expenses and investment cannot be obtained. Evidence introduced by the Commission's staff, on the other hand, supports the position that such separations are feasible. The testimony of applicants' witnesses in this proceeding, and that reproduced in Exhibit No. 68, supra, convey the impression of a manifest desire to search out reasons why the separations cannot be made, instead of willingness to adopt an open-minded attitude in the solution of the problem. Naturally, allocations would, in many instances, be necessary. And, while they might be somewhat inaccurate in the initial formulations, with the accumulation of experience they should reflect reliability. The evidence of record is convincing that the development of such separations procedures is feasible, as

it has proven to be in connection with similar problems in other public utility fields. With respect to the cost of developing the underlying data, the record shows that modern electronic computing machines are now available, which expedite and greatly facilitate the accumulation and processing of large masses of accounting, operating and other statistical data. It is a matter of common knowledge that some rail lines have already acquired such equipment and are using it extensively.

Staff counsel, in his motion for denial of the application, argued that intrastate revenues, expenses and investment are mandatory in proceedings of this kind, whereas applicants, in their reply thereto, urged the contrary. Numerous court and Interstate Commerce Commission decisions were cited in support of the respective positions. The most important case cited appears to be that of Mississippi Public Service Commission v. U. S. of America and the I.C.C., 124 F. Supp. 809 (affirmed by the United States Supreme Court in 349 US 908). Applicants and staff counsel take divergent views of the conclusions to be drawn therefrom. A review of the district court decision discloses that therein the court upheld a decision of the Mississippi Public Service Commission which denied, or granted only in part, as to certain commodities, increases in Mississippi intrastate rail rates corresponding to those authorized in I.C.C. Ex Parte 175. A Section 13 decision of the Interstate Commerce Commission seeking to supersede the decision of the Mississippi Commission was set aside and enjoined by the United States District Court in that case, which action was sustained by the Supreme Court of the United States. The reasons given for the court's finding included, inter alia, the failure of the Mississippi railroads to make separations as to intrastate revenues, expenses and properties.

As applied to the prescription of intrastate rates by State authority, it is jurisdictional that the intrastate revenues, expenses and properties be ascertained. (Smith v. Illinois Bell Telephone Co., 282 U.S. 133, 148-149, 75 L. ed. 255, 263--involving telephone service--; Simnson v. Shepard, 230 U.S. 352, 435, 57 L. ed. 1511, 1556--involving rail freight and passenger service--.) Findings on these issues must be made. (Smith v. Illinois Bell Telephone Co., supra, pages 148-149 U.S. Reports; Railroad Commission v. Maxcy, 281 U.S. 82, 83, 74 L. ed. 717, 718.) Telephone, telegraph, gas, electric and water utilities operating both in interstate and intrastate commerce are required to separate their operating results for the purpose of rate fixing. The same is true of passenger carriers by motor vehicle. These utilities have not available to them the privileged refuge of a Section 13 as do the railroads. These other utilities find separation feasible because the law compels it. The railroads may seek shelter in Section 13 of the Interstate Commerce Act, thus circumventing the rule of law by which other utilities are bound.

Applicants herein adduced certain other evidence in which "California operations" were segregated from over-all operations. These data, however, were not confined to California intrastate traffic, but included the California portions of shipments moving by rail between this State and other states as well as interstate traffic moving between California interior points and the ports. Under the circumstances, the data in question do not furnish a guide to the intrastate revenue needs of applicants.

With respect to the lack of any evidence in the record concerning 25 of the rail applicants<sup>13</sup> and the ten highway carriers<sup>14</sup> it is pertinent to quote here from a recent decision of this Commission relating to the question of increasing warehouse rates within the San Francisco Bay area. In that decision the Commission said:

"As a matter of general practice the Commission will expect all applicants in a joint proceeding to make their respective financial and other showings as necessary elements looking toward a rate adjustment. The Commission's consideration of the instant matter is not to be taken as a precedent, neither generally, nor specifically to the type of utilities which are applicants here."<sup>15</sup>

It appears that in excess of 90 per cent of the California intrastate revenues earned by all the rail applicants accrued to the eleven carriers for which some showing was made. This fact, however, is not justification of a need of increased revenues for the rest of the applicant carriers.

The only comment that need be made concerning the so-called "low-spot" rates is that applicants will be expected to continue assiduously their review of carload commodity rates applicable between points in this State, singling out those which appear to be depressed, and taking the necessary steps to have the latter increased to compensatory levels.

All of the evidence and argument has been carefully considered and appraised. Based upon the evidence, we hereby find

---

13

One of these is San Francisco & Napa Valley Railway. By Decision No. 53827, dated October 1, 1956, in Application No. 38375, that company was authorized to abandon the remaining portion of its line.

14

Increases sought for the applicant highway carriers are limited to joint rail-truck rates.

15

Footnote 3 of Decision No. 53527, dated August 3, 1956, in Application No. 37352.

that applicants have not shown that their present California intra-state rates are unreasonable or otherwise unlawful; neither have they shown that returns upon their California intrastate operations are unreasonable as applied to any of the applicants. Therefore, applicants have failed to sustain the burden of proof that the proposed rate increase is justified. Upon consideration of all the facts and circumstances of record, we are of the opinion and hereby find that the rate increase sought herein has not been justified. The application will be denied. The motion of staff counsel is hereby granted.



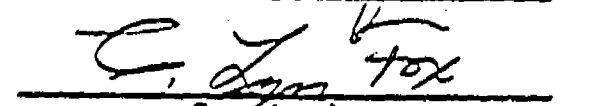
O R D E R

Based upon the evidence of record and on the conclusions and findings set forth in the preceding opinion,

IT IS HEREBY ORDERED that Application No. 37697 be and it is hereby denied.

Dated at San Francisco, California, this 11<sup>th</sup> day of DECEMBER, 1956.

  
President

  
  
  
Commissioners