

ORIGINALDecision No. 61102

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
 FRIEDKIN AERONAUTICS, INC. dba
 PACIFIC SOUTHWEST AIRLINES for order
 authorizing establishment of certain
 local and joint intrastate passenger
 fares applicable to service on
 Lockheed Electra 188C aircraft.

Application No. 42253

McInnis, Focht and Fitzgerald by John W. McInnis,
 for applicant.
 Dion Holm, Thomas M. O'Connor and Robert R. Laughead,
 for City and County of San Francisco,
 interested party.
Franklin Campbell, Harold H. Webster and Timothy J.
Canty, for the Commission staff.

O P I N I O N

Friedkin Aeronautics, Inc., doing business as Pacific Southwest Airlines, conducts an air coach passenger transportation service between San Diego, Los Angeles^{1/} and San Francisco. By application filed May 17, 1960, amended August 8, 1960 applicant seeks authority to increase passenger fares for service provided by its Lockheed Electra 188C aircraft. The following is a tabulation of the present fares and proposed fares.

Pacific Southwest Airlines
One Way Adult Fares

	<u>Present</u>	<u>Proposed</u>	<u>Percent Increase</u>
San Diego - Los Angeles	\$ 5.45	\$ 6.35	16.5%
Los Angeles - San Francisco	11.81	13.50	14.3
San Diego - San Francisco	\$17.26	\$19.85	15.0

Round Trip fares are double the one way fares.
 Children fares are one-half of the adult fares.

1/ Applicant has flights to and from Los Angeles International Airport and Lockheed Air Terminal at Burbank.

Public hearing was held September 16 and 21, 1960 before Examiner Jack E. Thompson at San Francisco.

Applicant's present fares were published May 2, 1958 to become effective June 18, 1958 pursuant to authority granted by Decision No. 56419 dated March 25, 1958 in Application No. 39172.

In November 1959, applicant received the first of three Electra aircraft it had ordered from Lockheed Aircraft Corporation. That aircraft was placed in service, as well as the two delivered in December 1959, during the period November 1959 to January 1960. The change-over in operation from four DC-4 aircraft to 3 Lockheed Electras was completed in January 1960. Subsequent to the change-over in operations, applicant had installed in San Francisco and in Los Angeles a new communications system for handling reservations. It contemplates placing the new system in San Diego in the near future.

Prior to the change-over in operations to Electras, applicant operated four DC 4's with a seating capacity of 70 passengers each on a schedule during the peak season of 82 flights per week and about 70 flights per week during the period between New Years and Easter. The Electras have a seating capacity of 98 seats and applicant presently operates a schedule of 132 flights per week.

On March 25, 1960 speed restrictions on the operations of Electras were imposed by the Administrator of the Federal Aviation Agency in an emergency airworthiness regulation issued following some in-flight accidents. This has resulted in increasing the flight hours necessary to operate the schedules. Lockheed Aircraft Corporation and applicant have entered into an agreement whereby Lockheed will make certain modifications in the airplanes without

cost to applicant which will remove them from the F.A.A. speed restrictions. The modifications will require approximately one month's work on each airplane. The dates such airplanes will be out of service as presently scheduled are:

1st Airplane: January 25, 1961 to February 21, 1961
2nd Airplane: February 22, 1961 to March 21, 1961
3rd Airplane: April 20, 1961 to May 17, 1961

Applicant's president testified that Lockheed will not furnish a plane to substitute for the ones taken out of service and that as far as may be determined now, the operations conducted during those periods will be with two aircraft.

Applicant presented an estimate of the results of operation for a year ending June 30, 1961 under present fares and under proposed fares. An engineer of the Commission's staff presented estimates for the same period. In the form presented the estimates are not comparable. Applicant's estimates have been rearranged in Table I in order to provide some degree of comparability. There are a number of differences in assumptions by the applicant and by the engineer in making their forecasts. The engineer included charter operations of the DC-4 airplanes as they affect revenues and expenses, including depreciation, and rate base, whereas applicant included only the Electras and revenues and expenses in connection with the scheduled operations of those planes. Applicant assumed operations with two Electra airplanes during the periods from January 25 through May 17, mentioned above, when the aircraft are scheduled for modification, whereas the engineer assumed a regular continuation of service throughout the rate year. The engineer estimated that maintenance expense for the rate year would be about the same as the book record for January through June annualized, whereas applicant assumed that its maintenance expense would increase greatly after November and December because of the expiration of warranties on the Electra parts and equipment. Table I shows the estimates presented by applicant and by the commission's staff.

TABLE 1
SUMMARY OF ESTIMATES
OF RESULTS OF OPERATIONS

Item	1		2		3		4		5	
	Adjusted Bk. Record	Jan.-June 1960	Annualized*	Applicant	Staff	Present Fares	Staff	Proposed Fares	Applicant	Staff
Revenue										
Passenger	\$6,639,998	\$7,126,112	\$7,274,000	\$7,654,946	\$8,035,880					
Contract & Charter	102,603	-	118,420	-	118,420					
Other	46,447	-	52,990	-	52,990					
Total	\$6,789,048	\$7,126,112	\$7,445,410	\$7,654,946	\$8,207,290					
Expenses:										
Flying	\$1,725,205	\$2,255,946	\$1,715,160	\$2,255,946	\$1,715,160					
Maintenance & Hangar	1,339,080	1,343,034	1,309,980	1,343,034	1,309,980					
Ticketing & Dispatching	1,079,832	768,000	939,880	768,000	939,880					
Traffic & Adv.	361,870	619,992	391,800	619,992	391,800					
Administrative	667,939	343,992	713,250	343,992	733,090					
Operating Taxes	120,357	285,000	249,700	285,000	249,700					
Depreciation	1,207,300	1,496,292	1,207,300	1,496,292	1,207,300					
Total	\$6,501,583	\$7,112,256	\$6,527,070	\$7,112,256	\$6,546,910					
Income before Income Taxes	\$287,465	\$13,856	\$918,340	\$542,690	\$1,660,380					
Income Tax	100 ⁽¹⁾	(2)	100 ⁽¹⁾	(2)	390,760					
Net Income	\$287,365	(2)	\$918,240	(2)	\$1,269,620					
Operating Ratio - %	95.8	98.4	87.7	96.4	84.5					
Rate Base	\$7,767,820	\$9,987,107	\$7,767,820	\$9,987,107	\$7,767,820					
Rate of Return - %	3.7	0.08	11.8	2.7	16.3					

* Column 1 was developed by the Commission's engineer in Exhibit No. 4, and represents adjustments in book records to remove non-recurring expenses such as training pilots in operation of Electras, elimination of interest and uncollectible expense and computation of depreciation on straight-line method rather than the double declining balance method; the adjustments are as follows:

	Book Record	Adjustment	Adjusted Balance
Flying Expense	\$2,090,693	\$ 365,488	\$1,725,205
Administrative Expense	1,465,359	797,420	667,939
Depreciation	2,258,167	1,050,867	1,207,300

(1) Interest and high depreciation expense computed on double declining balance provides minimum income tax.

(2) Applicant did not supply these figures.

We cannot accept applicant's estimates for rate making purposes. While, as contended by applicant, it may be that the taking of depreciation on aircraft on the double declining balance method will reflect the market value of the aircraft at any given time more closely than if depreciation is taken on the straight-line method, we are concerned here with the fixing of reasonable rates for the use of the aircraft in transporting the public. In cases such as that involved here where the principal assets have been acquired at one time and accelerated methods of depreciation are used, revenues which would be required during the first years of service to cover depreciation expenses would be many times over that required during the latter years. If the fares of applicant were to be reviewed annually, the result would be high fares the first year and lower fares each succeeding year until new airplanes were acquired. There would be very little stability of fares in such circumstances. Furthermore, although interest is an expense actually borne by applicant, it is an expense related to capital and not to operations. For rate making purposes, interest is not included as an operating expense but is considered in determining the revenue needs of the carrier in the rate of return.

With respect to the estimates of the Commission's staff, with very minor exception, the estimates of revenues and expenses reflect the operating conditions the engineer assumed would exist in the future. The record shows however, that those assumed operating conditions will probably not occur because of unusual circumstances in this case. Applicant is required by the F.A.A. to operate the Electras at reduced speed until modifications are made in the aircraft. The reduction in speed of aircraft has reduced

the efficiency of the operation. Applicant has contracted with Lockheed Aircraft Corporation to have the modifications in the aircraft made. For three months applicant will have only two operational aircraft instead of three. Applicant is required by contract to sell the DC-4 aircraft when there is a reasonable market for them. While the operation of DC-4 aircraft in substitution for Electra aircraft was conducted during the change-over period, it is an inefficient and costly procedure according to applicant's president. He further testified that he would not operate the DC-4's in the regular service even if they are still available for use. The first six months of 1960 was not a period of normal operations and, from the evidence, it appears that the twelve months ending June 30, 1961 also will not be a period of normal operations. Under such circumstances it is difficult to estimate what the operating results of applicant for that period might be. From the evidence, we are of the opinion that the results will be somewhat less favorable than estimated by the engineer and that the rate of return on the rate base estimated by the engineer will be somewhere between ten and thirteen percent. Assuming it to be the latter, is such a return reasonable for the operations to be conducted by this applicant? We find that special and unique circumstances surrounding that operation require a finding that it is reasonable.

Applicant has no certificate of public convenience and necessity; no such authorities are required for transportation by aircraft when the operations are conducted wholly within California. It has received no subsidy nor can it expect any in the form of direct subsidy or mail contracts should it be faced with operating losses. As of June 30, 1960 the book value of fixed assets, other than

aircraft and rotatable Electra parts, is \$137,341. According to the applicant's president, the market value of the three DC-4 aircraft is not over \$50,000 each. The purchase cost of the three Electras together with four spare motors, three spare propellers and four Q.E.C.'s (housings around the engines) was \$8,035,631. Applicant arranged the purchase of this equipment from Lockheed Aircraft Corporation through Electrahilt Corporation under a form of lease-purchase agreement. Applicant placed a cash deposit with Electrahilt which will constitute the last payment on the five year contract. For the year ending June 30, 1961 applicant will be required to pay Electrahilt, in the form of "payments," \$1,482,000. From June 30, 1961 to the end of the term of the agreement the payments are \$128,000 per month. It is obvious that over and above operating expenses, the financial obligations of applicant are very high.

The proposed fares of applicant are still lower than the present fares of the major airlines offering similar service. We take official notice of Application No. 42417 of Western Air Lines, Inc., Application No. 42430 of Trans World Airlines, Inc., Application No. 42435 of Bonanza Air Lines, Inc., Application No. 42452 of American Airlines, Inc., and Application No. 42461 of United Air Lines, Inc., all of which seek increases in fares for transportation between points served by applicant. The fares of United Air Lines are comparable to the fares of the other major airlines. The following table compares the present coach fares and the proposed coach fares of United with those proposed by applicant.

Coach Fares

	<u>P.S.A. Proposed</u>	<u>United Present</u>	<u>United Proposed</u>
San Diego - Los Angeles			
Regular Flight	\$ 6.35	\$ 6.50	\$ 8.00
Turbojet Flight*		7.50	9.00
San Diego - San Francisco			
Regular Flight	19.85	20.85	22.40
Turbojet Flight*		22.85	24.40
Los Angeles - San Francisco			
Regular Flight	13.50	15.05	16.45
Turbojet Flight*		17.05	18.45

* Turbojet flight in the case of United means with DC-8 or Boeing 720 aircraft. In the case of Western and T.W.A. it means with Boeing 707 aircraft.

Applicant's service is in the interest of the public. We find that the proposed increases in fares are justified.

ORDER

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

IT IS ORDERED:

1. That Friedkin Aeronautics, Inc., is authorized to establish, on not less than five days' notice to the Commission and to the public, the increased fares set forth in its amended application filed August 8, 1960 in this proceeding for service provided by Lockheed Electra 188C aircraft.

2. That the authority granted herein shall expire unless exercised within sixty days after the effective date of this order. The effective date of this order shall be twenty days after the date hereof.

Dated at San Francisco, California, this 22nd day of November, 1960.

[Signature]
President

[Signature]

[Signature]

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Commissioners