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ORIGINAL

Decision No. 79499

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Hughes Air Corp.,)
dba Air West, to increase its)
intrastate passenger fares.)

Application No. 52754
(Filed July 16, 1971)

Koteen & Burt, by John W. Simpson, Attorney
at Law, for Hughes Air Corp., dba Air West,
applicant.

Perry H. Taft, Attorney at Law, and Wilmer J.
Garrett, for City of Fresno; Earl D. Murphy,
Attorney at Law, for City of Redding;
Raymond W. Schneider and William J. Losh,
Attorneys at Law, and Dave Zebo, for County
of Humboldt; Mario E. de Solenni, Attorney
at Law, for City of Crescent City; Lawrence
Lazio, for Humboldt Council of Chambers of
Commerce and Eureka Chamber of Commerce;
Al Rosengren, for Del Norte County Chamber
of Commerce and Del Norte County Board of
Supervisors; and Arnie Braafladt, for
Associated Students, Humboldt State College;
protestants.

Edward J. Pulaski, Attorney at Law, for Air
California; George M. Wood, for City of Arcata;
and Mrs. Pat Meyer, for Arcata Area Chamber of
Commerce; interested parties.

Scott K. Carter, Attorney at Law, for the Commission
Staff.

O P I N I O N

Hughes Air Corp., doing business as Air West (hereinafter
Air West or applicant) is a common carrier by air of passengers and
property between points located in various states of the United
States, including California and Canada and Mexico. In the State of
California, applicant operates in intrastate as well as interstate
commerce providing local service between various California cities,
as well as between these cities and points in other states.

Applicant uses the same aircraft or types of aircraft in its intrastate operation which it uses for its interstate operations; namely, Douglas DC-9's and Fairchild F-27's.

In this application, Air West seeks an approximate six percent increase in all its intrastate air fares, except between Eureka-San Francisco and Eureka-Los Angeles.^{1/} The application states that the formula used to construct the proposed intrastate air fares is consistent with the fares for interstate operations that were approved by the Civil Aeronautics Board as a result of the Domestic Passenger Fare Investigation, Order 71-4-59/60, April 9, 1971.

Public hearing was held before Examiner Mallory at San Francisco on November 2 and 3, and in Eureka on November 5, 1971. The matter was submitted on the latter date. Evidence in support of the granting of the application was submitted by applicant and the Commission staff. Protestants appeared in opposition to the granting of increases in air fares between specific points.

Applicant's Evidence

Applicant's evidence was presented by a representative of a firm of consultants which regularly prepares economic data for presentation in regulatory proceedings. The testimony of the witness is summarized in the following statements. The proposed increased fares are identical to the presently effective interstate fares between the same points, and are at the same levels maintained by Air West and other local service airlines operating throughout the

^{1/} The fare formula used to construct the proposed Air West fares is as follows:

"The present fare (excluding tax) is increased by 6%; then multiply the result by 1.08, round to the nearest whole dollar (50 cents and over rounded upward, 49 cents and under rounded downward), and divide the resulting whole-dollar amount by 1.08."

nation. Present intrastate fares became effective January 28, 1971, pursuant to Decision No. 78179 in Applications Nos. 51654 and 51723, and said fares represent an overall increase of approximately 20 percent over prior fares.

The need for increased air fares results from the need for increased passenger revenues for all domestic air-carriers, including Air West. Said revenue deficiencies assertedly result from spiraling costs and lagging traffic growth. Assertedly, Air West has been no exception to the general trend of losses in the airline industry, having incurred operating losses (after subsidy) of \$8.5 million in 1968, \$15.2 million in 1969, and \$5.8 million in 1970; the Air West operating loss in the first quarter of 1971 was \$1.2 million.

The witness stated that in recent periods Air West has attempted to curtail operating losses by sharply reducing management and operating personnel, by disposing of excess aircraft, and by reducing schedules on flights where load factors are low. The witness indicated that establishment of further operating efficiencies of any magnitude are not possible; therefore, Air West's revenue needs must be realized from increased fares.

The witness developed allocations of revenues and expenses of California intrastate operations based on procedures described in his Exhibits AW-20, AW-30 and AW-31. The witness stated that said profit and loss analyses show that intra-California operations account for a substantial portion of Air West's operating losses. He indicated that when revenues and expenses are analysed separately, the reason for the intrastate deficit becomes apparent: California operations accounted for 22.65 percent of Air West's expenses, but produced only 20.45 percent of the system's revenues in the sample period used by the witness.

The witness showed that the average fare applicable to intra-California passengers will increase by about 5.4 percent under

proposed fare levels, and such increased fares will produce estimated additional annual revenues of \$494,000 for 1971, and \$567,000 for 1972, assuming no traffic diversion. It was the testimony of the witness that, in his opinion, the amount of the increase sought is relatively small, and that an increase of such magnitude should cause no significant diversion to other means of transportation.

The witness presented the forecast of Air West's system operations under present fares, as set forth in Table 1 below. He indicated that the data are based on a forecast for the last three quarters of 1971, and that such forecast assumes a market increase of 10 percent over the same period in the prior year. The witness testified that such traffic increase has not materialized; therefore, actual operating results for the 1971 year will be less favorable than his forecast.

TABLE 1
AIR WEST SYSTEM PROFIT AND LOSS FORECAST, 1971
(+000)

Commercial Revenue	\$ 93,031
Operating Expenses	
Direct	\$ 37,866
Indirect	<u>62,553</u>
	\$100,419
Operating Profit (Loss) Before Subsidy	\$ (7,388)
Subsidy	\$ 9,939
Operating Profit after Subsidy	\$ 2,551
Non-Operating Expenses	\$ 2,645
Net Profit (Loss)	\$ (94)

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The following table sets forth Air West's forecast of the results of its California intrastate operations in 1971 and 1972 as set forth in Exhibit AW-21:

TABLE 2
AIR WEST PROFIT AND LOSS FORECAST
California Operations, 1971 and 1972
(+000)

	<u>1971</u>	<u>1972</u>
Commercial Revenue	\$17,168	\$19,744
Operating Expenses:		
Direct	8,327	9,576
Indirect	<u>14,443</u>	<u>16,177</u>
	\$22,770	\$25,753
Operating Profit (Loss) Before Subsidy	(5,602)	(6,009)
Subsidy	3,162	3,037
Operating Profit (Loss) After Subsidy	(2,440)	(2,972)
Non-Operating Expenses	380	373
Net Profit (Loss)	(2,820)	(3,345)
Net Intra-California Profit (Loss)	(1,654)	(1,962)
Projected Revenue Gain from Proposed Fare Increase (full year effect)	<u>494</u>	<u>567</u>
Net Intra-California Profit (Loss) After Proposed Fare Increase	\$(1,160)	\$(1,395)

Staff Evidence

The report of the Commission staff (Exhibit 56) was jointly prepared and presented by a financial examiner and an engineer from the Commission's Finance and Accounts Division and Transportation Division, respectively. Said report contains income statements of Air West's system operations for the calendar years 1969, 1970 and fiscal year ended July 31, 1971, which show operating losses (after subsidy payments) of \$5,437,137, \$6,812,350 and \$15,221,777, respectively.

Said report contains the following estimated results of system and California-intrastate operations for the calendar year 1972. Projected system and intrastate results do not make provision for any income taxes because of an available tax loss carry-forward. Expenses reflect no increase over present levels. Operating revenues assume a growth in traffic in future periods and no diminution because of diversion resulting from fare increases.

TABLE 3
COMMISSION STAFF ESTIMATES OF REVENUES AND EXPENSES

	<u>AIR WEST</u>			
	<u>(+000)</u>			
	<u>Estimate System</u>		<u>Estimate Intrastate</u>	
	<u>Pres. Fare</u>	<u>Prop. Fare</u>	<u>Pres. Fare</u>	<u>Prop. Fare</u>
	<u>1972</u>	<u>1972</u>	<u>1972</u>	<u>1972</u>
<u>Operating Revenue</u>				
Passenger	\$ 83,770	\$ 84,300	\$ 9,784	\$10,313
Cargo-Charter-Incidental	6,900	6,900	802	846
Subsidy	10,700	10,700	2,028	2,028
Total	<u>\$101,370</u>	<u>\$101,900</u>	<u>\$12,614</u>	<u>\$13,187</u>
<u>Operating Expense</u>				
Flying Operations	\$ 31,300	\$ 31,300		
Maintenance	16,000	16,000		
Passenger Service	7,800	7,800		
Aircraft & Traffic Serv.	22,200	22,200		
Promotion & Sales	11,300	11,300		
General & Admin.	8,800	8,800		
Deprec. & Amortization	2,700	2,700		
Total	<u>\$100,100</u>	<u>\$100,100</u>	<u>\$13,203</u>	<u>\$13,203</u>
Operating Profit (Loss)	\$ 1,270	\$ 1,800	\$ <u>(589)</u>	\$ <u>(16)</u>

(Red Figure)

Based on the data in the above table and in the staff report, the staff witnesses reached the following conclusions:

- (a) Present fares if continued, and assuming pre-August 15, 1971 expense levels, will result in a California intrastate operating loss of about \$589,000 in 1972.
- (b) Proposed fares and assuming pre-August 15, 1971 expense levels will result in a California intrastate operating loss of some \$16,000 in 1972.

The staff witnesses recommended that the application be granted.

Protestant's Evidence

The City of Fresno, by its Director of Transportation, presented evidence in opposition to any increase in Air West's fare between Fresno and other California points. The witness testified that it is Fresno's position that existing fares applicable to Fresno inter-city markets are now priced at all the traffic will bear, if not above that level, and that there is no need for further increased air fares to and from Fresno.

The witness pointed out that the three largest markets for air service from and to Fresno are to and from Los Angeles, San Francisco, and San Diego. In these markets United Air Lines competes with Air West and maintains lower fares.^{2/}

The witness contested the statement of Air West's witness that little or no diversion will result from the increased air fares requested herein. The witness pointed out that Air West's traffic has diminished between Fresno and Los Angeles, and that effective October 31, 1971 Air West operated only one flight from LAX to FAT and two daily flights from FAT to LAX. In the same market United operates four daily round-trip flights between LAX and FAT. Similarly, in the Fresno-San Francisco market, Air West operates only one flight on Friday and Saturday service from FAT to SFO, and one daily flight from SFO to FAT. In the same market United operates four roundtrip daily flights between FAT and SFO.

^{2/} The following fares (including federal tax) are in effect or proposed:

<u>City Pair</u>	<u>Existing United "Y" Fare</u>	<u>Existing Air West "S" Fare</u>	<u>Proposed Air West "S" Fare</u>
FAT-SFO	\$16.20	\$21.00	\$22.00
FAT-LAX	19.44	24.00	25.00
FAT-SAN	27.00	35.00	37.00

The witness stated that, in his opinion, the fact that present Air West fares (including tax) exceed United fares by \$4.80 between FAT and SFO and by \$4.56 between FAT and LAX has caused substantial diversion from Air West to United in these markets, and that further increase of \$1.00 in these fares differentials, as proposed herein, will cause further diversion from Air West to United.

The airport manager of the City of Redding testified in opposition to the increase in Redding-San Francisco fares from \$23.15 to \$25.00, an increase of \$1.85. The witness showed that the Redding-San Francisco market for the year ending March 31, 1971 was ranked sixth in terms of on-line origin-destination (O-D) passengers and fifth in terms of non-stop passenger miles in Air West's top twenty California markets. Said market carried 36,504 passengers in the stated year.

The witness testified that it is the opinion of the City of Redding that an increase of \$1.85 in the San Francisco-Redding fare is excessive, and could be self-defeating for Air West. The witness contended that the greater Redding area is an economically depressed area and that commercial air travelers, students, businessmen and local residents cannot afford the sought increase in fares of \$1.85, when considered with the \$2.15 increase placed in effect in January, 1971. The witness stated that decreases in passengers resulted from the January 1971 fare increase in other Air West markets. Although such decrease did not occur in the Redding-San Francisco market, the witness believed that the further increase sought herein would have that effect.

The witness pointed out that the non-stop distance and number of passengers carried is comparable in the Redding-San Francisco and Fresno-Los Angeles markets (36,054 and 35,238 passengers, and 199 miles and 209 miles, respectively); however, Air West proposes a fare of \$25.00 in the Redding-San Francisco

market and \$23.15 in the Fresno-Los Angeles market. The witness stated that the foregoing indicates that Air West has departed from the basic formula approved by CAB in developing the compared fares.

The County of Humboldt, by the manager of the Arcata Airport, opposed the granting of further increases in fares between that airport and other California points. The thrust of the testimony of this witness was with respect to fares and service between Arcata-Eureka and San Francisco and Los Angeles, which points are exempted from Air West's request herein. The witness endeavored to show that following the last fare increase a substantial number of air passengers between Arcata-Eureka and San Francisco left Air West and used the services of Golden Pacific Airlines (GPA). The witness showed that in the months of February through June 1971, GPA had increases in the number of passengers enplaning at Arcata Airport over the same month in 1970 ranging from 22 percent to 72 percent; whereas in the compared periods Air West had decreases in enplaning passengers ranging from 14 to 31 percent. It was the position of the witness that any additional increase in fares will cause further diversion from Air West at Arcata-Eureka.

Testimony was received from representatives of Humboldt State College, The College of the Redwoods, the Humboldt Council of Chambers of Commerce, and the City of Crescent City in opposition to the fare increase. Documents expressing the opposition of the Del Norte Chamber of Commerce, the Del Norte Board of Supervisors, the Arcata Area Chamber of Commerce, and the City of Arcata were received in evidence.

Findings and Conclusion

1. Air West is a regional air carrier, certificated by the CAB to provide local service between points in several states, including California. As a regional air carrier, Air West is eligible for, and has received, subsidy for its operations as provided annually by the Congress of the United States, through the CAB.

2. System operations of Air West (after subsidy payments) have resulted in losses in recent years, as indicated in the preceding opinion.

3. Air West's California intrastate passenger operations for the year ended December 31, 1972 will result in substantial losses under present fares (Tables 2 and 3). Air West is in urgent need of additional revenues from its California routes.

4. Air West was granted an interstate fare increase averaging about six percent by CAB Order dated April 9, 1971. Air West proposes that the same increase be made applicable to its California intrastate fares. Fares based on the CAB formula will increase California revenues of Air West by about 5.4 percent and will produce an annual increase in revenues in 1972 of about \$529,000 (staff) or \$567,000 (applicant).

5. Estimates developed by Air West and by the Commission staff show that California intrastate operations under proposed fares will result in a loss in 1972 (Tables 2 and 3). Said estimates are developed on the basis that no substantial diversion will result from the sought fare increase.

6. Evidence adduced by the City of Fresno and County of Humboldt showed that substantial diversion from Air West to other air carriers occurred following the fare increase placed in effect in January 1, 1971 pursuant to Decision No. 78179 in the markets of Eureka/Arcata-San Francisco, Fresno-San Francisco, and Fresno-Los Angeles. Said fare increases averaged 20 percent.

7. Further diversion from Air West to United will occur in Fresno-San Francisco and Fresno-Los Angeles markets because the fare differential between Air West and United will be increased by \$1.00 as a result of the sought increase. Service of Air West in each of these markets has been reduced to one round trip flight per day or less. Additional diversion may cause further reduction of Air West's

service in the two markets. The fare increase sought herein between Fresno-San Francisco and Fresno-Los Angeles is not justified for the foregoing reasons.

8. No increase is sought herein in Arcata/Eureka-San Francisco nor the Arcata/Eureka-Los Angeles fares. Current service by Air West between Arcata/Eureka and California points on its system other than San Francisco or Los Angeles is provided through San Francisco or Los Angeles principally by means of connecting flights. No substantial diversion will occur at Arcata/Eureka as a result of this application, as no increase is sought in the principal markets with direct service by Air West, and the balance of said markets are served indirectly.

9. It has not been shown that substantial diversion will occur in other intra-California markets of Air West as a result of the fare increases sought herein.

10. The proposed fare for Air West's segment between San Francisco and Redding exceeds the proposed fare between Los Angeles and Fresno, whereas the distance between Redding and San Francisco is less than between Fresno and Los Angeles. Fares between Redding and San Francisco are "standard fares" based on formulae established by the CAB, whereas fares between Fresno and Los Angeles are on a lower basis than the "standard fares" to meet competition of other airlines. The foregoing disparity in fares does not warrant a holddown in the fare between Redding and San Francisco.

11. Except as indicated in finding 7, the fare increases proposed in the application are justified.

The Commission concludes that the application should be granted to the extent provided by the above findings.

The intrastate fares authorized herein will not return applicant's intrastate operating costs and the resulting revenue increases are necessary if applicant's operations for the public

are to continue. Therefore, the increased fares are consistent with the purposes of the Federal Government's economic stabilization program.

ORDER

IT IS ORDERED that:

1. Hughes Air Corp., a corporation, doing business as Air West, is authorized to establish the increased air fares as requested in Application No. 52754, except that no increase shall be made in fares between San Francisco and Fresno, and Los Angeles and Fresno.

2. Tariff publications authorized to be made as a result of the order herein shall be filed not earlier than the effective date of this order, and may be made effective not earlier than five days after the effective date of this order on not less than five days' notice to the Commission and the public.

3. The authority granted herein shall expire unless exercised within ninety days after the effective date of this order.

The effective date of this order shall be ten days after the date hereof.

Dated at San Francisco, California, this 9th day of DECEMBER, 1971.

[Signature]
Chairman

[Signature]

[Signature]

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Commissioners