

Decision No. 84841

ORIGINAL

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of
DREISBACH COLD STORAGE CO., GROWERS'
REFRIGERATION COMPANY, HASLETT COMPANY,
MERCHANTS ICE AND COLD STORAGE COMPANY,
SCHAEFER'S MEATS, UNION ICE & STORAGE
COMPANY, UNITED COLD STORAGE and UNITED
STATES COLD STORAGE OF CALIFORNIA, for
an Increase in Rates.

Application No. 55058
(Filed July 23, 1974)

Vaughan, Paul & Lyons, by John G. Lyons and
Dale N. Rettig, Attorneys at Law, and
Jack L. Dawson, for applicants.
William D. Mayer, for Del Monte Corporation,
Interested party.
Russell D. Corning, for the Commission staff.

FINAL OPINION

Applicants are public utility warehousemen operating warehouse facilities in the San Francisco Bay area for the storage of commodities requiring refrigeration. The rates charged by these applicants for freezing, storage, handling, and other services incidental thereto, and the rules and regulations governing the application of such rates, are contained in California Warehouse Tariff Bureau Cold Storage Warehouse Tariff No. 18, Cal. P.U.C. No. 227 of Jack L. Dawson, Agent, and in Growers' Refrigeration Company Cold Storage Warehouse Tariff No. 5, Cal. P.U.C. No. 5.

Decision No. 83485 dated September 24, 1974 authorized increases in rates and charges set forth in the margin pending

consideration of applicants' request for a five percent increase in all other rates and charges set forth in California Warehouse Tariff Bureau Cold Storage Warehouse Tariff No. 18.^{1/}

The original public hearing of Application No. 55058 was held before Examiner Mallory at San Francisco on January 17, 1975, and the matter was submitted. Pursuant to the Commission's order in Decision No. 84140 dated March 4, 1975, the proceeding was reopened and further hearing was held before Examiner O'Leary at San Francisco on May 15, 1975 at which time the matter was resubmitted.

1/ Applicants' interim authority is as follows:

Rate Changes in
CWTB Cold Storage Warehouse Tariff No. 18

- A. Establish the following new rule re Preparation of Book Inventories:

For the service of preparing a book inventory of stock on hand, the charge will be computed on the basis of 10¢ per lot inventory line, minimum charge \$5.00 per book inventory.

- B. Amend Rule No. 130 - Deliveries ex Warehouse - to read as follows:

Lot Deliveries

Each lot delivery will be subject to a charge of \$1.15 in addition to the handling rates provided in this Tariff.

Also, to amend rate pages 18 through 34 of CWTB Cold Storage Warehouse Tariff No. 18 by revising the lot delivery charge wording to read:

An additional charge of \$1.15 per delivery per lot will be made on all lot deliveries.

- C. Amend Rule No. 145 - Minimum Charges - by adding the following minimum monthly billing charge:

The minimum monthly billing charge to one account will be \$20.00.

- D. Amend Rules Nos. 185 and 190 by increasing the straight-time man-hour rate from \$7.82 to \$11.00; and the overtime man-hour rate from \$11.73 to \$15.00.

Evidence at Original Hearing

Applicants' tariff agent testified that approximately 1,800 notices were sent to applicants' storers advising them of the relief sought and the date and place of hearing. No one appeared in opposition to the relief sought.

Applicants' witness also testified with respect to the data set forth in exhibits attached to the application. Exhibit D to the application sets forth operating statements for each applicant for the year ended December 31, 1973 (year ended October 31, 1973 for Schaefer's Meats). The data from that period are from applicants' books and records, adjusted as explained in Exhibit E to the application. The witness made adjustments to substitute landlord expenses for rents in the instances that warehouse facilities are leased from an affiliated company; to make provision for owner-manager salaries when no provision is made on applicants' books; to eliminate interest as an operating expense; to exclude donations; to provide for general office and administrative expense when provided by a parent company; and to reduce downward the charge to operating expense for an extraordinarily large loss and damage claim.

The witness testified that the revenue data for 1973 were adjusted to give effect for a full year to the rate increase authorized by Decision No. 81756 dated August 21, 1973 in Application No. 53508 which became effective September 21, 1973, and for the interim and final rate increases authorized herein. Expense data, adjusted as indicated above, were further adjusted to give effect to known increases in labor and related payroll costs, taxes, and power costs through December 31, 1974. No adjustment of the historical data was made for the wage increase for engineers effective March 1, 1975 nor for plant operating labor effective June 1, 1975.

The historical and adjusted revenue and expense data are set forth individually and also in composite form for a group of five test warehousemen. The five test warehousemen used in applicants' study earn approximately 95.5 percent of the total revenues and operate approximately 94.0 percent of the warehouse space of all applicants as a group. The following table sets forth the composite operating results for a test year under the interim and full relief sought in the application for the five test warehousemen and for all applicants.^{2/}

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- ^{2/} The five test warehousemen are Dreisbach Cold Storage Co. (Dreisbach), Oakland; Growers' Refrigeration Company (Growers), San Francisco; Merchants Ice and Cold Storage Company (Merchants), San Francisco; United Cold Storage (United), South San Francisco; and United States Cold Storage of California (U.S.), San Francisco and Oakland.

TABLE 1

**Applicants' Estimated Results of Operation
For 1974 Test Year Under Interim Rates
And Under Final Rates**

<u>Under Proposed Rates and Revised Expenses</u>	<u>Five Test Warehousemen</u>	<u>Composite</u>	<u>All Warehousemen</u>
Revenue Proposed	\$4,224,606		\$4,422,351
Revised Expenses	3,485,051		3,652,615
Profit or (Loss) B.T.	739,555		769,736
Taxes	357,097		380,586
Revised Expenses A.T.	3,842,148		4,033,201
Profit or (Loss) A.T.	382,458		389,150
Revised Rate Base	4,893,759		5,289,608
Rate of Return A.T.	7.8%		7.4%
Operating Ratio A.T.	90.9%		91.2%
 <u>Under Interim Accessorial Rate Adjustment and Revised Expenses</u>			
Revenue Proposed	4,040,858		4,229,552
Revised Expenses	3,485,051		3,652,615
Profit or (Loss) B.T.	555,807		576,937
Taxes	260,299		279,766
Revised Expenses A.T.	3,745,350		3,932,381
Profit or (Loss) A.T.	295,508		297,171
Revised Rate Base	4,877,626		5,272,804
Rate of Return A.T.	6.1%		5.6%
Operating Ratio A.T.	92.7%		93%

B.T. - Before Taxes
A.T. - After Taxes

Income taxes in the above table were calculated by applicants' witness at the state and federal rates applicable, without adjustment for any deductions from net income authorized under tax statutes, such as deductions for interest paid. It consistently has been the Commission's policy to make provision for income taxes in test year operations on a basis that is as close as possible to the actual taxes that will be paid by the utilities. If consideration

is given to permissible deductions from net utility warehouse income in the same relative proportion to total net income that appears on the 1973 annual reports of the five test warehousemen, the following after-tax operating results would appear:

TABLE 2

Estimated Test Year Operating Results of
Five Test Warehousemen from Table 1,
Revised to Show Effect of Permissible
Deductions from Net Income
For Tax Purposes

<u>Operating Results Under Full Increase Sought</u>	<u>Five Test Warehousemen</u>
Net Income Before Taxes	\$ 739,555
Allowable Deductions from Net Income for Tax Purposes	62,198
Net Income for Tax Purposes	677,357
Income Taxes	342,291
Net Income After Taxes	397,264
Rate Base	4,893,759
Rate of Return	8.12%
Operating Ratio After Taxes	90.6%

The witness for applicants presented a compilation in Exhibit 3 to show that applicants will not achieve the rate of return or operating ratio set forth above because the full increase sought in the application will be in effect for only part of the 1975 test year, and because the estimated expenses for the test year fail to include the contractual increase for warehouse labor which will become effective June 1, 1975.

The witness testified that the rate of return sought by applicants will be reasonable in view of the current condition of the warehouse properties operated by applicants and the estimated costs of replacing the properties. According to the witness, the operating properties of the five test warehousemen are depreciated to the following extent:

Dreisbach	36.0%
Growers	28.4
Merchants	70.0
United	61.6
U.S.	<u>39.0</u>
Weighted Average	47.0%

Exhibit 4 shows the effect of expansion or replacement of applicants' facilities at present building costs. The witness assumed that all facilities will earn a profit of 5.4 cents per cubic foot, in line with the profit factor estimated to result from this application. If total warehouse space operated by applicants were increased by 20 percent the average net cost of the total property and equipment would be increased from 60.79 cents per cubic foot to 77.3 cents per cubic foot, and the estimated rate of return on total investment would drop from 7.8 percent to 6.3 percent. The witness testified that applicants have been operating at or near full capacity for the past two years, so that any further demands for public utility cold storage must be met by expansion.

Evidence on Further Hearing

In reopening this proceeding for further hearing the Commission, in Decision No. 84137, stated:

"It appearing...that operating ratios and rates of return for warehousemen...reflect a substantial diversity in profitability, and it further appearing that by reason of such diversity of profitability, it cannot be concluded that an

increase in charges is essential to ensure just and reasonable rates for the most efficient warehouse operations; and it further appearing that additional evidence is necessary to show special or unique circumstances applying to the less efficient warehousemen which would justify the Commission in treating them in a manner different from that accorded the more efficient warehousemen,

"IT IS HEREBY ORDERED that said proceeding is reopened for the taking of further evidence..."

In response to the Commission's order reopening this proceeding the tariff agent for the California Warehouse Tariff Bureau presented extensive testimony and a series of comparative statements (Exhibits 5 through 14) on behalf of applicants. He first emphasized that it was absolutely essential for applicants to maintain their cold storage warehouse operations at the peak of efficiency at all times in order to survive in the keen competitive conditions existing in the San Francisco Bay area. Secondly, the tariff agent stated that from his study and analysis he found no correlation between the efficiency of applicants' cold storage operations and their so-called diversity of profitability. He further explained that his studies clearly indicate that variations in warehouse operating revenues and expenses are brought about by the type of cold storage business handled and the kind of service required by the particular storage accounts. A summary of such variable factors follows:

1. Factors causing variations in the revenue positions of the various warehousemen.

A. Type of storage accounts.

- (1) Quick freezing.
- (2) Frozen.
- (3) Cooler storage.
- (4) In-transit storage.

- B. Character of storage lots.
 - (1) Distribution on a retail level.
 - (2) Distribution on a wholesale level.
 - (3) Large quantities from producers.
 - (4) Small quantities from producers.
 - (5) Consolidation into large lots for shipment outbound.
 - (6) Brokers or wholesalers.
- C. Activity of goods in storage.
 - (1) Withdrawals in large or small lots.
 - (2) Racking of goods in storage.
 - (3) Density of goods in storage.
 - (4) Rate of turnover of goods in storage.
 - (5) Favorable or unfavorable warehouse occupancy because of fluctuations in production.
- D. Type of warehouse - whether multistory or single story can influence the cubic foot revenues.
- E. Lot size of commodities offered for storage.
- 2. Factors causing variations in cubic foot storage costs.
 - A. Amount of labor and handling equipment required.
 - B. Amount of power necessary for the service required by storer.
 - C. Fluctuations in power demands creating electric demand charges which became minimum for months of less power usage.
 - D. Variations in building and equipment costs.
 - E. Variations in number and type of accounts served.
 - F. Loss and gain of accounts.
 - G. Number of outbound lots per each inbound lot received.
 - H. Number of inbound lots required to make up a consolidated lot for shipment as a large lot.

- I. Whether installation of racks required for small lot storage or for commodities requiring racks in order to high pile.
- J. Density and lot size of commodities offered for storage.

The tariff agent's comparative statements set forth the results of his study and analysis of the aforementioned economic factors as they are reflected in the 1973 cold storage operations of five test warehousemen.

In Exhibit 5 operating ratios and rates of return based upon assessor's value plus working capital are set forth as follows:

TABLE 3

<u>Test Warehouse</u>	<u>Percent of Space</u>	<u>Percent of Revenue</u>	<u>Operating* Ratio</u>	<u>Rate of Return</u>
U.S.	53.7	38.6	90.8	3.7
Merchants	16.1	13.7	91.3	3.6
United	4.7	7.2	90.0	5.7
Dreisbach	22.6	33.9	91.7	3.8
Growers	2.9	6.6	88.0	#

* Based on Assessor's Value Plus Working Capital.

Operates in Rented Facilities

Exhibit 6 analyzes expenses and proposed revenues per cubic foot of storage space operated. Pertinent portions of the exhibit are:

TABLE 4

Breakdown of Test Warehouses
According to Expenses and Revenues
Per Cubic Foot

Test Warehouse	Expenses Per Cu.Ft. (In Cents)	Proposed Revenue Per Cu.Ft.	Proposed Operating Ratio %	Rate of Return %		% Net Property & Equipment Depreciated
				(1)	(2)	
U.S.	37.9	41.7	90.8	3.9	6.1	39.0
Merchants	45.4	49.7	91.3	2.5	7.5	70.0
United	79.7	88.5	90.0	5.4	12.7	61.6
Dreisbach	80.0	87.2	91.7	5.8	8.65	36.0
Growers	114.9	130.5	88.0	15.1*	19.8*	28.4
Total	52.8	58.1	90.9	4.4	7.8	47

(1) On Undepreciated Rate Base

(2) On Depreciated Rate Base

* Rented Property not included
in Rate Base

In Exhibit 7 the tariff agent presents an analysis of the expenses incurred by the warehousemen for labor, power, depreciation, and property taxes. He explained that applicants' labor and power costs represent the only area for potential increases in operating efficiency. While labor and power costs are extremely sensitive to the influences of current economic inflationary trends, the warehousemen state that they have devoted substantial effort to maintain such costs at levels consistent with efficient operations. A summary of the tariff agent's cost analysis follows:

TABLE 5

Analysis of Labor and Power Costs Incurred
By the Test Warehousemen as of 1973

<u>Test Warehousemen</u>	<u>% of Proposed Revenue</u>	<u>% of Total Space</u>	<u>Labor Costs Per Cu.Ft. (In Cents)</u>	<u>Power Costs Per Cu.Ft. (In Cents)</u>	<u>Proposed Operating Ratio %</u>
U.S.	38.6	53.7	17.4	2.9	90.8
Merchants	13.7	16.1	14.0	3.6	91.3
United	7.2	4.7	36.8	8.1	90.0
Dreisbach	33.9	22.6	37.2	5.6	91.7
Growers	6.6	2.9	62.1	8.3	88.0
Total	100	100	24.9	4.0	-
% of Total Expenses Before Taxes	-	-	47.1	7.6	-

Labor and power costs constitute approximately 58 percent of the test warehousemen's total expenses. Any significant changes in these two major areas, due either to current inflationary trends or a deterioration in operating efficiency, would have a dramatic impact upon applicants' results of operations. No such correlation may be drawn, however, between the various differences in the test warehousemen's labor and power costs and their respective operating ratios.

The commodities tendered applicants for cold storage and handling services in the San Francisco Bay area consist primarily of prepared foodstuffs, fruits and vegetables, juices, juice concentrates, meat, fish, and poultry. The storage accounts may be generally classified as either distribution business (retail, wholesale, brokerage) or production business (food processors, packers, and agriculture). The storage and handling characteristics of such commodities as described in Exhibit 8 reflect the interplay of basic economic principles of marketing and distribution. The comparative data clearly show that the storage and handling characteristics of commodities have a considerable bearing upon the level of each warehouseman's operating revenues and expenses. However, such economic variables are not necessarily determinative per se of the diversity or degree of profitability experienced by each warehouseman as measured by its respective operating ratio.

Assuming a reasonable compensatory rate structure, applicants argue that it is the volume, velocity (storage turnover), and value of service which, in the final analysis, dictate the warehousemen's results of operations. Cyclical fluctuations in these basic economic elements are direct reflections of the general vitality of the economy as measured within the economic system of marketing and distribution of products. In Exhibit 12 the historical operating ratios authorized in prior rate proceedings are presented:

TABLE 6

Historical Operating Ratios Previously Authorized
The Test Warehousemen in Prior Rate Proceedings

<u>Warehousemen</u>	<u>Rate Proceedings-Applications Nos.</u>				<u>Average Operating Ratios</u>
	<u>55058 (1974) (1)</u>	<u>53508 (1972)</u>	<u>52095 (1970)</u>	<u>49750 (1967)</u>	
U.S.	90.8%	88.9%	89.9%	102.8%	93.1%
Merchants	91.3	100.0	99.9	94.8	96.5
United	90.0	91.1	94.4	91.3	91.7
Dreisbach	91.7	93.7	92.4	93.0	92.7
Growers	88.0	89.6	90.2	*	89.3
Total	90.9	92.1	92.3	98.0	93.3

* Not a test warehouse.

(1) Proposed operating ratios.

It is apparent from the record in this proceeding that there is no single factor which explains the variability of operating ratios and rates of return among the test warehouses. Variations might be due, among other factors, to: (1) failure of the relative rates for warehouse services to correspond to the relative cost of services--thus, for example, if storage charges are relatively too low and handling charges relatively too high, warehouses which perform a disproportionate amount of storage services will be less profitable than others; (2) differences in management efficiency; (3) unpredictable shifts in market conditions for storage for different commodities; and (4) the age of the warehouse. An older warehouse, which has been highly depreciated, may have a market value considerably higher than its book. Its rate of return on book value might then exceed the average for newer warehouses.

The appropriate way to reflect these differences is through the competitive process. Warehousing, today, is an inherently competitive industry, not a natural monopoly. For this reason the Commission has urged the legislature to end the public utility regulation of warehouses.

Absent new legislation, this Commission continues to have the duty to regulate warehouse rates. The record in this proceeding indicates that applicants are in need of rate relief and that the rates requested will allow applicant warehousemen an opportunity to experience operating results which have been found justified by this Commission in the past. The rate relief requested will be authorized.

However, the basic concern which led the Commission to reopen this proceeding for the taking of further evidence dictates that henceforth a new regulatory policy should be adopted in the regulation of warehouse rates. Principally, the Commission intends to encourage the availability of individual tariff filings by the various warehousemen and to protect the potentiality of individual action both within and among the various tariff bureaus. Accordingly, the Commission will henceforth set rates on an individual basis, granting permission to increase rates only to those warehouses which are both efficiently operated and unable to earn a reasonable return at existing rates. Group filings of a single rate for warehousing services where no individual justification has been made by the members of the group will be subject to dismissal.

The Commission is aware that the difficulty with this proposal is that individual warehouses may be unwilling to put rate increases into effect for fear of competition from other warehouses not allowed to increase rates. However, in that case the low-return warehouses could propose a rate schedule which would reflect the special aspects of their business (other than any inferior efficiency

of their operations) which are responsible for their relatively unsatisfactory rate of return. Thus, for example, the relative rates for storage and handling could be adjusted if it developed that most of the low-return warehouses were specialized in one or the other activity. Similarly, any enduring cost advantage of handling a particular commodity could be reflected in a new rate structure. After making these adjustments, the rate structure should provide a comparable rate of return to warehouses of comparable efficiency, with two exceptions: (a) any inaccuracies in the depreciation formula used for warehouses might be reflected in a relationship between the age of a warehouse and its profitability; and (b) unpredictable market shift would still affect profitability. These conditions, however, are likely to hold true under any system of regulation, and even in some degree under a competitive regime.

This alternative to the present regulatory scheme is not fully satisfactory as it will not produce as fair a rate schedule as would competitive pricing. We conclude, however, that this approach is more compatible with our regulatory responsibilities. So long as warehouses are regulated as public utilities, the Commission must aggressively pursue a policy that will not grant rates which result in exceptionally high profits unrelated to efficiency.

Findings

1. Prior to the interim relief granted herein applicants' rates were last considered by the Commission in Application No. 53508. Decision No. 81756 dated August 21, 1973 in that proceeding, it was estimated that, under the rates authorized therein, applicants' composite operations would result in an operating ratio (after taxes) of 92.6 percent and a rate of return of 5.6 percent.

2. Interim Decision No. 83485 dated September 24, 1974, in this proceeding authorized applicants to increase certain accessorial charges, pending hearing on the full amount of the relief sought. The interim increase was estimated to result in additional revenue of \$91,502.00, an operating ratio (after taxes) of 93.0 percent and a rate of return of approximately 5.6 percent.

3. Under the full increase sought herein applicants estimate that they will realize an additional revenue of \$192,799.00, a composite operating ratio (after taxes) of 91.2 percent and a rate of return of 7.4 percent for all applicants, and that the five test warehousemen selected by applicants will achieve an operating ratio (after taxes) of 90.9 percent and a rate of return of 7.8 percent. (Table 1.)

4. The estimates of applicants in Table 1 should be adjusted to reflect, as nearly as possible, income taxes actually paid. The adjusted results of operations for the five test warehousemen set forth in Table 2 reflect interest and similar allowable income deductions for tax purposes in proportion to the net public utility warehouse income of applicants. The operating results in Table 2 are reasonable for the purposes of this proceeding.

5. Storsers of property in applicants' warehouses were notified of the filing of this application and the time and place of hearing. No one appeared in opposition to the sought relief.

6. The increases in rates sought in Application No. 55058 are justified.

7. There is no apparent single factor which explains the variability of operating ratios and rates of return experienced by the test warehousemen. The appropriate method to reflect these differences is through the competitive process.

8. To promote the establishment of competitive ratemaking, rates should be set on an individual basis granting authority to increase rates only to those warehousemen which are both efficiently operated and unable to earn a reasonable return at existing rates. Henceforth, rate increase applications involving warehousemen will be considered on an individual basis.

Conclusions

1. To the extent not granted in the interim order herein, the relief sought should be authorized.

2. Applicants should be authorized to establish the authorized increases on five days' notice.

FINAL ORDER

IT IS ORDERED that:

1. Applicants are authorized to establish the increased rates proposed in Parts 1 and 2 of Appendix A to Application No. 55058. 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 less than five days after the effective date hereof on not less than five days' notice to the Commission and to the public.

2. The authority herein granted is subject to the express condition that applicants will never urge before this Commission in any proceeding under Section 734 of the Public Utilities Code, or in any other proceeding, that the opinion and order herein constitute a finding of fact of the reasonableness of any particular rate or change, and that the filing of rates and charges pursuant to the authority herein granted will be construed as a consent to this condition.


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

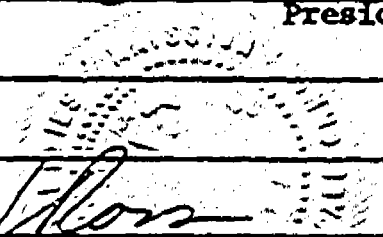
The effective date of this order is the date hereof.

Dated at San Francisco, California, this 26th day of AUGUST, 1975.

I dissent as to future
suggested rate regulation
William Ayers Jr.

I dissent
Vernon L. Sturgeon



President


Commissioners