

Decision 98-12-016 December 3, 1998

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the Matter of the Application of CATALINA CHANNEL EXPRESS, INC., a California corporation, for Authority to Establish a Zone of Rate Freedom for its Vessel Common Carrier Service Between Authorized Southern California Mainland Points and Authorized Points on Santa Catalina Island.

Application 98-04-051
(Filed April 21, 1998)

ORIGINAL

OPINION

Summary

We approve the application of Catalina Channel Express, Inc. (applicant) for authority to establish a zone of rate freedom (ZORF) of ten percent above and below its existing fare levels for passenger vessel services between points on the California mainland, on the one hand, and points on Santa Catalina Island (Catalina), on the other hand. This decision extends to a passenger vessel carrier a ratesetting concept we have utilized with respect to passenger stage carriers under Public Utilities (PU) Code § 454.2 for many years, and is consistent with a policy we recently announced favoring greater competition among the vessel carriers serving cross-channel routes.

This proceeding was categorized as a ratesetting matter by Resolution ALJ 176-2992 on May 7, 1998, and a preliminary determination was made that no hearings was necessary. The application is unopposed.

Background

The applicant is a common carrier by vessel which has authority to provide scheduled and non-scheduled cross-channel services between various California mainland points and points on Catalina. Commission-approved tariffs are in effect on these routes, the product of conventional cost-of-service proceedings conducted pursuant to PU Code § 454. Such proceedings require express Commission approval for fare increases and decreases (except for limited promotions, discounts, or special fares) before they become effective, and frequently require additional processing if they are protested by competitors or other persons. Even under the best of circumstances, protest periods, notice requirements, and "sunshine" requirements often cause a routine request for a fare change to require 120 days or more before a Commission order may become effective.

As a long history of proceedings before this Commission attests, ridership on the cross-channel Catalina vessel services is highly seasonal by reason of its recreational nature. Recently, in response to a growing interest in establishing new routes and types of service to Catalina, the Commission eased historical barriers to entry by new operators and opened the cross-channel service to greater competition. (Decision (D.) 97-11-027; D. 97-06-103.) The present application is made with express recognition of that fact, and the applicant contends that its proposal is consistent with the more competitive environment in which it now operates.

The applicant requests authority to establish a ZORF for its cross-channel passenger fares, allowing the applicant to alter its fares ten percent above or below its presently established fares on ten days' notice to the Commission and the public, and without prior Commission approval for such fare increases and reductions. This device has been utilized by the Commission to give greater

flexibility to passenger stage operators where competition exists since ZORFs were first authorized by PU Code § 454.2 in 1984, and has been embraced by airport shuttle companies as an effective device for adapting quickly to changes in their competitive circumstances.

Section 454.2 states:

"Notwithstanding Section 454, the Commission may, upon application, establish a 'zone of rate freedom' for any passenger stage transportation service which the Commission finds is operating in competition with another substantially similar passenger stage transportation service or competitive passenger transportation service from any other means of transportation, if the Commission finds that these competitive transportation services will result in reasonable rates and charges when considered along with the authorized zone of rate freedom. An adjustment in rates or charges within a zone of rate freedom established by the Commission is hereby deemed just and reasonable. The Commission may, upon protest or on its own motion, suspend any adjustment in rates or charges under this section and institute proceedings pursuant to Section 491."

The Commission has not previously extended the application of this concept to modes other than passenger stage carriers, and this proceeding is consequently one of first impression.

Discussion

Applicant argues that we should extend the ZORF concept to its cross-channel vessel services because there is competition on these routes, and because it needs to respond to seasonal fluctuations in traffic to cover its costs in times of light ridership. It is thus implied that the same factors make it appropriate to employ the ZORF concept here as for passenger stage operators who operate in a competitive environment.

Applicant asserts that we have sufficient discretion in selecting methods for regulating common carrier rates to allow us to extend the ZORF concept to

vessel carriers in the absence of express authorization by statute. We agree. Authority in the California Constitution and PU Code, as well as the authority cited by the applicant in In Re Regulation of General Freight Transportation by Truck, 35 CPUC 2d 307, 346 (1990) and Investigation of Reduced Rates for Transportation of Bulk Cement, 50 CPUC 622, 632-33 (1951), persuade us that we are free to "think outside the box" of traditional cost-of-service regulation to adopt more flexible and responsive fare setting methods where competition exists, if we find that any potential fare falls within a range of reasonableness.

Article XII, Section 4 of the California Constitution provides:

"The Commission may fix rates and establish rules for the transportation of passengers and property by transportation companies,...A transportation company may not raise a rate or incidental charge except after a showing to and a decision by the Commission that the increase is justified,..."

PU Code § 701 provides, in part, that the Commission,

"may do all things, whether specifically designated in [the Public Utilities Act] or in addition thereto, which are necessary and convenient in the exercise of [its] power and jurisdiction."

Taken together, California Constitution Article XII, Section 4 and PU Code § 701 grant the Commission broad discretion to fashion rules relating to transportation rates in the State which are unorthodox by comparison to traditional cost-of-service regulation.

The Commission has interpreted its jurisdiction to be consistent with the exercise of such discretion in other transportation matters. In In Re Regulation of General Freight Transportation by Truck, *supra*, the Commission held:

¹ Section 4, further provides that, "this decision shall not be subject to judicial review except as to whether confiscation of property will result."

"In short, we conclude that (1) the Commission is not restricted to a cost-of-service form of regulation, and (2) there is ample authority to establish an appropriate and effective form of flexible rate regulation."

In so holding, the Commission relied on and cited with Investigation of Reduced Rates for Transportation of Bulk Cement, *supra*, which held:

"It is well established that rates may be unreasonable because they are too low as well as because they are too high. There is a zone of reasonableness within which common carriers so long as statutory restrictions are not transgressed, may and should exercise discretion in establishing their rates. The upper limits of that zone are represented by the level at which rates would be above the value of the service, or be excessive. The lower limits are fixed, generally, by the point at which the rates would fail to contribute revenue above the out-of-pocket cost of performing the service, would cast an undue burden on other traffic (of Applicant), or would be harmful to the public interest. Rates at the upper limits of the zone may be termed maximum reasonable rates; those at the lower limits of the zone may be termed minimum reasonable rates."²

Applicant's present fares were set by D. 96-04-048 in Application (A.) 95-12-003. Our decision to approve those fares was based upon a finding that they are just and reasonable. The basic adult round trip fare is \$34.00 for the crossing in applicant's 20 knot and above vessel, so a ten percent variation above and below this level will yield maximum and minimum fares of \$37.40 and \$30.60, respectively. We regard this as a reasonable range for the type of service and length of the route involved. Competition, rather than the applicant's desire to cover its existing cost of operation at all times, will effectively determine where it will fix its fare within this range.

² The Commission's broad discretion in setting rates has also been approved by the California Supreme Court in California Trucking Association v. Public Utilities Commission, (1977) 19 Cal. 3d 2240, 246 & n.10, p. 247.

We recognize the risk that the applicant could use its flexibility to reduce fares to discourage new competitors from entering this market. However, we do not believe that a short-term reduction of ten percent would be sufficient to thwart a new entrant, and applicant's financial condition would not permit it to maintain such a reduction in the long run. The applicant's financial statements reveal that its current pretax profit margin is under five percent on revenues of about \$14.5 million, well below the capital requirement for vessel replacement and other capital costs. It would be economically suicidal for the applicant to maintain its rates at a level below the current baseline for long, given the existence of established competitors who would undoubtedly exploit any degradation of its services resulting from deferral of capital expenditures.

The applicant asks us to authorize it to set rates within the established zone for a 12-month period without additional Commission approval, and to allow all rates to become effective on 10 days' notice to the Commission and the public. The latter condition is a natural adjunct to the authority we are granting, and we will approve it. However, we perceive no purpose in limiting the duration to 12 months, nor are we willing to grant applicant's request for authority without further Commission approval to adjust the upper limit of the zone of reasonableness for each succeeding 12-month period to allow for further rate increases of up to ten percent from the established rates, and to maintain a zone of rate freedom of ten percent above and below whatever rates may be in effect in tariff form at any particular time. This would effectively allow the applicant to raise the baseline rates by as much as ten percent annually without Commission oversight. The applicant has made no showing whatsoever that the resultant rates would be fair and reasonable, and we cannot approve such a mechanism. If the applicant desires to raise the baseline in the future to accommodate

inflationary or other cost increases, it will have to make the necessary showing under PU Code § 452.

This application requests a ZORF for one specific vessel common carrier, which we will approve with the exceptions noted. The rationale for approving a ZORF may well extend to all vessel common carriers. We will require service of this order on all such carriers and invite any party to file an application for a ZORF.

Findings of Fact

1. Applicant is a common carrier by vessel, and is authorized to transport passengers and their baggage in scheduled service between Berth 95-96 in Los Angeles Harbor (San Pedro) and Redondo Beach, on the one hand, and certain points on Santa Catalina Island, on the other hand, and between Long Beach and Dana Point, on the one hand, and Avalon on Santa Catalina Island, on the other hand. Applicant is also authorized to transport passengers and their baggage in non-scheduled service between San Pedro and Long Beach, on the one hand, and all points on Santa Catalina Island, on the other hand. Applicant currently has Commission-approved tariffs for the cross-channel services it operates.

2. There is competition for the applicant's services by substantially similar vessel carriers on all cross-channel routes that the applicant serves.

3. Fares of up to ten percent above or below applicant's currently authorized fares would be fair and reasonable for the routes and services it operates.

4. Since 1984 the Commission has approved the establishment of ZORFs to afford passenger stage operators flexibility to change their rates where competition exists.

5. Allowing the applicant to adjust its fares up to ten percent above and below its currently authorized fares on ten days' notice to the Commission and

the public would enable the applicant to respond quickly to changing circumstances in the cross-channel market it serves, and would result in reasonable rates and charges in light of the existence of competitive transportation services.

Conclusions of Law

1. The Commission may lawfully exercise discretion to allow a vessel common carrier to establish a ZORF under Article XII, Section 4 of the California Constitution and Section 701 of the Public Utilities Code.

2. The Commission's policy with respect to cross-channel vessel services between California mainland points and Santa Catalina Island favors more open competition than has heretofore existed on these routes, and we have exercised this policy in our recent decisions concerning the establishment of new services on these routes.

3. Authorization of ZORFs is consistent with reliance upon competition to regulate the transportation marketplace, where competition exists between substantially similar established carriers.

4. We should grant the applicant's request for authority to establish a ZORF allowing it to raise or lower its rates up to ten percent above or below current levels, but not to allow applicant to adjust the upper level of the ZORF every 12 months .

O R D E R

IT IS ORDERED that:

1. Catalina Channel Express, Inc. (Applicant) may set rates within a zone of rate freedom (ZORF) of ten percent below and ten percent above the approved rates which are on file with this Commission as of this date, or which are

hereafter filed for the first time, for the vessel common carrier services it is authorized to operate between Long Beach, San Pedro, Redondo Beach, and Dana Point, on the one hand, and Avalon and other points on Santa Catalina Island, on the other hand. Applicant shall file its ZORF tariff on not less than 10 days' notice to the Commission and the public.

2. Applicant's authority to set its rates under the ZORF tariff shall expire unless exercised within 60 days after the effective date of this order.

3. Applicant may make rate changes within the ZORF by filing amended tariffs on not less than ten days' notice to the Commission and the public. The tariff shall include for each route the authorized maximum and minimum rates and the rate to be charged. In no event shall the applicant change the currently effective rates that will serve as the baseline for its ZORF without applying for an order from this Commission for authority to do so.

4. Notice to the public of rate changes made pursuant to this order shall be conspicuously posted in applicant's terminals and in the vessels used to furnish the affected services, and shall remain posted for at least 30 days unless subsequently changed within that period.

5. The Executive Director is directed to serve a copy of this order on all vessel common carriers.

A.98-04-051 ALJ/VDR/avs ‡

6. Application 98-04-051 is closed.

This order is effective today.

Dated December 3, 1998, at San Francisco, California.

RICHARD A. BILAS
President

P. GREGORY CONLON

JESSIE J. KNIGHT, JR.

HENRY M. DUQUE

JOSIAH L. NEEPER

Commissioners