

BEFORE THE
WASHINGTON METROPOLITAN AREA TRANSIT COMMISSION
WASHINGTON, D.C.

ORDER NO. 702

IN THE MATTER OF:

Served April 14, 1967

Application of Washington,)
Virginia and Maryland Coach)
Company, Inc., for Increase)
of Fares.)

Application No. 410

Docket No. 135

APPEARANCES:

MANUEL J. DAVIS, Attorney for Washington, Virginia
and Maryland Coach Company, Inc., Applicant.

JAMES M. HENDERSON, appearing for the Fairfax County
Federation of Citizens Associations, Intervenor.

JAY E. SHANKLIN, pro se, Protestant.

FREDERICK P. HITZ, appearing for the City of Fairfax,
Protestant.

JERRY EMRICH, Attorney for the Board of Supervisors,
Arlington County, Intervenor.

RUSSELL W. CUNNINGHAM, General Counsel, Washington
Metropolitan Area Transit Commission.

BEFORE EDWARD D. STORM, CHAIRMAN; H. LESTER HOOKER,
VICE-CHAIRMAN; GEORGE A. AVERY, COMMISSIONER.

On December 29, 1966, Washington, Virginia and Maryland Coach Company, Inc. ("W. V. & M."), filed an application with the Washington Metropolitan Area Transit Commission ("Commission") seeking authority to increase certain of its fares for the transportation of passengers interstate between points in Northern Virginia, on the one hand, and points within the District of Columbia, on the other.

W. V. & M.'s application was accompanied by appropriate prepared testimony and exhibits as well as the following tariffs setting forth new and increased fares.

- (A) WMATC Tariff No. 29 (Tariff of W. V. & M.)
Generally, this tariff seeks to increase interstate adult fares by five cents (5¢) each in Zones 1 through 6, to increase interstate children's fares by five cents (5¢) each in Zones 1, 3, and 5, and to increase the token rate from four (4) for eighty-five cents (85¢) to four (4) for \$1.05.
- (B) WMATC Tariff No. 30 (Tariff of W. V. & M.)
Generally, this tariff seeks to increase interline passenger fares by five cents (5¢) each in Zones 1 through 6.

The tariffs were issued December 29, 1966, and stated an effective date of January 29, 1967. By Order No. 661, served January 24, 1967, the Commission suspended the above mentioned tariffs until April 28, 1967, scheduled the matter for public hearing on March 9, 1967, made provision for the availability of W. V. & M.'s proposed testimony and exhibits, and directed applicant to post notice on its buses, and publish in a newspaper, notice of the scheduled hearing.

Pre-hearing conference was held, after due notice, on February 17, 1967, to formulate and consider the issues in this case as suggested by Commission Rule 17-01.

Notice was duly given according to the Commission's Rules and Regulations, and public hearings commenced on March 9, 1967.

Four formal parties were admitted to the proceeding. The Commission processed approximately 65 informal protests in connection with the proposed fare increases.

Two sessions of the public hearing were held on March 9 and 10, 1967, producing a transcript of 228 pages and 37 exhibits.

W.V. & M. presented the testimony of its President, S. A. DeStefano, and of its Operations Manager, William W. Wheeler. The Commission staff presented the testimony of its Chief Accountant, Melvin E. Lewis, and its Chief Engineer, Charles W. Overhouse. Jay E. Shanklin, Protestant, appeared and gave testimony on his own behalf. James M. Henderson submitted a written argument on behalf of the City of Fairfax, Protestant, after the close of the hearings.

Witness Lewis testified that his staff had made a thorough audit of the books of W. V. & M. and after making minor adjustments, was satisfied as to their accuracy.

PROJECTED OPERATING RESULTS

The financial and operating data utilized by the applicant in this case covered the historical period of October 1, 1965 to September 30, 1966, supplemented by book data for the twelve months ended October 31, 1966. The Commission staff used the historical year ended November 30, 1966. Each succeeding twelve month period showed a reducing amount of net operating income.

The "rate period" utilized by the applicant and the Commission staff was for the twelve months ended February 29, 1968.

The applicant's projection of revenue estimates for the rate year, under present fares and under proposed fares, differed markedly from those submitted by the Commission staff. (Exh. S-3) This was due to the different methods used of projecting regular route revenue. W. V. & M. took the regular route revenue per mile for each month during the period October 1, 1965 to September 30, 1966, and applied the revenue per mile figure to the projected mileage for each corresponding month in the rate year, thus arriving at projected revenue. The company estimates that it will operate more miles in the rate year than

it did in the historical year, thereby experiencing more revenue.

It is generally considered in the transit industry that an increase in miles operated will normally result in an increase in revenue. However, it should be pointed out, and this Commission recognizes, that while W. V. & M. has continued to operate more miles, it has not experienced any substantial increase in revenue.

The Commission's staff estimated that W. V. & M. would receive approximately the same amount of regular route revenue in the rate year under present fares as it had received for each 12 month period ending with each month from March, 1966 through December, 1966, inclusive.

As a result, the operating revenue projections of the applicant were \$95,000 higher than those of the Commission staff for the rate year at present fares, and \$83,000 higher for the rate year at the proposed fare level. The Commission, however, after careful analysis, accepts the forecasts of the Commission staff as being more realistic, and will use them in computing the operating results of applicant for the rate year.

There was just minor divergence between the expense estimates of the applicant and those of the Commission staff, so the expense estimates made by the staff will be used in arriving at the decision in this case.

The following tabulation indicates the results which the Commission finds would be experienced by applicant under present fares and under proposed fares: (Exh #S-3)

	<u>PRESENT FARES</u>	<u>PROPOSED FARES</u>
Operating Revenue	\$ 4,093,607	\$ 4,510,540
Operating Expense	<u>4,269,805</u>	<u>4,269,805</u>
Net Income Before Income Taxes (Loss)	(176,198)	240,735
Income Taxes	-0-	6,675
Net Income After Income Taxes (Loss)	<u>\$ (176,198)</u>	<u>\$ 234,060</u>
Operating Ratio	104.30%	94.81%
Return on Gross Operating Revenue (negative)	(4.30%)	5.19%

The income taxes charged above were on the actual-tax flow-through basis, giving effect to the estimated net operating loss deduction available in 1967 from 1966. This treatment is consistent with the action of the Commission in applicant's last rate case (WMATC Order No. 452, March 10, 1965.) (Tr. p. 171).

It should also be noted that all projections used were based on the assumption that the adjustment in intrastate fares applied for before the Virginia State Corporation Commission would be granted. This Commission has now been advised by the State Corporation Commission that it has decided to grant the fare adjustments applied for by W. V. & M.

FAIR RETURN

We now have before us the applicant's projected operating results under the present fare structure and under the proposed fare structure.

For guidance on the applicable law governing the determination of what constitutes a fair return, we look generally to our Compact and to the decision of the U.S. Court of Appeals for the District of Columbia Circuit in D. C. Transit System, Inc., v. WMATC, 350 F. 2d 753 (1965).

The latter case spelled out the rate-making objective as involving, among other considerations, the task of assuring

"that all the enterprise's legitimate expenses will be met, and ... cover interest on its debt, pay dividends sufficient to continue to attract investors, and retain a sufficient surplus to permit it to finance down payments of new equipment and generally to provide both the form and substance of financial strength and stability." (D. C. Transit System, Inc., v. WMATC, supra, 350 F. 2d 778)

We are still governed by the constraints spelled out in the Washington Metropolitan Area Transit Regulation Compact (Article XII, Sec. 6 (a) (4), quoted below:

(4) It is hereby declared as a matter of legislative policy that in order to assure the Washington Metropolitan District of an adequate transportation system operating as private enterprises the carriers therein, in accordance with standards and rules prescribed by the Commission, should be afforded the opportunity of earning such return as to make the carriers attractive investments to private investors. As an incident thereto, the opportunity to earn a return of at least 6-1/2 per centum net after all taxes properly chargeable to transportation operations, including but not limited to income taxes, on gross operating revenues, shall not be considered unreasonable.

This commits the Commission to a primary reliance on the operating ratio method, which relates operating expenses (and incidentally net operating income) to gross operating revenues.

This Commission is aware of the peculiar value of the operating-ratio approach to rate-making in the motor carrier industry, as differentiated from the rate-base and return-on-investment techniques. The latter techniques are well suited to a high-cost, long-lived investment base where fixed costs are the major financial considerations. In the motor carrier industry, however, the basic plant devoted to public use is relatively short-lived, and the strategic financial problem turns upon the current operating costs and their delicate relationship to operating revenues.

In the specific case of this applicant, there is no real property; its "long-term" or "fixed" tangible assets are mainly in rolling stock.

This Commission must consider the specific relationship between projected revenues and projected costs, and try to leave a spread between projected revenue and projected costs. This spread represents the carrier's margin, which will have to provide the funds to (1) enable applicant to meet its interest requirements; (2) pay reasonable dividends; (3) permit retention of a reasonable amount in the business to provide for contingencies;

and (4) attract the necessary funds to meet future capital needs.

It hardly needs saying that the net operating loss of \$176,000 forecast for the rate period at present fares (Exh. #S-2) does not satisfy the guidelines of the Compact as to a viable financial situation.

Turning now to the projected results of operations for the rate period, we find that the fares requested, after providing for the new fares to be granted by the State Corporation Commission of Virginia, will produce a net operating income of some \$234,000 (Exh. #S-3), or a margin of 5.19% of projected gross operating revenue. The net operating income here considered was found to equate to a return on projected average rate base, as calculated in staff Exhibit #S-8, of 8.98%; income available to investors, per staff Exhibit #S-9 would be 9.28% of book equity. Each of these percentages fall well within the lower percentiles of the range of reasonableness, in the judgment of the Commission, for a transit company. This applicant has the added disadvantage of a small capital turnover ratio. Whereas capital turnover (the relation of annual operating costs to capital investment) is characteristically high in the passenger motor carrier industry, applicant's turnover, based on operating costs of \$4.3 million (S-3) and projected average rate base of \$2.6 million (S-8) is not even 1-3/4 times. The U. S. Court of Appeals for the District of Columbia Circuit, in D. C. Transit System, Inc. v. WMATC, 350 F. 2d 753 (1965), p. 9, observed:

Among motor carriers, annual operating expenses are often three or four times as great as investment in property. The principal risk in such operations inheres in the cost of operation, not in the investment. (Underscoring added by the Commission.)

Here we are confronted with a case where the risk, lying as it does in the operating costs, is compounded because of lack of productivity of applicant's rate base -- that base is generating a turnover that should be twice what it is, based on the Court's observation of the industry.

The 28 : 72 relationship of equity to debt (Exh. #S-9) contributes to the basic fiscal difficulties of applicant, so

that of the 5.19% margin projected, 3.23% is pre-empted by interest charges. Of the \$234,000 projected net operating income, then, only \$88,500 remains after meeting the interest expense (Exh. #S-11).

On a cash basis, Exhibit S-11 shows that a net cash inflow of \$37,421 can be anticipated in the rate year if the requested fare structure is put into effect. Given the fluctuating fiscal fortunes of this applicant, per Exhibit #S-13, there can be no doubt that the fare increase, if granted, would provide the company with a minimal financial return.

NEED FOR STUDY TO DEVELOP SERVICE IMPROVEMENTS

The brief filed on behalf of the Fairfax Federation of Citizens Associations is basically concerned with the solution of what it considers to be critical transportation problems in the W. V. & M. service area. The Federation contends that a fare increase tends to compound transportation problems and should be approved only in conjunction with remedial measures such as improved service, added convenience, and augmented equipment to mitigate the deleterious effects of any increase in fares.

The City of Fairfax, in its brief, pointed to the potential lying undeveloped in better bus service to and from the City of Fairfax, urging a thorough study by applicant of ways and means to attract more riders.

In this connection, the staff has been informed that, effective in June, 1967, W. V. & M. will provide direct service, hourly, between Washington, D. C. and the City of Fairfax during the midday. It is noted (staff Exhibit S-1) that the company has made some service improvements recently.

The Commission detects some improvement in the quality of applicant's fleet; on pages 8 and 9 of staff Exhibit S-1, it is noted that the average age of buses in service improved from 12.44 years in 1964 to 9.44 years at the end of September, 1966, the percentage of air-conditioned buses in the fleet being, respectively, 26% and 51%. It was forecast also that at the end of the rate year, the average bus age would be 9.20 years and 59% of the fleet would be air-conditioned.

The Commission is governed by the language in its Compact (Title II, Article XIII, Sec. 6(a)(3)) which points to "adequate and efficient transportation services by such carriers at the lowest cost consistent with the furnishing of such service" -- the latter part of the phrase is a necessary concomitant of the first part. The Commission in this Order, as in all of its rate orders, addresses itself to the task of arriving at the exact point of balance that will achieve the former goal without violating the constitutional and practical constraints implicit in the latter.

We recognize that this company faces the classic problem encountered by so many urban and suburban transportation companies throughout the country. In the face of a rapidly growing population, its share of the market is declining or, at best, growing at a rate considerably under the rate of growth of population. Meanwhile its costs are increasing significantly. Thus, a greater need for revenue is being imposed on a declining number of passengers, forcing rate increases which in turn lead to further decreases in ridership.

This Commission, as much as or more than anyone, would like to find a way to break out of this bleak downward spiral. We find merit in the suggestion of the City of Fairfax and the Citizens Associations that means of improving the situation be studied and will order the company to undertake a study. We are also directing our staff, as we issue this order, to work with the company in formulating the kind of study which should be undertaken. We will expect the company fully to cooperate in these efforts. At such time as is appropriate we will enter whatever further orders may be necessary directing the company to undertake studies on its own behalf or hire consultants to assist it.

The problem faced by this company is not a simple one. Indeed, it is highly complex. We are not so foolish as to think that it will yield to some simple analysis or minimal effort. Indeed, it may well be beyond the power of the company or this Commission to effect any improvement. We are unwilling, however, simply to deplore the situation and throw up our hands as to possible means of improvement. Some effort, at least, is warranted. We will pursue that effort in conjunction with the company.

Upon the evidence adduced, the Commission further finds and concludes:

1. That the present fares of applicant are unjust and unreasonable, and will not generate sufficient revenues to maintain applicant in a sound financial condition, and consequently, will not enable applicant to render adequate and satisfactory service to the public in the future.

2. That the fares proposed by applicant are just and reasonable and are not unduly preferential or unduly discriminatory either between riders or sections of the Metropolitan District.

3. That the fares authorized by this Order (together with those now to be authorized by the Virginia State Corporation Commission) will produce sufficient net earnings to allow applicant to service its debt and retain a reasonable amount of earnings in its business, and will enable applicant to render proper, adequate and satisfactory service to the public.

THEREFORE, IT IS ORDERED:

1. That, effective 5:00 A. M., April 16, 1967, W.V. & M. Coach Company be, and it is hereby, authorized to establish the rates of fare as shown in WMATC Tariff No. 29 (Tariff of W. V. & M) and in WMATC Tariff No. 30 (Tariff of W. V. & M.).

2. That applicant file with this Commission, forthwith, appropriate tariffs pursuant to the authority herein granted.

3. That applicant post in all of its buses, forthwith, appropriate notices indicating all such fare changes pursuant to the authority herein granted.

4. That applicant undertake an active program of research and development, hiring the necessary personnel and engaging the necessary equipment, to revise its schedules, its routes, and its standard of service so that riding on this carrier is an attractive choice for its patrons and for the residents and workers

in its service area. Applicant is further ordered, to report to the staff of the Commission as to details of its work in this matter and as to progress being made, within sixty (60) days of the date of issuance of this Order.

BY DIRECTION OF THE COMMISSION:

A handwritten signature in cursive script that reads "George A. Avery". The signature is written in black ink and is positioned above the printed name and title.

GEORGE A. AVERY
Commissioner