[fol. 295] Q. Did you feel that your function was confined merely to eliminations?

A. No, I felt that the company would include what they felt were sufficient expenses.

Q. What they felt were sufficient expenses?

A. Yes.

Q. And you felt that your only duty was to inquire as to whether that was too high, in your opinion, is that correct, Mr. Wiskup?

A. I had no reason to——

Q. Now, I asked you what you thought. Now, please answer my question. If you would like to have it read again, we will read it.

The Witness: Would you please read it, Mr. Reporter?

(The question was read by the reporter.)

The Witness: No, sir, I don't feel that that is my only duty.

By Mr. White:

Q. What, in addition, do you conceive that you should do?

A. I believe it is my duty to inquire as to whether it is proper or not.

Q. If you would discover, Mr. Wiskup, that in your opinion the company hadn't asked for enough expense allowance whether in this category or not, do you think it would be your duty to make an adjustment upward?

A. If I were to discover that in my opinion that had not included enough, yes, sir.

Q. Have you ever done that?

A. Have I ever discovered any?

Q. Yes.

A. Do you mean in this instant case?

Q. Yes.

A. Yes, sir, I think I have.

Q. What is it?

A. I think on Schedule A-7, particularly the last item, where the company would not allow itself enough average gas plant, I increased it.

Q. You discovered an accounting error there, as a matter of fact, didn't you? That wasn't strictly an estimate.

A. I discovered what I thought was not a proper allowance.

Q. I am asking you about an estimate now.

[fols. 296-316] Presiding Examiner: Well, the answer was really argumentative, and not responsive. He asked you specifically whether you had discovered an error. That is the question. The question is whether or not it is an error.

Now, you can go ahead and explain it otherwise, if you want.

Mr. Goldberg: Explain what that item is. Don't quibble about it. Explain what it is.

Presiding Examiner: I don't know what the answer should have been, but I know it wasn't responsive to the question.

The Witness: The company simply took an average, a two-year average, instead of a one-year average, for a particular item in gas plant and I felt that they should get a one-year average consistent with what the staff allows in the averaging process and made the adjustments.

Mr. Goldberg: The adjustment increased the average gas plant?

The Witness: Yes, sir.

By Mr. White:

Q. Did you discover any relation to an estimate, rather than an error in the method of handling figures, Mr. Wiskup, in which you increased an expense allowance?

A. An expense allowance?

Q. Yes.

A. No, sir.

*   *   *   *   *   *   *

[fol. 317] BEFORE THE FEDERAL POWER COMMISSION

TRANSCRIPT OF ORAL ARGUMENT

Hearing Room, Federal Power Commission, Hurley-Wright Building, 1800 Pennsylvania Avenue, N. W., Washington, D. C., Monday, June 9, 1952.

The above-entitled matter came on for oral argument, pursuant to notice, at 10:00 o'clock a. m.

Before: Commissioners Thomas C. Buchanan (Chairman), Dale E. Doty, Claude L. Draper, Nelson Lee Smith, Harrington Wimberly.

[fol. 318] APPEARANCES:

James L. White, Dougherty and White, 30 Rockefeller Plaza, New York, N. Y., and Charles E. McGee, 1729 H Street, N. W., Washington, D. C., appearing on behalf of Colorado Interstate Gas Company.

Jacob Goldberg, appearing on behalf of the Staff of the Federal Power Commission.

The Chairman: Let us be in order.

This matter is before us on a proceeding initiated on the Commission's own motion instituting an investigation under Section 5 of the Natural Gas Act to determine whether any rate collected by Canadian River Gas Company and Colorado Interstate Gas Company subject to the jurisdiction of this Commission is unjust, unreasonable, unduly discriminatory or preferential.

During the course of the proceeding, Colorado Interstate was permitted under the authority of this Commission to acquire the properties of Canadian River so that the present action is confined solely to Colorado Interstate. Following extensive hearings, the Commission by order directed that the intermediate decision procedure be omitted, and set the issues developed by the record for oral argument at this time and place, after the filing of briefs.

Time for oral argument has been allotted as follows:

Commission Staff Counsel, 60 minutes.

Colorado Interstate Gas Company, 60 minutes.

The Commission Staff Counsel may reserve from his opening argument such part of his time as he may indicate for rebuttal.

The reporter is directed to insert in the transcript at this point the Certificate of the Secretary of the Commission with respect to the public notice of this oral argument.

(The certificate of the Secretary, as above-referred to, is as follows):

[fol. 319] FEDERAL POWER COMMISSION

June 3, 1952.

In the Matter of: Colorado Interstate Gas Company, Docket No. G-1115.

Memorandum for the Commission:

The record in the Office of the Secretary shows that oral argument scheduled to commence on June 9, 1952, in the above-entitled matter was published in the Federal Register on May 30, 1952; 17FR; p. 4962, and was sent on May 26, 1952, to the parties and interested persons of record and to States or other governmental authorities deemed to have an official interest in the proceeding.

Leon M. Fuquay, Secretary.

The Chairman: Will counsel enter their appearances in the order designated above?

Mr. Goldberg: Mr. Chairman, for the Staff of the Commission, Jacob Goldberg, Attorney.

The Chairman: And how do you wish to divide your time?

Mr. Goldberg: I shall take 45 minutes for my main argument, and 15 minutes for rebuttal.

Mr. White: For Colorado Interstate, James L. White, Dougherty and White, 30 Rockefeller Plaza, New York;

and Charles E. McGee, 1729 H Street, N. W., Washington, D. C.

The Chairman: You may proceed, Mr. Goldberg.

Oral Argument of Jacob Goldberg, on Behalf of the Staff of the Federal Power Commission

Mr. Goldberg: May it please the Commission, as has been indicated, this is a proceeding under the Commission's own motion under Section 5 of the Natural Gas Act.

I may say that hearings began on October 1, 1951, and the exhibits that were introduced were pro forma on the basis [fol. 320] of a mergered corporation, so there is no difficulty about the merger of Colorado and Candian River.

The Staff exhibits consisted of a cost of service study based on company operation for a year ending June 30, 1951, and also the Staff introduced an allocation based on that cost of service, a rate of return study, an allocation of the gasoline loss operations, and a full complete rate case.

The allocation at that time showed that excess revenues amounted to $3,272,521.

Thereafter Colorado Interstate raised the question that the facilities authorized at Docket No. G-1326, and the facilities in the pending application at Docket No. G-1677, were not included in the Staff's cost of service study, and Colorado Interstate at that time stated it was expected that these facilities would be in operation during 1952. Accordingly, the Staff then introduced a cost of service study for the future based on the years 1951, '52 and '53, and these estimates were taken from the figures given in the application filed by Colorado Interstate at Docket No. G-1677.

After that, Colorado Interstate came in with a cost of service study in which it, in the main, relied on the estimates in the application at Docket No. G-1677, but broken down. At that time, however, Colorado Interstate did not introduce an allocation, and did not introduce any allocation of gasoline operations, but it introduced a rate of return study.

Following that, the Staff introduced a cost of service study for 1952, based on the estimates which Colorado Interstate had introduced in its case in chief, and thereafter Colorado Interstate introduced another cost of service study for 1952, together with an allocation, and an allocation of gasoline operations, among other things, but those are the highlights.

Now, the Staff does not consider that the amended cost of service study warrants or at least shows any items that are proper costs, so we are relying on the cost of service [fol. 321] study which we introduced following Colorado Interstate's estimates, in which we accepted all their estimates of revenues, their rate base, their accrued depreciation, we accepted their estimates of operating expenses, by and large. There are a few adjustments which I shall refer to. In all, the Staff made six adjustments. Several of course which were introduced in the beginning, which were implicit in this rate hearing, namely the gasoline loss operations, and the depletion for tax purposes.

Now, I shall discuss these six adjustments. Incidentally, the last adjustment has to do with taxes, and that necessarily follows, from any adjustment you make you have got to adjust your tax liability.

Now, the first adjustment is a very simple one. It merely reduced the return from a 6½ per cent rate, which Colorado Interstate had used, to what we then considered a 6 per cent rate of return for illustrative purposes. That deduction was $274,666. Since then, the close of the record, the Staff has recommended a 5¾ per cent rate of return, so that the net result there is $431,061.

There were minor changes in plant account which Colorado Interstate subsequently accepted. There was a minor change in accrued depreciation, or rather in the net plant because of the difference in depreciation for the year, and also a change in working capital because of adjustments in operating expenses.

Commissioner Smith: Mr. Goldberg, does that recommendation of the 5¾ per cent, as contrasted with 6 per cent as a fair rate of return, does that in part reflect your criticisms of the witness Merrill's testimony in respect of rate of return, and does it involve any question whether in view of the financial costs here shown, management is fully efficient?

[fol. 322] Mr. Goldberg: No, sir, our rate of return, which I shall come to as a separate discussion, if I may——

Commissioner Smith: I thought you were leaving the point.

Mr. Goldberg: I am perfectly willing to discuss it now, but I would prefer to discuss the adjustment and then come to that as a separate discussion.

Now the next adjustment was Regulatory Commission Expense. That is divided into three parts. The first part is $10,000, which was paid to Price, Waterhouse for the testimony of Mr. Houlihan in the merger proceedings. That is non-recurring.

In effect, Colorado Interstate states it is non-recurring, but states that a certain cushion has to be allowed for the occurrence of non-recurring items. We maintain that very statement shows it is a synthetic cost, and not a know- cost.

Also, there is an item of $95,000 involving court review of this very proceeding, and we have recommended that that amount be disallowed, because nobody knows what the Commission determination will be in this proceeding, and nobody knows, whatever the Commission determination will be in this proceeding, whether Colorado Interstate will seek Court review.

The third item was the amortization period. Colorado Interstate amortized regulatory commission expense over a three-year period, and we recommend a five-year period. A five-year period is the one usually adopted, and we say there are no unusual circumstances here that warrant a change from the five to the three-year period.

The next adjustment is the annual depreciation and depletion allowance. There has been a great deal of confusion, I am afraid, as to what the staff did in this case, and I think what the staff did is perfectly simple.

[fol. 323] Commissioner Draper: Did they put it on the record, what they did?

Mr. Goldberg: Oh, absolutely.

Commissioner Draper: All right.

Mr. Goldberg: Absolutely. Everything I am saying here this morning is on the record, Mr. Commissioner.

What the staff did in the first go-round, we rolled into depreciation for all the various accounting properties, the Panhandle and Hugoton line were rolled into one composite depreciation rate, and at that point there was very little dollar difference between the annual depreciation that Colorado Interstate claimed, and what we allowed. Part of it was due to the fact that we allowed more for field lines and gathering system than Colorado Interstate claimed because we did it on a unit of production method, rather than straight line of depreciation method.

When it came to the new facilities, the staff felt that this composite rate for the old facilities had already been testified to, had already been cross-examined upon, and the question arose to the service life of the new facilities, and we kept them separate. Now, that is not to say that you can't roll in the whole business, because that is what we did in the first place. We took the service lives of the Panhandle field, the services lives of the the Panhandle properties, and the Hugoton properties, and by the mechanics of weighing them in, dollars, age, and so forth, rolled it in. That is the result here, except we kept it separate to show what we did first, and what we were doing the second time.

Now, in the second—for the new facil-ties, the staff recommended a 25-year service life. The staff witness explained thoroughly on the record the basis of the 25-year service life, the reserves in the Panhandle and Hugoton fields, the fact that 80 per cent of these facilities were to be used for transmission, and therefore any new gas reserves would necessarily be tied on to the transmission facilities. They are not apt to discard the transmission facilities and build new facilities, but if they get a new field, they will [fol. 324] tie it into the existing transmission facilities.

The fact that Colorado Interstate filed an application to tap the Keyes Field along the route of these new facilities, the fact there is exploratory work in the area, all those facts were explained on the record as to why this witness took a 25-year service life.

Of course, insofar as the facilities are assumed to be in operation as of January 1, 1952, he started to depreciate based on a 4 per - basis as of January 1, 1952.

Now, what did Colorado Interstate do, they work on a diminishing life basis, they take their net plant, and depreciate 1/25th, 1/24th, and when they came to the new facilities, they assigned one twenty first, and one twentieth and a half for those starting during the year. The result of that is they take a service life of only 20 years for the new facilities, and don't show any reason why - take a 20-year service life, except they have started to depreciate on this diminishing life basis beginning January 1, 1948, and just say "We will use the same rate for these facilities," without any reason as to why they are using a shorter service life for these new facilities.

I may say also because the staff has used a different service life than Colorado Interstate, Colorado Interstate says the staff should recompute the accrued depreciation. Well, that isn't so, because the Commission is aware of the fact that the Commission will accept the book reserves, especially where the book reserves have been set up in a rate case, and they have been built up under rates following that rate case, and I need not remind you gentlemen that in 1942 the Commission entered an order fixing the rates of Colorado Interstate, and also fixed the book reserves as of that date.

The fourth adjustment is an adjustment to reflect the loss on the gasoline operations. Now, this entails a discussion of the Commission order in the merger proceed- [fol. 325] ings at Docket No. G-1326. It will be recalled that in the order issuing a certificate in which the merger was approved, the Commission conditioned the approval to provide that the costs properly allocable to the gasoline operations, if they exceeded the amounts that Colorado Interstate would receive from the gasoline operations, then and in that event such excess would not become a part of the cost of service and not be chargeable to the ratepayers in any rate inquiry.

Now, the staff has made a study of the costs properly allocable to the gasoline operations, and have found that based on a 6 per cent rate of return the loss on gasoline operations is $601,000, and based on a 5¾ per cent rate of return is $585,528.

Now, I may refer, or rather refresh your recollection as to the operations under the merger proceeding. Under the plan which is now operating, Colorado Interstate produces, gathers the liquid hydrocarbons, brings them to the two plants that Colorado Interstate owns and operates, the Bivins plant, and the Fourway plant, processes these hydrocarbons, and delivers them at the loading rack to Southwestern, or Southwestern's nominee, now West-Pan Hydrocarbon. In turn, West-Pan sells the finished gasoline, and in turn transmits 50 per cent to Colorado Interstate, out of which Colorado Interstate has to pay the cost of producing, gathering and extracting the gasoline and hydrocarbons.

Now, as to the Fritch plant, operated by the Natural Gas Pipe Line Company, Colorado Interstate receives certain revenues from Natural Gas Pipe Line—in other words, Natural Gas Pipe Lines takes off some direct costs, and transmits the remainder to the Colorado Interstate. Under the merger agreement, 85 per cent of those revenues received from Natural Gas Pipe Line are transferred to the West-Pan, and only 15 per cent remain with Colorado Interstate.

Now, in making the allocation of the cost of the gasoline operations—and there is no denial that the Commission intended that the gathering cost should be included in [fol. 326] the cost, and Colorado Interstate so admits—the staff used what is known as the relative market value theory.

Commissioner Draper: What theory?

Mr. Goldberg: The relative market value theory, or sometimes called the relative value theory. What they did was this: They took five cents as the cost of the dry gas, and took the estimated revenues received from all the sales, the West-Pan revenues, minus the cost to make it marketable, and those revenues, incidentally, were based on a 5½-cent price for the gasoline, and by weighing them against the relative volumes of gas processed, arrived at a figure of 18.6 per cent as the total of the wellmouth and gathering cost for the three plants to be allocated to gasoline, and the remainder better than 80 per cent stays with the dry gas.

Now, against that, Colorado Interstate allocates 1.27 per cent of the total wellmouth and gathering cost to the gasoline, and better than 98 per cent to the dry gas, and the reason they arrive at a 1.27 per cent figure is they take one per cent as the shrinkage of the wet gas going into the Bivins and Fourway plant, and 2 per cent as to the gasoline being processed in the Fritch plant, and because of the weighing of the volumes they come out with a 1.27 percentage.

The important thing is that out of total cost of $4,323,547 which Colorado Interstate states is the cost of wellmouth and gathering, only $55,000 is allocated to the gasoline, and I might say that out of $3,852,000 of total wellmouth and gathering cost which the staff found, $715,000 is assigned to the gasoline.

The Chairman: What percentage would that be?

Mr. Goldberg: A little better than 18 per cent, sir. Now as to the gasoline plant, the staff allocated all the cost of the gasoline plant to the gasoline on the theory that the gasoline plants are for the benefit of the gasoline. They did take out a certain amount of cost of plant that is used to dehydrate the gas, and there again there was evidence that in processing the gas through the gasoline plant, it [fol. 327] picks up a certain amount of moisture. That is why the dehydration always is at the tail gate of the plant, rather than at the beginning, because it would be a waste to dehydrate it at the beginning because it would pick up moisture going through the process. Despite that we allocated a certain portion of dehydration cost, or rather all the dehydration cost to the dry gas.

Now, I should say that Colorado Interstate allocates a portion of the gasoline plant to the dry gas, and they do it this way. They say a certain portion, or at least a half of the cost of the gasoline plant are joint costs, and the minute they say it is joint cost, they run into this 1.27 per cent allocation, so in effect they are saying about two-thirds of the cost, when you include also the cost they assign as direct to the dry gas, in effect they say that two-thirds of the cost of the gasoline plant is to be ascribed to the dry gas, and only one-third to the gasoline extraction.

As a matter of fact, if you take all their wellmouth and gathering costs, and all the gasoline plant costs, and total up all the costs that they assign to the gasoline, you arrive at the fact that only 8 per cent of all these costs is assigned to the gasoline.

Now, we maintain, may it please the Commission, that the relative market value is a more reasonable one, it comports with common sense, it gives due weight to what the parties are investing their money for, the value of the product.

There has been a great deal of literature written on the subject, and from what I have read of it, the relative market value theory is the one that is universally—I say universally, I mean usually, all the writers say the relative market value theory is the one that is universally used in the petroleum industry.

Now, Colorado Interstate also says even if the relative market value theory is the correct theory, the staff has not used the correct market values, and we maintain that we have.

[fol. 328] The five-cent value of the dry gas is much above the weighted average that the Texas Railroad Commission found in the order just preceding the introduction of our evidence.

Commissioner Draper: Where did you get the five cents?

Mr. Goldberg: The Texas Railroad Commission twice a year has hearings, Mr. Draper, as to the weighted average of gas being paid in the Panhandle field, and that study of September of 1951—and this evidence was introduced in October 1951—that evidence showed that the weighted average being paid in the Panhandle field, on the same pressure base that we used, was a little under five cents for the wet gas and dry gas, and we gave them the benefit of the doubt and used five cents for the dry gas.

Now, also, Texas has a production tax as well as a gathering tax. It had a production tax for a long time. Under the production tax, the producer has to pay a tax based on the market value of the gas and in paying that tax, Colorado Interstate, or rather Canadian River, used a value of 4.33 cents for the gas. That was what they said was the market value of the gas.

Also, as I will come to in a moment, we used a five-cent allowance for depletion purposes, and we felt to be consistent if we were going to use the five cents for tax purposes, we should use the same five-cent value for this allocation, and also, so far as this relative market value and shrinkage theory is concerned, when Colorado Interstate pays special royalties for the gasoline content, there are some contracts where there is a special allowance for the royalty for the gasoline content, they don't pay the royalties based on shrinkage, they pay them on the gross revenues received at the tail gate of the gasoline plant. That is what the royalties are based on, on the value.

The fifth adjustment has to do with depletion allowances for tax purposes, and I refer to the Commission opinion in Docket G-1326. I think you gentlemen will recall that Colorado Interstate, in support of the public convenience and necessity for the merger alleged that the benefit that Colo-[fol. 329] rado Interstate would receive from the merger would be the five-cent depletion allowance, and when it was pointed out that the last settlement with the Internal Revenue for the 1945 tax year was based on a 3.17 cents depletion allowance, Colorado Interstate said, ''Oh, no, we are going to get the five-cent allowance.'' Based on that—and I need not quote the Commission, it is in the order—they found that it was reasonable to assume that the five-cent value would be allowed, and all the evidence in Docket G-1326, all of which evidence was incorporated by reference in this proceeding, there has been no new fact to show any change of condition, nothing, and we maintain that Colorado Interstate is estopped, for one thing, now, to say that the rate should be fixed on the 3.17-cent allowance for tax purposes as against the five-cent rate. The Commission was led to believe that the five-cent rate would be proper——

Commissioner Draper: Well, we are dealing with facts here, suppose we presume it is five cents. Should we adhere to the 3.17, or what should we do?

Mr. Goldberg: We took a five-cent value, because that is what they said they would get. They are claiming more than 3.17 now, and have been since the merger proceedings.

Commissioner Smith: How much time intervened between the representation made in the merger case, and the presentation of evidence in the rate case?

Mr. Goldberg: I will say this much. The merger hearing was concluded, the order was issued in February 1951. Now, certainly if they knew of any facts that would disprove the five-cent rate, I think they were duty-bound to inform the Commission.

Commissioner Smith: It would seem so to me. I take it your position is if the contention is made in one direction in one case, then that contention should not be departed from five minutes later for purposes of another case. Is that your position?

[fol. 330] Mr. Goldberg: Well, not as *bald* as that. I do say this, however, Mr. Commissioner. Where they make a representation on which they expect the Commission to rely, and on which public convenience and necessity is the basis of the representation, the Commission relies on that representation, issues the certificate, then in those circumstances I don't think it lies in their mouth to turn around and say they want the 3.17-cent rate for tax purposes. Not only that, but in April 1951, after notice of this hearing went out, you will recall notice of this hearing went out in March of 1951, or at least it was intimated in the order of the merger proceedings that the Commission intended to set the rate matter for hearing. The order went out in March. In April of 1951, they filed application in Docket G-1677, and at that time in their pro forma estimate of expenses, operating expenses, they used a five-cent rate for tax purposes, for the depletion allowance.

Not only on the theory of estoppel, but on the theory there are no new facts here, aside from the time, if there were any new facts within the period of time, they introduced none at the hearing, and we maintain they couldn't introduce any, there were none to our knowledge, so based on the same facts they intended the Commission should rely on for the five-cent rate, they should rely on the same facts in this hearing.

Now, the sixth adjustment has to do with taxes. There is nothing to discuss there, because they follow automatically from the other adjustments.

I want to say a word about the amended cost of service that Colorado Interstate introduced. What they did, they took their January payroll figures for general and administrative, added 4 per cent to that, and multiplied it by 12 and came out with an annual payroll. They increased that amount by $165,000.

The four per cent increase, of course, is synthetic. That is something that they expect the cost to increase by that amount, and we show as of the date when they introduced that, the cost of service actually was declining.

[fol. 331] The other operating labor they increased by 8 per cent, 4 per cent of which they say——

Commissioner Wimberly: You say the operating costs were declining. Are you referring to payroll cost?

Mr. Goldberg: I said the Department of Labor Monthly Statistics declined. They said 4 per cent increase because of future cost of living increases. T-ey are not paying that 4 per cent, but they said there may be some future cost of living increases. We showed that at the same time they were saying the cost of living was going to increase, we introduced the Department of Labor statistics showing a decrease, and the other operating labor they increased by 8 per cent, 4 per cent they say they are actually paying, and 4 per cent is future increase in cost of living.

We maintain that so far as the actual 4 per cent, that has already been taken care of because there are a lot of future operating expenses in these estimates. Nobody knows what will happen——

Commissioner Wimberly: In making their estimates, they included figures for increased costs?

Mr. Goldberg: Yes, sir, for more employees.

Commissioner Wimberly: And then added another 4 per cent?

Mr. Goldberg: On that, another 4 per cent. Now, we allowed all the future employees they said they would hire. We made no adjustment downward because somebody might leave a job and they wouldn't fill the job. We made no allowance for the fact that as a result of the merger certain economies would result: office rent, office machines, and so forth.

Now, the other costs are the gas royalty expense they say they will incur, those were not actually known costs.

We included everything they were paying. These were things they said they might possibly have to pay, except one [fol. 332] item, the directors and executive committee payments. Apparently they will pay that because that was voted on at a board of directors meeting. I need not go into the details of that, it is explained in my brief.

In March, just before the public offering of the stock, the two largest stockholders, the Union Securities group, and the Sinclair Oil Corporation, the presidents of each became directors, and also members of the executive committee, and they voted themselves a $5,000 fee as director, and a $30,000 fee for Mr. King, president of Union Securities, and $15,000 fee to Mr. Spencer of Sinclair.

Commissioner Wimberly: $15,000 annually?

Mr. Goldberg: In addition to the five, and then in the next month those corporations were going to sell their stock to the public, and we maintain prior thereto the directors never got fees as such, they got expenses, and the executive committee never got fees, as such. There was nothing in the record to show what these people were going to do. The circumstances surrounding the voting of these payments we felt showed they were not proper costs of service.

The Chairman: You seem to relate these new fees to the sale of stock. What is the relationship there, or is there any?

Mr. Goldberg: Well, I say within a month. It was less than a month, within three weeks after this Board of Directors meeting, the Union Securities group was going to sell most of its shares, and Sinclair was going to sell all of its shares, and yet the President of Sinclair becomes one of the remaining Board of Directors, and Executive Committee, and Mr. King remains as one of the remaining directórs, and also Chairman of the Executive Committee, and it just seems to us the whole circumstance showed a clear-case of feather-bedding.

Commissioner Smith: In effect, you are contending this is a kind of lame-duck action, which resulted in a sort of feather-bedding?

Mr. Goldberg: Yes, sir.

[fol. 333] Commissioner Smith: You spoke of the circumstances. Does the record show the circumstances of the directors meeting?

Mr. Goldberg: Yes, sir. I couldn't get into it too thoroughly, but it shows the dates, the sequence, who the people are, and the fact of the public offering.

Commissioner Smith: Does it show the voting of the respective directors?

Mr. Goldberg: I tried to get that, but couldn't, Mr. Smith.

Commissioner Smith: You mean the information was refused?

Mr. Goldberg: Well, the Examiner ruled, as I remember his ruling, that so long as the Board of Directors voted on that, we could not ask the witness who sponsored the cost of service, and who stated that all of these costs were proper costs of service, we could not cross-examine that witness on that line, and at that time I was stymied, despite the fact that I tried to get—the witness admitted he was sponsoring all these as proper costs of service, the Examiner felt that the Board of Directors having voted, it was an ipse dixit transaction.

Now, I understand that Mr. Spencer has refused to take the $15,000. You can draw any conclusion from that that you want, gentlemen. At any rate, it is not a cost of service, if they are not going to pay it to him.

Commissioner Draper: Maybe he doesn't need the money.

Mr. Goldberg: It may be because of his income tax.

The Chairman: But he did refuse the $5,000 directors' salary?

Mr. Goldberg: I think so. As I read it, he is going to resign from the whole Colorado Interstate situation. He hasn't done it yet, that I know of.

Commissioner Smith: Let me see if I understand your position here. You are not necessarily, as I understand your position, you are not necessarily objecting to proper [fol. 334] payments to what you might call public directors for services which they may have to render in connection with the responsibilities that they assume, but you are pointing here to the fact that these are not public directors in the usual sense, these represented institutional investors, or controlling companies, or financial institutions.

Mr. Goldberg: Quite right.

Commissioner Smith: Mr. King is who?

Mr. Goldberg: President of Union Securities Corporation, which is in turn a subsidiary of Tri-Continental, another holding company.

Commissioner Smith: Well, I am not interested in that, but Union Securities, you said they were disposing of their ownership interests, in large part, at least, in Colorado Interstate.

Mr. Goldberg: Yes, sir.

Commissioner Smith: Well, now, does what you say Mr. King's position is——

Mr. Goldberg: He is president of Union Securities.

Commissioner Smith: I mean his position with Colorado Interstate.

Mr. Goldberg: Director, and Chairman of the Executive Commmittee.

Commissioner Smith: And as Chairman of the Executive Committee, would he be in a particularly advantageous position in so far as acquiring the financing of Colorado Interstate is concerned in the future?

Mr. Goldberg: I don't think he would be in any more favorable position than anyone else so far as helping Colorado Interstate's financing.

[fol. 335] Commissioner Smith: I wasn't talking about that, I was talking about securing that business for his own concern, Union Securities.

Mr. Goldberg: Oh, yes, sir.

Commissioner Smith: Does the record show whether Union Securities participates in pipe line financing?

Mr. Goldberg: This record doesn't show it, no, sir.

Commissioner Wimberly: Is Union Securities a financing house?

Mr. Goldberg: Yes, sir, and I think it is common knowledge that they financed Mississippi River Fuel, and some others.

Commissioner Smith: Mississippi River Fuel, did you say?

Mr. Goldberg: Yes, I am pretty sure about that.

Commissioner Smith: Didn't the president of the Mississippi Fuel recently go on the Board of Colorado Interstate?

Mr. Goldberg: Quite right.

The Chairman: That was at the same time, was it not?

Mr. Goldberg: Yes, sir.

The Chairman: Did you say Union Securities was the agencies for the sale of stock?

Mr. Goldberg: Yes, sir, for the public offering.

The Chairman: In response to Commissioner Smith's question, there was relationship, then.

Mr. Goldberg: As a matter of fact they got quite a fee for handling the sale of the public securities.

Commissioner Wimberly: Just a minute. Was any additional stock sold to the public other than that which was owned by Sinclair, and by Union Securities?

Mr. Goldberg: Largely those two. I think there was a [fol. 336] small amount that some private people sold, but whatever it was, it was so small it was lost in the shuffle.

There is one other point about the pension benefits, and so forth. Now, we allowed every cost for pension and group hospitalization, but they came in with their amended cost of service and said one insurance company had submitted a new plan which would increase the cost. The Board of Directors hadn't even considered that plan, and we rejected it.

The Chairman: Are there any representatives of that insurance company on this Board?

Mr. Goldberg: Well, the insurance company happened to be Prudential. All I can say is that Prudential Life Insurance Company owns most of the notes of Colorado Interstate, but this was one plan by one insurance company, the Board of Directors hadn't even considered it, and we felt in view of that it was not a known cost that should be allowed in cost of service, but we did allow every cost they are actually incurring for the payment of pensions and hospitalization.

Now, classification and allocation will take just a moment. The recent Atlantic Seaboard case, we think, is determinative of this case, and dispells the allocation classification that Colorado Interstate made. Every known cost they could consider fixed was classified as a fixed cost, and thereby transmitted into a demand cost.

As to rate of return, we feel that this is a very unusual case, and that the Commission here has concrete evidence as to what the cost of equity capital is. I may say that the cost of debt financing, and preferred stock financing, there is no dispute between the Staff and the company, that we come to the cost of equity capital, and you couldn't have a better case. Two days before the hearing closed, they sold to the public 966,000 shares of stock, Union Securities group, and the Sinclair group, and they sold them to the public at $26.75, net to the sellers, $25.25.

Based on the $1.88 earnings as of December 31, 1951, on earnings price ratio, it is 7 per cent. If you want it on the net company price ratio, it is 7.5 per cent.
[fol. 337] Now, I can't see what better evidence you want of what the cost of equity money is when two days before the hearing closed, they sold 56 per cent of the outstanding shares to the public, at a cost of 7 per cent, and we allowed almost 9 per cent, 8.95 per cent, so certainly the Staff was generous in allowing 9 per cent, or almost 9 per cent as against the 7 per cent it actually cost them.

Their financial expert, Merrill, said the cost of equity capital should be 11 per cent, and he based it on certain earnings price ratios he picked out, and came out to 11 per cent. The staff of course also used earnings company price ratios based on the monthly averages of the natural gas stocks that are traded on the New York Stock Exchange. We took the monthly average of the seven natural gas com-anies who report to the Commission, and that averaged out at 8 per cent on an earnings price ratio, and we allowed 8.95 per cent.

The Staff feels that 5¾ per cent over-all rate of return is generous to the company, and I might say that had we stayed with the 7 per cent, or the 7.5 per cent as the cost of equity money, the over-all rate would have been something like 5⅛ per cent rate of return.

I don't know whether you gentlemen are interested in the results of that financing, but unfortunately the hearing closed before the results became known, but Colorado Interstate has filed a post-effective amendment No. 1 to their registration statement, which is already incorporated in these proceedings, and I should like to move that that post-effective amendment No. 1 of the registration statement be incorporated by reference in this proceeding.

Mr. White: I have no objection, Mr. Chairman.

The Chairman: We will take the matter under advisement.

Mr. Goldberg: I should like to disclose, however, that they oversold their shares, and the result is they have got [fol. 338] to buy back on the open market, or buy back from Sinclair some remaining shares at a price higher than what they sold to the public.

Commisioner Smith: Who is they?

Mr. Goldberg: The sellers, the Union Securities Group, the head of the underwriters. Now, we maintain, may it please the Commission, that the cost of service proposed by the Staff, and the allocations are just as reasonable, and should be accepted by the Commission. Thank you.

The Chairman: We will recess for five minutes.

(Whereupon, at 10:52 a. m., a recess was taken until 10:57 a. m.)

The Chairman: Mr. White?

Oral Argument of James L. White, on Behalf of Colorado Interstate Gas Company

Mr. White: May it please the Commission, as indicated by Staff counsel, the differences between the company and the Staff at this point in the case relates to rate of return, depreciation, the cost of gasoline plant operations, income taxes, particularly the wellhead value percentage depletion, and certain adjustments to cost of service, as well as the allocation of cost as to which there are fundamental differences, but the allocation of cost - always be dependent first on the cost of service which you allocate, the main stress has been placed and will be placed by me upon the cost of service itself.

Commissioner Draper: In dollars, what is the difference between the Staff?

Mr. White: Between the Staff and the company, Mr. Commissioner, it is roughly about $4,000,000.

Commissioner Wimberly: That is the over-all difference?

Mr. White: The over-all difference, yes. In our principal brief, page 3, starting at page 3, we indicate the various [fol. 339] costs of service which the Staff had put in, and they indicate an overall excess of $3,296,000 on their last cost of service, the year 1952, which upon allocation amounts to $3,077,365, and the company indicates a deficiency applicable to jurisdictional sales in the amount of $1,837,000.

The over-all deficiency is $838,819, in the company's presentation, Exhibit 30 in this case.

Now, on the matter of rate of return, the principles under which this Commission must act, and will act, have been set forth in the famous Bluefield Water Works case, and more lately in the Supreme Court opinion in the Hope Natural Gas Company case. The principle upon which you are to proceed is that the financial soundness of the business must be assured, and the return to the equity owners should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover—and I am quoting the.Supreme Court Hope case now—should be sufficient to insure confidence in the financial integrity of the enterprise so as to maintain its credit, and to attract capital.

It is our contention that the application of that principle here requires a minimum rate of return of 6½ per cent. You must bear in mind that all companies, all industries regulated and non-regulated, compete for the investor's dollar, and the investor is a fellow who can look at things pretty objectively and find what offers him the best rate of return.

As Mr. Goldberg says the greatest difference between the Staff and the company on the rate of return presentation is the requirement of the return on the common equity. Mr. Goldberg made reference to the fact that the stock had been sold just two days before the conclusion of the hearings in this rate case, a substantial block of the company's stock. I must point out that the company did not get any new money out of that stock. That wasn't the company's stock that was being sold.

[fol. 340] Commissioner Smith: What has that to do with it? That nevertheless represented the independent investors' market appraisal of the worth of the stock?

Mr. White: I wonder if it does.

Commissioner Smith: I don't know how you could get a better test.

Mr. White: Mr. Commissioner, there is this to it. You must remember in effect there was being a liquidation of certain interests which had previously held Colorado Interstate Gas Company, and it was pursuant in part to an order of the Securities and Exchange Commission. Now, the company had been newly merged, only as of the first of this year, and investors may be willing under those circumstances to take a smaller yield where there is a greater dependence upon developing earning power as in effect a new enterprise proceeds, which is the fact here. This is the first time the company has operated as an integrated company.

Commissioner Smith: I recognize the force of what you say, but notwithstanding the fact that this was in a sense a forced sale, the fact that there was, at least so Mr. Goldberg asserted, over subscription, it looks as though not only is your company competing for the investor's dollar, but the investors were competing for your company's securities at this price.

Mr. White: That appears to be the case, and there is no gainsaying the fact that there was an oversubscription of it, but there are these other factors which must be borne in mind. Were the company itself in a position of acquiring funds, then the investors' appraisal might be a different one entirely.

Coming again to the Bluefield and the Hope principles on that, we have got to look at what must be given from the competitive standpoint so we effectively can compete for this investor's dollar, and it is on this basis that we contend that the return on this equity hadn't been the 8.95 [fol. 341] per cent which Staff counsel is contending for, but must be 11 per cent.

Now, as to the 8.95 per cent which the Staff has put forth, the Staff in effect—I think its brief clearly indicates this point—has decided 5¾ per cent is an adequate return to Colorado Interstate Gas Company, and from that they determine that 8.95 per cent return would result on the common equity.

Now, we have replied to that at some length, and I am not going to quote from the brief, in any respect. I am confident that the Commission will read the briefs in this case, but I do, for the purposes outlined, want to follow what we say there in relation to this 8.95 per cent which the Staff contends is adequate.

In arriving at this, the Staff has eliminated from schedules in their rate of return exhibit anything that is higher than 8½ per cent yield on common equity. In effect, what they do is eliminate items, six in number—I am sorry, what I mean to say is if they are going to effectively determine what is an investor's appraisal of the requirements of return upon equity money, they should eliminate any items that are those of companies that have as yet undeveloped earning power.

Now, in the schedule which they assume to use as support for this 8.95 percent, there are six issues of the Tennessee Gas Transmission Company which it is shown in this record has not developed its earning power, and similarly the case of Texas Eastern Transmission Corporation, two issues of Texas Gas Transmission Corporation, MidSouth Gas Company, which is probably the baby of all the gas companies right at the moment, Equitable Gas Company because there again there was not an offer for new money, it was a great deal in the situation of Colorado Interstate, it was being sloughed off as a part of a previous holding company system, and we contend that out of a list of 25, only seven of the 18 used by the Staff—they didn't use 25, they used

18—are left, and if we take the yield requirements on those common stocks we find that we come up not with 8.95 per [fol. 342] cent, but rather with 9.8 per cent.

Commissioner Smith: You are saying, as I understand it, that there should have been eliminated those companies to which you referred because their full earning power had not yet been developed.

Mr. White: That is correct.

Commissioner Smith: I thought in terms of your answer to my earlier question, you contend those are the very companies that should be taken into account, because comparable to your own situation.

Mr. White: I don't mean to indicate that, sir. I am indicating only this, both with relation to the recent sale of Colorado Interstate's stock, and the companies to which I was just referring, that someone is willing to take less now when he expects more in the future as the company develops.

Commissioner Smith: I understand your point, I think.

Mr. White: I think that is the case here.

Now, in developing the contention that 11 per cent is the return we should have on our common equity stock, I want to discuss just how this was approached by the witness Merrill, Colorado Interstate's witness. He noted the position of the natural gas industry in the over-all economic picture, and one of his prime sources of material on that was this Commission's statistics of natural gas companies, and he noted there the tremendous uptrend in gas sales which has been going on for some time, and he noted comparative profit trends, and he compared the trend of the net income of natural gas companies,. as shown by the Commission's statistics, with the trend of the net income of 20 leading oil producers and refining companies, and with about 350, or 378, I think, to be exact, industrial companies.

[fol. 343] Now, the results of this study showed that from 1946 to 1950, profits of the oil industry increased 116 per cent. The profits of the industrial group increased 100 per cent, while the profits of natural gas industry fell behind both of these groups, and increased only 78 per cent above the 1946 level. At the same time the gas sales had increased far and beyond any of these comparable industries so far as their gross output was concerned.

Now, reducing that to percentages, for comparative purposes, the average return by representative oil companies showed an increase of from 6.52 per cent to 12.92 per cent between the three pre-war years 1939 to 1941, and in the five post-war years, 1946-1950. Manufacturing companies showed an increase from 9.40 per cent to 14.5 per cent during those two different periods. The average rate earning power of natural gas companies, however, was 6.82 per cent in the pre-war years, and only 7.04 per cent for the five post-war years. Now, we just aren't keeping up with the general economy on that basis, so then he analyzed the composition of the invested capital in these various industries, and he found that the natural gas industry from 1939 through 1950, the long-term debt to total capitalization rose from 35.4 per cent since the end of the war to 54.3 per cent in 1950, and the period January 1, 1946, the total increases in invested capital was $2,228,000,000, of which $1,506,000,000, or 67.6 per cent was raised by debt financing. Contrasted with this the oil industry, which we conceive of as being comparable, it is an extractive industry engaged in developing a wasting asset, they raised substantially all their new capital without very significant changes in long-term debt, about 85 per cent of their new money being secured in that way.

Now, the purpose of pointing all this out is that you have got to realize that one of two things is happening. Either the companies just like to finance through debt, which I don't think is true, or else they have got to preserve a reasonable earning for the common stockholder by having equity thinned out, or, as we sometimes refer to it, highly levered.

[fol. 344] Now, the cost of debt money, the composite company cost is 3.21 per cent. The latest cost of debt money to the company, however, as the Commission knows, is 3.75 per cent, and that was the most recent loan from Prudential Insurance Company, the loan agreement itself antedating the merger of the two companies. The industrywide requirements seem to be 3.50 per cent. The cost of debt money has increased over the years. It seems particularly to have increased since the early spring of 1951 when the Government withdrew its support of Government bonds.

On preferred stock, the situation isn't very important, but the company does have a small amount of preferred stock and as the Commission will note from Exhibit 43, I think it is, in this case, it is contemplated that that could be retired. It will have to be retired either through replacement by more debt money to be able to retire it, or it will have to be replaced with common stock issuing, in either of which case the effect would be, if it were done through further debt financing, while the effect of the preferred stock on the over-all return picture here would be lessened, you would still have at least 3¾ per cent to be earned on that money, or, if you replaced it with common stock, as we contend, 11 per cent is required.

The evidence in this case, I am confident, shows if you will take those instances, those companies which are putting out common stock issues, if you take the evidence in this record, and I think any place where it is available, the common stockholder is going to require more than 8.95 per cent. There is no question that the common stock has always required a higher return than anything else. There is no question about the fact that if you take an objective appraisal of it to come below the 11 per cent is just not going to give the common stockholder enough to warrant his attention.

I have touched upon this matter in the discussion of the rate of return. In 1945, the Mississippi River Fuel rate case, the first rate case, I have reason to remember, the [fol. 345] rate of return was reduced from 6½ to 6 per cent.

The statistics which I have just noted, when you are comparing the trends of natural gas financing with the trends in financing of other companies, particularly in this period since the time of the Mississippi River Fuel decision reducing the rate from 6½ to 6, we will see the great influx of heavy debt financing by the natural gas companies. Exhibit 19 in this case contains some very illustrative charts showing in columnar form just how that is building up, greatly ahead of other industries which have remained practically the same in their ratio of debt to equity financing.

It seems to me that there must be more encouragement given, there must be more thought given to allowing a company some encouragement for doing more equity financing. The fixed charges that result from heavy debt financing, the companies in the natural gas industry could well end up in somewhat the same position as the railroad industry did. We know what happened there because of the heavy debt financing.

Commissioner Smith: That wouldn't be so likely in this field where you have for the most part serial maturities with sinking funds which were lacking in the case of rail bonds?

Mr. White: The serial maturities and sinking funds' requirements still require a heavy drain upon the company's cash as it is earned, and you won't find——

Commissioner Smith: It also provides for the extinguishment of the debt.

Mr. White: That is true, but at the same time there is hardly any difference if you are going to have to spend too much money to meet the fixed cost of debt, including serial retirements over a 10-year period, or have to meet it at the end of that 10-year period, if you are going to be embarrassed every year, or every time you have to meet serial retirements.

Commissioner Smith: Suppose we were to agree with you [fol. 346] in the contention you have just made, could we require the conversion of debt into equity in the case of your company, absent new construction requiring a certificate?

Mr. White: I am sorry, sir, I didn't hear the last part.

Commissioner Smith: If we were to agree with your last contention, could we then require the conversion of your debt into equity securities, absent any certificate proceedings?

Mr. White: I don't think so, sir. The company will certainly be financing in the future, and so will others.

I might say the matter of greatest difference between the Staff and the company relates to Federal income taxes.

The sole issue I am going to discuss on Federal income taxes relates to the wellhead value for percentage depletion. I might say there is no question that the company estimated in the merger case and fully intended to get a five-cent wellhead value for percentage depletion purposes. We are certainly still firm in our purpose that that is exactly what we want to do.

The question is, since you are in a position now where, if it is found that we are charging too much, if there are excessive revenues, in other words, you will take actual cash away from us in the sense that you will not permit us to earn those excess revenues, there is a great question as to exactly what to do between now and the time the company can realize that depletion value if it ever does.

Now, this Commission has recognized in the merger case it has no control over this wellhead value. You stated in the majority opinion there, as I recall it, that you do not, and do not seek to control the Bureau of Internal Revenue in whatever it may decide is proper wellhead value for percentage depletion purposes.

I think there were even stronger opinions in the dissenting opinion. The majority said these things can't be forecast with exactness. We don't know what the wellhead value is going to be. We think that based on what would [fol. 347] appear to be reasonable, five cents seemed to be reasonable to us, then we don't know whether it is going to be four cents, it might be six cents. I hope it is. But the fact is that when you are in a rate proceeding, where the actual dollars will not be permitted to be earned by the company if you use a smaller income tax allowance because of a higher wellhead value, then I think we must pause before we decide what the company can do, and what can be asked of the company to do.

Now, your Honors may be interested in what the company has been doing. There hasn't been much time since this merger was accomplished, and if your Honors would care to do so, I can bring you up to date on what has been done, which is not in the record. I have the company treasurer here, and could put him on the witness stand if that would help complete the record, but there has been this. The company has asked the Bureau of Internal

Revenue for a ruling on what that wellhead value would be. Last week, in pursuance of that, there was a conference held with the man in charge of the natural resources section of the Bureau of Internal Revenue, and he stated at that time that while they appreciated this company's problems—we acquainted them with the rate situation, we said this is important to us, we have got to know it, it is important to the Power Commission, and is important to the public. He stated it is the settled policy of the Bureau of Internal Revenue not to issue rulings which are necessarily factual before the facts are available, and he said for the year 1952, those facts will not be available before the end of the year 1952.

The Chairman: That is the same explanation we got in the merger case back in 1950, almost identical.

Mr. White: I think that is correct, sir, yes.

The Chairman: So it is just a continuing process.

Mr. White: You are always behind on income tax.

The Chairman: You are always hopeful?

[fol. 348] Mr. White: Oh, yes, we certainly are, but we want to be hopeful with the money, too, and the thing here is we ask if there is some formula that we can make a more intelligent estimate on, because this is a matter of importance to us, he had no such formula to offer. We asked then if we could go to the field engineer and have him work on it in advance, and he said that can't be done, so the fact is until the actual year's taxes, the returns are filed and the Bureau of Internal Revenue knows what their determination is going to be, and it may have to go to court review, and we would certainly take it up there to try to get the wellhead value, this company can't know what it stands to lose on the actual wellhead value, and it may be more than a million dollars a year until that particular situation is met. Make no mistake about it, we want that higher wellhead value. It would be a mistake for us not to try to get it, but with the interposition of another agency, such as the Bureau of Internal Revenue, and with those very practical situations, I submit to the Commission it would be unrealistic to knock us down on federal income tax allowance until there was something definite to go on.

If it would please your Honors, I would be willing to give the reporter a copy of the letter with the request for ruling, if you would care to have it copied into the record.

· The Chairman: I don't believe we do.

Mr. White: On the matter of costing gasoline operations, as Mr. Goldberg has already pointed out, the staff used what purported to be a relative market value method. This, again, is a matter which was discussed at some length in the merger case, and I believe that the Commissioners are familiar with how it operates.

We contend that the relative market value method is, in itself, an unsound one, an economically unsound one. While we recognize it is popular in a good many places, particularly in refining of petroleum products, it is used there as an expedient because there seems to be no other way they can attem-t to cost things, it is one which by its own terms falls if the two joint products that you are trying [fol. 349] to price are of different stabilities.

We have here, for one thing, a stable natural gas price, and a gasoline price which is subject to very extreme fluctuations. Exhibit 31 in this case indicates they fluctuated in the last seven years more than 800 per cent.

Now, if you have enough variation, you will find that you are making money on the products today, doing exactly the same thing to it tomorrow, but losing money. That, to me, does not indicate an economically sound approach to costing joint products.

Commissioner Smith: Is your objection based on the view that you don't have true joint cost production when you can vary the relationships between the simultaneously produced products?

Mr. White: Do I understand you to mean, Commissioner, that you may control the output of each of the two products, that you can cut down on the production of gasoline?

Commissioner Smith: Yes.

Mr. White: I think there is definitely something to that, because they are not too necessarily joint products, you can say.

Commissioner Smith: That might be a theoretical objection to the use of the method.

Mr. White: As a matter of fact, under the terms of the operating agreements, the memorandum stipulations which preceded the merger, which is a part of the record in this case, the Colorado Interstate Gas Company, in cases of necessity, can by-pass the gasoline plant and shoot wet gas up until such point where as a practical operating matter it starts clogging its line and couldn't do it any more. What I mean is that it is not necessary to take that product out in every instance, but, as a matter of good operating practice, you must take it out or else you are not going to get the maximum efficiency out of your transportation [fol. 350] system. But that certainly is one of the factors that weighs very heavily upon it.

But I am saying this: Where you are assuming to price joint products, and assume for the moment there are joint products for this purpose, if you are attempting to price joint products on certain ratios, and it is recognized by all the authorities that those ratios can vary, as long as they sort of vary together, where you have one subject to wide fluctuation, and the other fairly steady, it is universally recognized that the method breaks down.

Now, in this case there was one piece of literature introduced in the record saying you can use some kind of averaging process, but over what period of time you are supposed to average, I don't know. That was the opinion of one writer upon the subject, but it seems to me it would be perfectly ridiculous to adopt a method of costing a product when you are doing the exact thing; today, you - making X dollars, tomorrow, XY dollars, and maybe the next day zero dollars. It just doesn't seem to be sensible.

Now, there is another factor we have to consider here, and tacitly it has been admitted by staff counsel that while the staff witness attempted to use, or purported to use a market value method, he did not use market value as to natural gas. Market value, he recognized to be the results of arm's length bargaining in a recent transaction, but the amount which he purported to use was a conglomerate mass of prices paid by Colorado Interstate Gas Company for gas, under contracts going back for 20 or more years, and by other companies in the field where he attempted to use this weighted average of the Texas Railroad Commission, and he admitted that so far as he knew there might even be distress sales in that particular conglomerate mass. Now, that does not represent market value.

They say we pay a Texas production tax, 4.33 cents, I believe is the exact figure, but the Texas production tax is based upon statutory definition as to what you do with it, [fol. 351] and it is not market value. Market value again is recognized, and the witness himself recognized, is the price paid after arm's length bargaining in recent transactions.

I say by his own admission he has taken us away entirely from the market value method of allocation, and in effect has made no allocation whatsoever.

Now, in speaking of the method used by the company, staff counsel—and if I misquote him, I am sure he will correct me, I don't mean to do so—stated that the company used only $55,000 as the part of the joint costs applicable to gasoline extraction. We are talking about joint costs at this point, where they are still joint, before the point of split off where you have indentifiable gasoline, and identifiable dry gas.

He fails to point out there are $93,000, in addition to the $55,000, of direct gasoline royalties, which are certainly charged, and charged by the study submitted by Colorado Interstate Gas Company, directly to the gasoline operations.

Now, one thing that struck me, he also sought support for using a five-cent value for natural gas because it is consistent with certain royalty payments, and for depletion purposes they used five cents, and then for the sake of consistency, we should use five cents for that purpose here. I am wondering why not, for the sake of consistency, we should not attribute five cents for rate making purposes also. That Panhandle gas comes out considerably less than five cents.

Commissioner Smith: You made no such claim in this case?

Mr. White: We did not, sir. I was just talking about consistency. I thought if the staff was going to be consistent up to one point they ought to carry it out the whole way.

Now, on the company method of costing these gasoline plant operations—I am sorry, I had intended to have a schematic drawing available for the Commission here, but [fol. 352] it did not develop. I have a few copies of an exhibit which was introduced in this case, if any of the Commissioners would care to see it, which is Exhibit 32, a schematic drawing of the Bivins gasoline plant.

A staff witness in this particular case did not attempt to make any study of the gasoline plant before he determined how he was going to cost the operations, he just used the application of the approach, or the relative market value method.

What I want to point out to the Commissioners is that this is a pretty complicated operation, at least it is complicated to me. Down in the lower left-hand corner, the wet gas which has not yet been stripped enters into the plant, passes through absorbers, where absorbing oil is brought in contact with it. This is a bank of three absorbers in this Bivins plant, in which case the clean oil absorbitive picks up the liquid fractions and carries it as enriched oil on over to another heading. Now, you will notice in the upper part of each one of these are dashed lines, we call joint gas and gasoline. This rich oil goes into reabsorbers which takes out still more, and is subject to various processes on down until again it is condensed or distilled, and finally you have a point of split off where this dashed line occurs.

Now, this represents the work of Mr. Otto Praeger, who is certainly a well qualified engineer. He has been dealing with this type of operation ever since he was discharged from the Army back in the early 20's. He went back in the Army during the course of the last war, and concerned himself with analogous problems. He is a man who redesigned this plant, and certainly is an expert to speak upon it.

It is his expert opinion, and he was able to be cross-examined at length upon it, and it was never shaken, that up to this split off point you have a joint operation. Now, the staff witness aside from a small amount of dehydration cost, never attributed one cent of cost to dry natural gas after the stream of wet gas entered the extraction plant, although he recognized that it was necessary to take [fol. 353] out natural gasoline in order to make the gas transportable.

Mr. Spurrier, I think, admitted he had been inside a gasoline plant. He did not attempt, as was brought out on his cross-examination, to equate into his study any part of the actual business of operating the plant.

Mr. Praeger, on the other hand, as I have pointed out as to this Bivins plant—he is an expert engineer, on these things overall, redesigned the plant, knows intimately what is in it, and on the basis of his expert judgment he indicates that this is what the facts are.

Subsequent to exploring what goes on in the gasoline plant, and there was a similar drawing of the Fourway plant, Mr. Praeger split in detail, on the basis of actual studies, what happens in that plant, the application of labor to this, the application of material, the split up of investment between these various things.

After having that, our expert witness on allocation, Mr. James O'Connor, allocated these joint costs, and he did it on a volumetric basis, and by volumetric, I mean here that he did it for several reasons, one is that it is the Commission's practice usually to allocate cost on a volumetric basis, not referring to classification of cost, necessarily, but once you have costs classified, and decide how to spread them, you do it on a number of cubic feet, either taking it on the peak period, if it is demand cost, or on an overall basis.

He felt it was proper to use a volumetric basis for that reason, and also for the reason that gasoline and gas are themselves inseparable products, except what incidental amounts may come out through drips, and so forth, until you reach a point of separation, so consequently it is the overall volume which determines the size of field gathering lines, and so forth, and I think there are sound reasons for using this method.

[fol. 354] It is on that basis that he comes up with the percentage overall of 2 per cent for the Fritch gasoline operation, 1 per cent for the others, and it seems that if that is the result of a sensible method, that is the method that should be used, so instead of having a $600,000 loss which the staff contends we have on this gasoline plant operation, we have shown a $600,000 profit under the facts of merger, where we give up 50 per cent of the Fourway and Bivins operation to the new hydrocarbon company, and where we give up 85 per cent of the net out of the Fritch gasoline plant operation.

Commissioner Draper: You are going to show that situation?

Mr. White: Our books will certainly show the situation. I don't know that there will be an allocation as we go along, but it will certainly show what money we make.

Commissioner Wimberly: There is a dispute as to the allocation.

Mr. White: Exactly. There is no fundamental dispute on the other. There is some variation between the two, but when you come down to the real nub of this problem, that isn't what matters, it is the method you use to allocate these costs.

Now, on depreciation, it is sought to reduce the company's claim by approximately $141,000, and I want to point out that the depreciation method used in the presentation of its case here by the company is the method reflected on the company's books, and that is the remaining life method of 25 years from January 1, 1948.

It may be that we are not claiming enough depreciation, because the Commission itself, 25 years from that date brings us out to December 31, 1972, and since this problem is tied into reserves, and the staff counsel himself has recognized it is so tied in, I would like to quote just one particularly appropriate part of the Commission's Opinion 209, which was issued in the merger case. There they were talking about the availability of gas in the future, the [fol. 355] the Commission was, and is response to the contentions made by the staff there would be available Canadian acreage in the future to the ratepayers. It says the figure advanced is based upon the assumption that gas will be available from the Canadian acreage from Colorado's Clayton-Denver line after 1972. We think that this assumption is unfounded, since the record shows the production from the Canadian acreage will probably have declined by 1972 to such a point that the volume of gas available therefrom will be sufficient only to supply the requirements of the Texas markets which retain their priority over those in the Rocky Mountain area.

Now, if depreciation policy is tied into the present reserves of the company, and this is what the Commission has to say about our present run-out period of 1972, it may well be that we should be claiming more.

In addition to that, the Commission has limited us in Docket G-1677, under a provision which presently is subject to rehearing, I recognize that, because the Commission has so acted, but it is because of the general present reserve situation of the company.

Now, the facilities that are involved here are tied into those reserves, and if there is some misgiving about our ability to produce gas for our main transmission system, even up to 1972, I submit the remaining life method, which we are using at present, to run out in 1972 is completely realistic, if perhaps not a little too much on the conservative side from the standpoint of the all annual accrual.

The Chairman: Are you going to be consistent and claim that lesser depreciation, then, that is the time for depreciation, and discard the five-cent depletion?

Mr. White: I am sorry.

The Chairman: Are you going to deny the one and accept the other, just to be consistent?

Mr. White: I am not denying the depreciation. All I am asking is that we take it per books. Our taxes, as a matter of fact, on our books, if that is what the Chairman [fol. 356] means, are being accrued at 3.17.

The Chairman: If you want to depreciate on a lesser period of time than the 1972 period, that is what you are seeking——

Mr. White: I am not seeking to do that. What I am pointing out here is perhaps what we are doing is not enough. We are not changing it. We are continuing the remaining life method, which would run us out in December 1972.

The Chairman: You are seeking a higher rate?

Mr. White: We are not seeking a higher rate than we are booking. We are saying we are entitled to a higher rate than the staff says we are entitled to.

Commissioner Smith: And is the difference simply between straight line and remaining life?

Mr. White: No, there is a service life of 25 years from 1952 used on new facilities, which would run those new facilities out in 1977. But, at the same time, the reserves would not last that long, except perhaps on some diminishing balance basis, if that might be the policy of the Commission, where you are not going to utilize facilities in the future after the expiration of the remaining life, or even a straight line period, as far as that is concerned, Commissioner Smith.

Now, on certain miscellaneous expenses—do I have 12 minutes, Mr. Chairman?

The Chairman: Yes, you have.

Mr. Smith: On the miscellaneous expenses, the subject has been thoroughly briefed by Colorado Interstate. Since we are here fixing rates for the future, I think it is the admonition of most authorities that regulatory commissions should allow what is necessary for the company to keep in business, and to maintain its usual methods of doing business, keep progress——

[fol. 357] Commissioner Draper: To what end?

Mr. White: I don't think for one moment that it helps the public to have a company that isn't going to be assured a return and expenses which it is expected it would meet.

Now, on regulatory commission expenses, I am going to skip over these except the one which has caused so much pain. On regulatory commission expenses, the fee of Mr. Houlihan, which the Commission staff sought to eliminate, they say is non-recurring, related to gasoline plant costing. I think this case is the best example that that is not a non-recurring item. It is a question that is apt to come up before this Commission very often. While Mr. Houlihan testified on that subject in the merger case, and the merger won't be reoccurring, certainly the question of costing joint products in these gasoline plant operations will recur in the future.

The regulatory commission expense relates, as Mr. Goldberg said, to review of these rate proceedings. We have cited cases, the opinion of Mr. Justice Cordoza, in which he recognizes that is a legitimate item of expense.

They have also sought to amortize it over five years, what they do allow over five years rather than three years. They do that on the basis that that is the Commission's policy. I state with its great influx of regulatory cases, this Commission is certainly conscious of how that has increased in the last several years, it is time that this period be shortened, because you are going to have running concurrently too doggone many amortization periods of regulatory commission expenses.

On salaries and wages, this additional estimated increase —and it has been the company's policy to grant increases, as the record shows, based on cost of living, and promotional increases, and so forth—we think are wholly justified by the record, and that has been analyzed in the briefs of Colorado Interstate Gas Company.

On the amount of gas royalties, I don't recall too much said by staff counsel, but there has been an adjustment of [fol. 358] gas royalties based upon the settlement of an actual claim, and on the settlement of lawsuits, and we arè attempting to get rid of all of those drainage suits, is what they are. They came up in the Panhandle field. They have been brought by the royalty owners of the former Canadian River Gas Company, and that was a matter of considerable concern during the progress of the merger, as the record in that case will indicate, so much so that it was a matter of specific question by staff counsel in that case to me as counsel for Colorado Interstate as to whether the merger would mean it would cost more on drainage cases if a merger took place than if it hadn't taken place, and I said no it wouldn't, but they have got to get rid of these drainage cases and keep our royalty owners satisfied on the basis of what happens in the future.

Now, there is involved the compensation to directors of the company, $5000, each, a year, and also the fees to be paid to the Chairman and other non-employee members of the executive committee.

I would like to point out that Exhibit 43 points out that Mr. Spencer, who was one of these selling stockholders, one of the lame ducks, so to speak, stated that he was not going to take his $15,000, and he didn't take his $5000. The amount is still payable to the other non-employee member of the executive committee. Whether he has been elected yet or not, I frankly don't know. I have been busy on other things, and there have been directors meetings within the past two weeks, and I am not sure whether the vacancy has been filled or not. But it will be filled.

The question centers around this fact: Should the ratepayer have to pay for that? That is the subject of the inquiry, as I see it. Now, the executive committee is a recognized adjunct of corporate management, and I don't think it is up to a regulatory commission until facts show it is an unreasonable expenditure, to override the discretion of management in deciding that this should be done.

[fol. 359] Now, this company is in effect a new company. It is actively seeking gas reserves, it has to have them, this Commission has stated it has to have them, and you can't do that sort of thing without paying for somebody who is willing to scout around and send people out and do whatever is necessary to get those reserves for the company. It seems to me——

The Chairman: Is that what the executive committee or directors are going to do, scout around for reserves?

Mr. White: They are already engaged in doing it, Mr. Commissioner.

Commissioner Smith: You mean they are authorizing it to be done?

Mr. White: And they, themselves, are doing a considerable amount of work on it.

Commissioner Smith: Can you enlighten me on this, perhaps this isn't a proper question, I don't know, about this so-called lame duck action, as to who was present, and what the voting was?

Mr. White: I don't know who was present, but I understand one director dissented, Mr. Parks, and he is a director. Public Service of Colorado owns only 15 per cent of the stock in that matter.

Commissioner Smith: And being a principal customer of the company.

Mr. White: And being a principal customer of the company. Whether that is what motivated him or not, I don't know.

Commissioner Smith: I think it would be very helpful for us to have that record here.

Mr. White: I think the implication was left in the record that the request was made for these minutes. I am sure it was not made. It wasn't made while I was conducting the hearings, and Mr. McGee was conducting them when I wasn't.

[fol. 360] The Chairman: Well, the record will speak for itself in that respect.

Mr. White: Of course it will.

Commissioner Wimberly: How many directors are there of Colorado Interstate?

Mr. White: Seven.

Commissioner Wimberly: What fees had they been getting prior to this action?

Mr. White: $100 a meeting, or $150 a meeting, I believe.

Commissioner Smith: Would you have any objection, Mr. White, to supplying that minute of this particular meeting, if the Commission should decide to reopen this record and request it?

Mr. White: I have no objection, sir.

Commissioner Smith: Can you speak for the company?

Mr. White: I think I can speak for the others. I have no objection to doing it, and if the Commission deems it advisable to inquire into it, from that standpoint I am personally willing, and will so recommend to the others.

That covers the miscellaneous general expenses. The employee's welfare and pension expenses I am going to have to submit on the brief, because I have one further word to say, and I do ask the Commission carefully to review the untouched questions as well as the others.

That is the end result of what is proposed here. We are used to talking in terms of end results these days, particularly since the Hope case in the Supreme Court of the United States. It was rather surprising to me, on getting the reply brief from the staff in this case in which they have their Table 2 as an appendix to the brief, to show that for total jurisdictional sales on the Denver system, in the Rocky Mountain area, excluding Natural Gas Pipe Line of America, the total average cost of the gas is 11.46 cents a thousand. This is after the gas has been produced, after it has been compressed, after it has been stripped, after it [fol. 361] has been transported, 350 miles in one case, 320 miles in another. The average cost, city gate price, 11.46 cents.

Now, this company—and it is in the record in this case—in its acquisition recently of gas supplies, has been paying roughly 10 cents a thousand at the wellhead. After that, the gas has to be transported at least 310 miles, and usually more because it also has to be gathered. Now, we are interested here in the overall reasonableness of this company's present rates. We aren't proposing a rate increase, this is a 5(a) case. Somebody is contending these rates of ours are unreasonable.

It seems to me that that in itself is one of the most telling things that you could cite, a company today being exhorted to get more gas reserves, and having to pay a price at the wellhead which is practically the same as the price shown at the city gate in the Rocky Mountain area in this case.

I think, Mr. Chairman, I will give you back the remaining minute.

Thank you very much, sir.

The Chairman: Mr. Goldberg?

You have about 17 minutes, I believe.

Rebuttal Argument of Jacob Goldberg

Mr. Goldberg: In referenct to the $4,000,000-figure Mr. White gave as to the difference between the cost of service allocated between the Staff and the company, I should like to observe that about half of that is made up of the taxes that result because of the difference in the cost of service in the beginning, and which of course merely means that they have got to make so much more revenue to pay for the taxes associated.

Actually, if you take the taxes away, there is only about a $2,000,000 difference.

[fol. 362] Now, Mr. White mentioned something about the Staff Exhibit 25 items, eliminating 6, and then there were another 18 we included. The 6 or 7 we eliminated on the rate of return study of Mr. Goubleman were financed before 1946. The table was made up from 1935 to date. Five or six had financed prior to 1946. Obviously the economic situation as to natural gas companies has changed radically since the termination of World War II, so he eliminated those.

Now, I don't understand the business of eliminating the Tennessee Gas Transmission stock issue. To me that is a natural gas company like any other natural gas company, and to try to anticipate what investors do about that stock as contrasted with what investors do about another stock is just hopeless. Every stock has a certain discount —there are certain aspects as to every stock as to what investors regard, and to arbitrarily say a whole issue of Tennessee Gas should be eliminated because of what Mr. Merrill says the investor is paying more for future earnings just doesn't make sense. They discount everything. They discount low earnings, they discount increased earnings, they discount the fact that the president is an old man, is aggressive, or whatever it is. Every stock has a discount factor, and to arbitrarily eliminate some issues just to come up with the issues you want just doesn't seem fair to me, and we took in everything, Tennessee, Texas Eastern, Texas Gas, all of them, because they are all gas companies, and they are all discounted for some reason or other.

Now, on this business of the depletion allowance for tax purposes, five cents against the 3.17, Mr. Commissioner Smith, I forgot to answer to your question about making a statement at one time, and changing it at another time, for important is this on the theory of estoppel. When you make a statement and get something, if you want to recast your statement or deny your statement, the least you ought to do with good conscience is give back what you took, and nobody yet has mentioned the fact for all this time in 1952 it is estimated the West-Pan Hydro Carbon [fol. 363] Company is going to get better than $1,400,000. That, Mr. White doesn't say, while they are claiming the

3.17 rate we are going to give back $1,400,000. No, they want to give up the $1,400,000, which would have been a credit to the cost of gas, but they say we may be harmed if we don't get the 3.17 rate. As a matter of fact, they are claiming more than the 3.17 rate, and they were claiming more than that at the time of the merger proceedings. I can't see how there is much merit in Mr. White's statement about the 3.17 rate.

Now, so far as costing the joint operations, Mr. White's statement reminded me of the oft-quoted Justice Brandeis, "It is must easier to criticize a formula than to derive one."

That is the situation here. There is no formula that is perfect. It is a joint operation, it is a question of judgment, and as a practical business outlook are you going to say that $55,000 out of better than $4,500,000 is a proper cost, or are you going to say that roughly 20 per cent is a proper cost? We maintain something under 20 per cent is the proper cost when you come to allocate the joint cost, and so far as the gasoline plant is concerned, while the chart is very interesting, and shows how a gasoline plant operates, the chart shows that the gasoline plant is for the gasoline operation, and if it is for the gasoline operations, it is the gasoline that *that* has to stand the expense.

Now, so far as the depreciation, and the company ending business in 1972, Mr. White has cleverly incorporated the opinion of the Commission pertaining to the Panhandle reserves as if it applies to all the reserves of Colorado Interstate. That isn't so. Our witnesses, when they estimated the 25-year service life of the new facilities, said not only are the Panhandle reserves assumed, if you want, to expire in 1972, but the Hugoton reserves are expected to continue to 1976, and also the Keyes Field, you are just attaching a new field, and he said there is more exploration going on. Mr. White said the executive committee is also hunting for new gas. Well, we take that into consideration in fixing the service life, so we maintain when you look at the whole thing, and just don't try to read in what the [fol. 364] Commission said about the Panhandle Field as illustrative of what happens to all the reserves of the company, you will come up with what the Staff said was the correct service life.

So far as Mr. Houlihan's testimony in the merger proceedings, testifying to an allocation for the gasoline operations, the short answer to that is this: We have allowed in this hearing all the rate case expenses that they have estimated before the Commission, including the testimony of Mr. Praeger, the testimony of Mr. O'Connor, all the people who testified on allocation, they have been paid. Houlihan was paid in the other case, and that is the end of it. I can't see why Mr. Houlihan's salary should be put back here in this proceeding.

In conclusion I should like to note that Mr. White read off the figure of the excess revenues based on the 6 per cent return. If you will look at Table 1 of the reply brief, the excess revenues based on the 5¾ per cent return is $3,554,250 of jurisdictional business.

Thank you.

The Chairman: We will take the matter under advisement.

Whereupon, at 12:05 p. m., the oral argument in the above-entitled matter was concluded.

[fol. 365–366]

EXHIBIT 1

A. E. WISKUP

SCHEDULE 3

Docket No. G–1115

Colorado Interstate Gas Company
Canadian River Gas Company

Pro Forma Statement Reflecting the Staff's Computation of Federal Income Tax Giving Effect to the Merger
For the Year Ended June 30, 1951

	Reference	Total	Eliminations for Tax Computation Purposes	Total for Tax Computation Purposes
Return at 6%	Sch. 1	$2,560,816.42	$ —	$2,560,816.42
Add: Other Income				
Revenue from Lease of Other Physical Property	Sch. 7	31.20	—	31.20
Interest Revenues	Sch. 7	284.03	—	284.03
Miscellaneous Nonoperating Revenues	Sch. 7	669.33	—	669.33
Nonoperating Revenue Deductions	Sch. 7	(1,336.63)	—	(1,336.63)
Total Other Income		(352.07)	—	(352.07)
Less: Income Deductions				
Interest on Long-Term Debt	Sch. 7	568,333.32	(432.21)	567,901.11
Interest Charged to Acct. 142.2—Other Preliminary Survey and Investigation Charges		60,000.00	—	60,000.00
Amortization of Debt Discount and Expense	Sch. 7	3,488.25	—	3,488.25
Amortization of Premium on Debt—Cr.	Sch. 7	(999.96)	—	(999.96)
Other Interest Charges	Sch. 7	79.36	—	79.36
Interest Charged Construction—Cr.	Sch. 7	(30,432.21)	30,432.21	—
Miscellaneous Income Deductions				
Staff Adjustments	Sch. 7	78,686.69	(78,686.69)	—
Other—Contributions, etc.	Sch. 7	13,385.84	129.11	13,514.95
Total Income Deductions		692,541.29	(48,557.58)	643,983.71
Add: Depreciation and Depletion for Rate Case Purposes	Sch. 1	1,831,495.57	—	1,831,495.57

Exhibit 1

A. E. WISKUP

Schedule 3

Docket No. G-1115

Colorado Interstate Gas Company
Canadian River Gas Company

Pro Forma Statement Reflecting the Staff's Computation of Federal Income Tax Giving Effect to the Merger
For the Year Ended June 30, 1951

	Reference	Total	Eliminations for Tax Computation Purposes	Total for Tax Computation Purposes
Less: Tax Return Deductions				
Depreciation for Tax Purposes—Colorado Interstate Gas Company Properties	Sch. 3a	1,329,622.18	—	1,329,622.18
Depreciation for Tax Purposes—Canadian River Gas Company Properties	Sch. 3b	355,329.13	—	355,329.13
Depletion for Tax Purposes	Sch. 3c	931,027.13	—	931,027.13
Intangible Productive Well Drilling Costs		1,056,049.48	—	1,056,049.48
Property Removal Costs		22,775.63	—	22,775.63
Total Tax Return Deductions		3,694,803.55	—	3,694,803.55
Net Taxable Income After Tax		$ 4,615.08	($48,557.58)	53,172.66
Less: Credit for Dividends Paid on Preferred Stock (30% x $120,000)				36,000.00
Tax Base				$ 17,172.66
Normal Tax at 25% (25/75)				$ 5,724.22

Note: No surtax to be computed as surtax applies to income over $25,000.

(Here follows Schedule 8, folios 367-382)

[fol. 367–382]

Docket No. C–1115

A. E. WISKUP

Schedule 8

Colorado Interstate Gas Company
Canadian River Gas Company

Pro Forma Balance Sheets Giving Effect to the Merger
as at June 30, 1950 and 1951

Assets and Other Debits	As of June 30,	
	1950	1951
Utility Plant		
Gas Plant in Service	$53,973,577.25	$56,780,715.30
Construction Work in Progress	950,359.18	1,317,289.00
Gas Plant Held for Future Use	46,648.30	46,648.30
Total Utility Plant	54,970,584.73	58,144,652.60
Investment and Fund Accounts		
Other Physical Property	13,219.07	2,011.55
Current and Accrued Assets		
Cash	2,217,709.13	3,702,029.92
Special Deposits	610,483.37	6,083.28
Working Funds	75.00	75.00
Notes Receivable	914.77	452.25
Accounts Receivable	1,097,265.51	1,285,318.83
Materials and Supplies	1,657,714.51	1,320,459.81
Prepayments	62,116.64	57,511.71
Total Current and Accrued Assets	5,646,278.93	6,371,930.80
Deferred Debits	58,337.00	179,896.19
Total Assets and Other Debits	$60,688,419.73	$64,698,491.14

Liabilities and Other Credits	As of June 30,	
	1950	1951
Capital Stock		
Common	$ 2,352,942.17	$ 2,352,942.17
Preferred	2,000,000.00	2,000,000.00
Total Capital Stock	4,352,942.17	4,352,942.17
Long-Term Debt	19,600,000.00	18,800,000.00
Current and Accrued Liabilities		
Accounts Payable	1,075,353.58	1,217,590.85
Taxes Accrued	2,731,838.73	3,883,456.35
Interest Accrued	111,666.69	109,000.01
Other Current and Accrued Liabilities	9,513.18	99,136.45
Total Current and Accrued Liabilities	3,928,372.18	5,309,183.66
Deferred Credits	18,749.25	17,749.29
Reserves for Depreciation and Depletion	13,893,950.12	15,747,865.70
Employees Death Benefit Reserve	—	3,500.00
Contributions in Aid of Construction	137,342.27	139,302.44
Earned Surplus	18,757,063.74	20,327,947.88
Total Liabilities and Other Credits	$60,688,419.73	$64,698,491.14

Note: Above represent balance sheets per books combined with intercompany receivables and payables eliminated.

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Exhibit 11

Natural Gas Common Stocks Offered to the Public During the Period 1935 to Date
With Earnings-Offering Price Ratio and Cost of Financing

Line No.	Name of Issue	Approximate Offering Date	No. of Shares Offered	Price to Public		Price Per Share to Underwriter	Line No.
				Total	Per Share		
	(a)	(b)	(c)	(d)	(e)	(f)	
1	Kansas Pipe Line & Gas Co., (1), $5.00 Par (16)	Aug. 1936	110,000	$ 550,000	$ 5.00	$ 4.82	1
2	Northern Natural Gas Co., $20.00 Par (6)	Sept. 1941	355,250	11,368,000	32.00	29.65	2
3	Kansas-Nebraska Natural Gas Co., Inc., $5.00 Par (16)	Dec. 1941	48,468	315,042	6.50	5.49	3
4	Kansas-Nebraska Natural Gas Co., Inc., $5.00 Par (16)	May 1944	17,765 (9)	124,355	7.00	6.22 (9)	4
5	Montana-Dakota Utilities Co., $5.00 Par (16)	Oct. 1945	223,352	2,568,544	11.50	10.55	5
6	Tennessee Gas Transmission Co., $5.00 Par (4)	Jan. 1946	812,100 (4)	9,745,200	12.00	11.10	6
7	Tennessee Gas Transmission Co., $5.00 Par (5)	Apr. 1946	484,444 (5)	9,567,769	19.75	18.65	7
8	El Paso Natural Gas Co., $3.00 Par (16)	July 1946	2,697 (12)	113,274	42.00	41.62	8
9	Texas Eastern Transmission Corp. No Par (13)	Nov. 1947	3,550,000 (13)	33,725,000	9.50	8.50	9
10	Northern Natural Gas Co., $10 Par (14)	Dec. 1947	710,500 (14)	19,183,500	27.00	25.80	10
11	Washington Gas Light Co., No Par (17)	Jan. 1948	13,790 (17)	279,248	20.25	19.25	11
12	Montana-Dakota Utilities Co., $5.00 Par (15)	June 1948	150,000	1,875,000	12.50	11.60	12
13	Tennessee Gas Transmission Co., $5.00 Par (19)	Sept. 1948	400,000	12,100,000	30.25	28.60	13
14	Mississippi River Fuel Corp. $10 Par (18)	Jan. 1949	144,200 (18)	4,326,000	30.00	28.00	14
15	Mississippi River Fuel Corp., $10 Par (20)	Apr. 1949	435,282 (20)	13,058,460	30.00	(20)	15
16	Texas Gas Transmission Corp., $5 Par (21)	Aug. 1949	218,625	2,623,500	12.00	11.10	16
17	Tennessee Gas Transmission Co., $5 Par (22)	Sept. 1949	400,000	12,100,000	30.25	28.80	17
18	Equitable Gas Co., $8.50 Par (23)	Mar. 1950	2,000,000	48,500,000	24.25	22.88	18
19	Texas Gas Transmission Corp., $5 Par (24)	Mar. 1950	193,306	3,527,835	18.25	17.13	19
20	Tennessee Gas Transmission Co., $5 Par (2)	Oct. 1950	250,000	7,500,000	30.00	28.55	20
21	Washington Gas Light Company, No Par (25)	Apr. 1951	20,596	507,279	24.63	(3)	21
22	Tennessee Gas Transmission Co., $5 Par (26)	Apr. 1951	400,000	9,600,000	24.00	22.75	22
23	Midsouth Gas Company, $1.00 Par (27)	July 1951	100,000	675,000	6.75	(3)	23

[fols. 385-386]

Natural Gas Common Stocks Offered to the Public During the Period 1935 to Date With Earnings—Offering Price Ratio and Cost of Financing

			Cost of Flotation per share		Earnings per Share			
Line No.	Net Proceeds Per Share to Company	Expenses to Issuing Co. Incidental To Flotation	Amount (e−g)	Percent of Price to Public (i÷e)	12 Mos. Ended	Amount	Earnings—Offering Price Ratio	Line No.
	(g)	(h)	(i)	(j)	(k)	(l)	(m)	
1	$4.73	$0.09	$0.27	5.4%	Mar. 31, 1937	$0.71 (8)	14.2%	1
2	(3)	(3)	(3)	(3)	Dec. 31, 1940	3.65 (6)	11.4	2
3	5.41	0.08	1.09	16.8	Nov. 30, 1941	0.54 (11)	8.3	3
4	6.15 (9)	0.07 (9)	0.85 (9)	12.1 (9)	Dec. 31, 1943	0.82 (10)	11.7	4
5	10.47	0.08	1.03	8.9	Dec. 31, 1944	0.60 (7)	5.2	5
6	11.01	0.09	0.99	8.3	Nov. 30, 1945	2.07 (4)	17.3	6
7	18.62	0.03	1.13	5.7	Dec. 31, 1945	2.46 (5)	12.5	7
8	41.11	0.52	0.89	2.1	May 31, 1946	3.39 (12)	8.1	8
9	8.45	0.05	1.05	11.1	(13)	(13)	(13)	9
10	25.70	0.10	1.30	4.8	Sept. 30, 1947	3.43 (14)	12.7	10
11	18.71	0.54	1.54	7.1	Nov. 30, 1947	1.45 (17)	7.1	11
12	11.44	0.16	1.06	8.5	Dec. 31, 1947	1.39 (15)	11.1	12
13	28.41	0.19	1.84	6.4	Dec. 31, 1947	2.40 (19)	7.9	13
14	27.51	0.49	2.49	8.3	Dec. 31, 1947	2.46 (18)	8.3	14
15	(20)	(20)	(20)	(20)	Dec. 31, 1948	3.49	11.6	15
16	10.92	0.18	1.08	9.0	May 31, 1949	0.75	6.3	16
17	28.68	0.12	1.57	5.2	July 31, 1949	2.24	7.4	17
18	22.83	0.05	1.42	5.9	Dec. 31, 1949	1.84	7.6	18
19	16.72	0.41	1.53	8.4	Dec. 31, 1949	0.81	4.4	19
20	28.31	0.24	1.69	5.6	Aug. 31, 1950	1.84	6.1	20
21	(3)	(3)	(3)	(3)	Dec. 31, 1950	2.84	11.5	21
22	22.64	0.11	1.36	5.7	Dec. 31, 1950	1.73	7.2	22
23	(3)	(3)	(3)	(3)	Dec. 31, 1950	0.47	7.0	23

[fols. 387-388]

EXHIBIT 11
Page 13

Earnings—Price Ratios of Outstanding Common Stocks of Seven Natural Gas Companies
January 1940 To Date

	1940	1941	1942	1943	1944	1945	1946	1947	1948	1949	1950	1951	1952
Jan.	10.5%	11.8%	13.7%	12.4%	10.4%	9.4%	6.6%	7.6%	9.4%	8.9%	6.8%	7.4%	
Feb.	9.8	12.3	13.3	11.8	10.3	9.1	7.2	7.8	9.9	9.2	6.8	7.3	
Mar.	10.0	12.4	15.0	11.6	10.6	9.4	6.8	8.3	9.2	8.8	6.7	7.3	
Apr.	10.2	13.6	16.1	11.3	10.9	9.1	6.7	8.4	8.7	9.1	6.9	7.4	
May	12.9	13.1	16.2	10.5	10.8	9.3	6.8	9.2	8.5	9.1	6.7	7.6	
June	11.3	12.7	16.3	10.6	10.8	8.5	6.9	9.1	8.4	9.3	7.2	7.6	
July	13.3	11.5	15.7	10.3	10.7	8.9	7.1	8.9	8.5	9.1	8.5	6.7	
Aug.	13.3	11.5	15.1	10.3	10.3	8.8	7.6	9.4	8.4	8.5	8.0	6.6	
Sept.	13.0	11.5	14.8	10.1	10.4	8.7	8.1	9.2	8.7	8.3	7.7		
Oct.	12.3	11.9	14.6	10.1	10.0	8.2	8.0	8.9	8.6	7.6	7.9		
Nov.	11.9	14.2	13.8	10.6	10.3	7.5	8.1	9.0	9.8	7.3	8.0		
Dec.	11.9	15.6	13.5	10.6	10.0	7.4	7.9	9.0	9.3	6.8	7.9		
Straight Average	11.7%	12.7%	14.8%	10.9%	10.5%	8.7%	7.3%	8.7%	9.0%	8.5%	7.4%		

Note: The above data are based on the closing market quotations at the end of the month and the latest available earnings for a twelve months period immediately preceding the particular month. Also, the earnings-price ratios are based on weighted figures.

Source of Data: Moody's Public Utility Cumulative Index, Standard & Poor's Stock Guide and Bank and Quotation Record.

[fols. 389-392]

Exhibit 11
Page 13a

Earnings-Price Ratios and Yields on 7 Natural Gas Pipe Line Company Common Stocks
July 31, 1951

	No. Shares	Market Price		Earnings					
Company	Outstanding (000)	7/31/51	Total (000)	12 Mos. Ended	Per Share	Total (000)	E.P.R.	Div. Rate	Yield
(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)
Consolidated Gas Utilities Corp.......	886	$11.63	$10,304	4/30/51	$1.52	$1,347	13.1	$0.75	6.4%
El Paso Natural Gas Company.......	2,701	29.88	80,706	5/31/51	2.88	7,779	9.6	1.60	5.4
Lone Star Gas Company............	5,499	27.63	151,937	6/30/51	1.89	10,393	6.8	1.40	5.1
Mountain Fuel Supply Company.....	1,990	17.00	33,830	12/31/50	0.99	1,970	5.8	0.60	3.5
Northern Natural Gas Company.....	2,741	38.00	104,158	3/31/51	2.09	5,729	5.5	1.80	4.7
Panhandle Eastern Pipe Line Co......	3,240	54.50	176,580	3/31/51	2.73	8,845	5.0	2.00	3.7
Southern Natural Gas Co............	1,711	45.38	77,645	3/31/51	3.63	6,211	8.0	2.50	5.5
Totals....................			$635,160			$42,274	6.7%		

Source of Data: Standard & Poor's Stock Guide, August, 1951.

[fols. 393-404]

EXHIBIT 13

SCHEDULE B

Docket No. G–1115

Sheet 1 of 3

Colorado Interstate Gas Company
Canadian River Gas Company

Return at Assumed Rate of 6%
Based on Estimates of Colorado Interstate Gas Company
In Application In Docket G–1677, as Adjusted Years 1951, 1952 and 1953

	Source	1951	1952	1953
Colorado Interstate Gas Co.	Sch. B, Sheet 2	$2,050,022	$2,246,679	$2,213,738
Canadian River Gas Co.	Sch. B, Sheet 3	999,875	1,299,020	1,367,339
Total		$3,049,897	$3,545,699	$3,581,077

[fols. 405–410]

Exhibit 18

Docket No. G–1115

Colorado Interstate Gas Company

Allocation—Excess Earnings

Particulars	Excess Earnings Based on Company Estimates in Docket No. G–1677 As Adjusted			Line
	1951	1952	1953	
Sales to Other Utilities				
Production System—Firm				
Amarillo Oil Co.	$ (106,000)	$ (127,453)	$ (77,834)	1
Transmission System—Firm				
P–1	162,841	195,798	119,572	2
G–1	1,508,967	1,814,360	1,108,010	3
Clayton Gas Co.	1,728	2,078	1,269	4
Dalhart Gas Co.	2,304	2,770	1,692	5
Total Firm	1,675,840	2,015,006	1,230,543	6
Transmission System—Interruptible				
I–1	47,815	57,492	35,110	7
I–2	91,598	110,136	67,259	8
Clayton Gas Co. (Ind.)	(576)	(693)	(423)	9
Dalhart Gas Co. (Ind.)	(1,920)	(2,309)	(1,410)	10
Total Interruptible	136,917	164,626	100,536	11
Total Transmission System	1,812,757	2,179,632	1,331,079	12
Leased Transmission System				
Nat. Gas P.L. Co. of America	(159,384)	(191,641)	(117,033)	13
Total Sales to Other Utilities	$1,547,373	$1,860,538	$1,136,212	14
Direct Sales				
Production System				
Firm	$ 12,482	$ 15,008	$ 9,165	15
Interruptible	768	924	564	16
Total Production System	13,250	15,932	9,729	17
Transmission System				
Firm	9,025	10,852	6,627	18
Interruptible	350,646	421,611	257,474	19
Total Transmission System	$ 359,671	$ 432,463	$ 264,101	20
Total Direct Sales	$ 372,921	$ 448,395	$ 273,830	21
Total System Sales	$1,920,294	$2,308,933	$1,410,042	22
Total Jurisdictional	$1,652,989	$1,987,530	$1,213,764	23

Note: Jurisdictional Sales = Line 14—Line 1—Line 5—Line 10

( ) Indicates Red Figures

[fols. 411–416]

Exhibit 21

Schedule No. 1

Canadian River Gas Company
Colorado Interstate Gas Company

Estimated Cost of Service and Excess Revenues
Year 1952

Line No.		Reference (1)	Total (2)
1	Gas Service Revenues	Sch. 3	$17,962,532
2	Cost of Service		
3	Operating Revenue Deductions		
4	Gasoline Net Revenues	Sch. 5	(598,218)
5	Other Gas Revenues—Rent	Sch. 4	(37,500)
6	Production Expenses		
7	Gas Purchased	Sch. 6	2,082,000
8	Gas Used in Operations	Sch. 6	(270,300)
9	Other Production Expenses	Sch. 7	1,907,669
10	Transmission Expenses		
11	Operation & Maintenance	Sch. 7	2,385,700
12	Rental of Leased Facilities	Sch. 7	443,000
13	Distribution Expenses	Sch. 7	163,166
14	Administrative & General	Sch. 7	1,255,126
15	Sub-Total		7,330,643
16	Depreciation	Sch. 8	2,678,673
17	Depletion	Sch. 9	57,688
18	Taxes—Federal Income	Sch. 10	2,245,479
19	—State Income	Sch. 11	63,765
20	—Other	Sch. 12	1,835,229
21	Total Operating Rev. Ded.		14,211,477
22	Return at 6.5%	Exh. 20	3,704,545
23	Total Cost of Service		$17,916,022
24	Excess Revenues		$ 46,510

(Here follows Exhibit 26 folios 417-424)

[fols. 417–424]

Docket No. G–1115

EXHIBIT 26

SCHEDULE A–1

Colorado Interstate Gas Company (Merged)
Estimated Excess Revenues and Cost of Service
Based on Estimates of Colorado Interstate Gas Company in Docket G–1115
As Adjusted
Year 1952

Line No.		Per Schedule No. 1 of Exhibit 21	Staff Reclassifications Per Schedule A–2		As Reclassified	Staff Adjustments		As Adjusted
			Reference	Amount		Reference	Amount	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1	Gas Service Revenues	$17,962,532			$17,962,532			$17,962,532
	Cost of Service							
2	Gas Purchased	$ 2,082,000	Entry No. 1	($2,082,000)	$ —	—	$ —	$ —
3	Operating Expenses	—	Entry No. 1 Entry No. 2	7,966,361) 505,802)	— 8,472,163	— Sch. A–3	— (54,456)	— 8,417,707
4	Depreciation	2,678,673	—	—	2,678,673	Sch. A–4	(140,934)	2,537,739
5	Depletion	57,688	—	—	57,688	—	—	57,688
	Taxes:							
6	Federal Income	2,245,479	—	—	2,245,479	Sch. A–5	(2,118,252)	127,227
7	State Income	63,765	—	—	63,765	Sch. A–5	(59,948)	3,817
8	Other	1,835,229	—	—	1,835,229	—	—	1,835,229
9	Return	3,704,545	—	—	3,704,545	Sch. A–7	(274,666)	3,429,879
10	Other Gas Revenues	(37,500)	—	—	(37,500)	—	—	(37,500)
11	Gasoline Revenues	—	Entry No. 2	(1,104,020)	(1,104,020)	—	—	(1,104,020)
12	Loss on Gasoline Operations Not Chargeable to Ratepayers	—	—	—	—	Sch. A–8	(601,260)	(601,260)
13	Gasoline Net Revenues	(598,218)	Entry No. 2	598,218	—	—	—	—
14	Gas Used in Operations	(270,300)	Entry No. 1	270,300	—	—	—	—
15	Other Production Expenses	1,907,669	Entry No. 1	(1,907,669)	—	—	—	—
16	Transmission Expenses—Operation and Maintenance	2,385,700	Entry No. 1	(2,385,700)	—	—	—	—
17	Transmission Expenses—Rental of Leased Facilities	443,000	Entry No. 1	(443,000)	—	—	—	—
18	Distribution Expenses	163,166	Entry No. 1	(163,166)	—	—	—	—
19	Administrative and General	1,255,126	Entry No. 1	(1,255,126)	—	—	—	—
20	Total Cost of Service	$17,916,022		$ —	$17,916,022		($3,249,516)	$14,666,506
21	Excess Revenues	$ 46,510			$ 46,510			$ 3,296,026

( ) Denote red figures.

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[fols. 425–436]

Exhibit 26

Schedule A–7

Docket No. G–1115

Colorado Interstate Gas Company (Merged)

Staff Adjustment of Return
Year 1952

		Adjustment of Return
Decrease in return due to substitution of a 6% rate for the 6½% rate:		
Return, per Sch. 1 of Exh. 20 (Rate base of $56,993,006 times 6½%)	$3,704,545	
Above return using a 6% rate ($56,993,006 times 6%)	3,419,580	$ 284,965
Decrease in return due to staff adjustment of Regulatory Commission Expense (Per Sch. A–3):		
Adjustment of $54,456 times 1/8 equals $6,807 working capital times 6%		408
Total Decreases		285,373
Increase in return due to staff adjustment of depreciation provision:		
Decrease of $140,934 in provision (Per Sch. A–4) is reflected in the reserve for depreciation ending balance on Sch. A–19, divided by 2 the decrease gives $70,467 less average reserve for depreciation and higher rate base in Sch. A–15 than in Sch. 1 of Exh. 20. The increase in return is $70,467 times 6%		4,228
Increase in return due to use of year 1952 average Gas Plant Held for Future Use:		
Average Gas Plant Held for Future Use for 1952 per Sch. A–17	269,213	
Two year average used in Sch. 3, Exh. 20	161,232	
Increase in rate base	107,981	
Increase in return ($107,981 times 6%)		6,479
Total Increases		10,707
Staff Adjustment (Net Decrease)		$ 274,666

Here follows Exhibit 28, folios 437-440 and Exhibit 30, folios 441-548)

[fols. 437–440]

Exhibit 28

Table No. II

Docket No. G–1115

Colorado Interstate Gas Company

Summary—Allocation of Cost of Service

Total System
Year 1952—Estimated

Line	Customer and Class of Sale	Annual Volume Mcf [1]	Revenue	Cost of Service				Excess Revenue Over Cost of Service	Average Revenue Cents/Mcf [1]	Average Cost Cents/Mcf [1]
				Production	Transmission	Distribution [2]	Total			
	(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)
	Transmission System									
	Sales to Other Utilities									
	Jurisdictional									
1	G–1 Rate Schedule	66,179,300	$10,747,115	$2,424,316	$5,264,683	$131,894	$7,820,893	$2,926,222	16.24	11.82
2	G–2 Rate Schedule	264,000	45,288	9,673	22,268	2,997	34,938	10,350	17.15	13.23
3	P–1 Rate Schedule	16,482,000	2,187,885	603,768	1,239,682	20,696	1,864,146	323,739	13.27	11.31
4	I–1 Rate Schedule	2,953,700	369,213	108,196	193,345	8,917	310,458	58,755	12.50	10.51
5	I–2 Rate Schedule	([3])	([3])	—	—	—	—	—	—	—
6	Clayton Gas Company	240,000	35,160	8,768	24,481	2,975	36,224	(1,064)	14.65	15.09
7	Total Jurisdictional	86,119,000	13,384,661	3,154,721	6,744,459	167,479	10,066,659	3,318,002	15.54	11.69
	Non-Jurisdictional									
8	Dalhart Gas Company	535,000	72,225	19,603	51,647	6,000	77,250	(5,025)	13.50	14.44
9	Total Sales to Other Utilities	86,654,000	13,456,886	3,174,324	6,796,106	173,479	10,143,909	3,312,977	15.53	11.71
10	Direct Sales—Non-Jurisdictional	15,958,000	2,135,721	584,565	1,038,397	35,357	1,658,319	477,402	13.38	10.39
11	Total Transmission System Sales	102,612,000	15,592,607	3,758,889	7,834,503	208,836	11,802,228	3,790,379	15.20	11.50
	Leased Transmission System									
	Jurisdictional									
12	Natural Gas Pipeline Co. of America	48,051,000	1,945,400	1,760,213	443,000	52,544	2,255,757	(310,357)	4.05	4.49
	Field System									
	Non-Jurisdictional									
	Amarillo Oil Company									
	Contract "B"									
13	Well Mouth	6,323,000	133,785	179,309		15,465	194,774	(60,989)	2.12	2.08
14	Gathering	7,682,000	181,745	322,753		12,862	335,615	(153,870)	2.37	4.37
15	Total Contract "B"	14,005,000	315,530	502,062		28,327	530,389	(214,859)	2.25	3.79
16	Contract "C"—Gathering	112,000	9,005	4,684		2,857	7,541	1,464	8.04	6.73
17	Total Amarillo Oil Co.	14,117,000	324,535	506,746		31,184	537,930	(213,395)	2.30	3.81
18	Other Field Sales	1,355,000	99,990	56,951		13,640	70,591	29,399	7.38	5.21
19	Total Field System Sales	15,472,000	424,525	563,697		44,824	608,521	(183,996)	2.74	3.93
20	Total All Sales	166,135,000	$17,962,532	$6,082,799	$8,277,503	$306,204	$14,666,506	$3,296,026	10.81	8.83
	Recapitulation									
21	Jurisdictional	134,170,000	15,330,061	4,914,934	7,187,459	220,023	12,322,416	3,007,645	11.43	9.18
22	Non-Jurisdictional	31,965,000	2,632,471	1,167,865	1,090,044	86,181	2,344,090	288,381	8.24	7.33
23	Total System Sales	166,135,000	$17,962,532	$6,082,799	$8,277,503	$306,204	$14,666,506	$3,296,026	10.81	8.83

[1] Pressure Base 14.65 p.s.i.a.
[2] Distribution Costs Allocated 50% Commodity—50% Customer
[3] The small amount of I–2 gas has been included under G–1
( ) Indicates Negative Figure

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[fol. 441–548]

Exhibit 30

Schedule No. 1

Colorado Interstate Gas Company

Estimated Cost of Service and Deficiency in Revenues as Estimated for Year 1952

			Production															
				Panhandle Field						Hugoton and Loveland Fields					Transmission			
Line No.		Total (1)	Total Production (2)	Well Mouth (3)	Gathering (4)	Fourway Dehydration (5)	Fourway Gasoline (6)	Bivins Gasoline (7)	Fritch Gasoline (8)	Gas Purchased (9)	Well Mouth (10)	Gathering (11)	Lakin Dehydration (12)	Lakin Gasoline (13)	Total Transmission (14)	Bivins Dehydration (15)	Other (16)	Total Distribution (17)
1	Gas Service Revenues (Sch. 3)	$17,962,532																
2	Cost of Service																	
3	Operating Revenue Deductions																	
4	Gasoline Net Revenues (Sch. 5)	(583,324)	($ 583,324)	$	$	$	($109,978)	($228,319)	($39,920)	$	$	$	$	($205,107)	$	$	$	$
5	Other Gas Revenues—Rent (Sch. 4)	(37,500)	(3,450)				(1,250)	(2,200)							(34,050)		(34,050)	
6	Production Expenses																	
7	Gas Purchased (Sch. 6)	2,082,000	2,082,000							2,082,000								
8	Gas Used in Operations (Sch. 6)	(270,300)	(270,300)	(167,100)							(103,200)							
9	Other Production Expenses (Sch. 7)	2,018,250	2,018,250	1,642,304	100,243	5,058					146,427	118,903	5,315					
10	Transmission Expenses																	
11	Operation and Maintenance (Sch. 7)	2,507,120													2,507,120	27,840	2,479,280	
12	Rental of Leased Facilities (Sch. 7)	443,000													443,000		443,000	
13	Distribution Expenses (Sch. 7)	173,303																173,303
14	Administrative and General (Sch. 7)	1,808,611	604,888	285,475	100,735	6,182	34,184	10,663			6,001	137,647	6,182	17,819	1,189,722	5,273	1,184,449	14,001
15	Sub-Total	8,141,160	3,848,064	1,760,679	200,978	11,240	(77,044)	(219,856)	(39,920)	2,082,000	49,228	256,550	11,497	(187,288)	4,105,792	33,113	4,072,679	187,304
16	Depreciation (Sch. 8)	2,678,673	903,868	375,286	153,373	10,200	57,707	26,440			9,936	229,716	10,384	30,826	1,755,598	9,663	1,745,935	19,207
17	Depletion (Sch. 9)	57,688	57,688	57,688														
18	Taxes—Federal Income (Sch. 10)	2,306,808	293,595	(312,211)	170,165	11,383	64,373	29,739			25,717	257,957	11,720	34,752	1,989,119	11,013	1,978,106	24,094
19	—State Income (Sch. 11)	63,765													63,765		63,765	
20	—Other (Sch. 12)	1,835,229	1,174,095	420,000	628,659	3,397	18,775	11,185			3,295	75,601	3,396	9,787	653,444	2,896	650,548	7,690
21	Total Operating Revenue Deductions	15,083,323	6,277,310	2,301,442	1,153,175	36,220	63,811	(152,492)	(39,920)	2,082,000	88,176	819,824	36,997	(111,923)	8,567,718	56,685	8,511,033	238,295
22	Return at 6.5%	3,718,028	1,276,183	539,286	206,806	13,885	78,329	36,158			31,378	313,771	14,186	42,384	2,412,940	13,363	2,399,577	28,905
23	Total Cost of Service	$18,801,351	$7,553,493	$2,840,728	$1,359,981	$50,105	$142,140	($116,334)	($39,920)	$2,082,000	$119,554	$1,133,595	$51,183	($ 69,539)	$10,980,658	$70,048	$10,910,610	$267,200
24	Deficiency	($ 838,819)																

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[fol. 549] Before the Federal Power Commission
Items by Reference

Item A

March 16, 1951.

United States of America, Federal Power Commission. In the Matter of Colorado Interstate Gas Company and Canadian River Gas Company. Docket No. G-1326.

Before Commissioners: Mon C. Wallgren, Chairman; Thomas C. Buchanan, Claude L. Draper, Nelson Lee Smith and Harrington Wimberly.

Opinion No. 209

On March 1, 1951, we authorized Colorado Interstate Gas Company (Colorado) to acquire by merger and to operate all of the properties of Canadian River Gas Company (Canadian) which are subject to our jurisdiction. This we did by order without opinion, since we thought that preparation of an opinion would unduly delay the beginning of construction of the pipeline facilities proposed, contingent upon our approval of the merger, to be built by Colorado, and which are sorely needed to augument the supply of natural gas available to Denver, Cheyenne and the Rocky Mountain area. We thought also that the project, considered as a whole, was so plainly desirable in the public interest that a detailed exposition of our views was unnecessary.

On March 6, 1951, however, Commissioner Buchanan, who dissented from our order, filed a dissenting opinion which, by unjustified insinuation and intemperate assertion, violently assails our action and, in effect, the Commisioners who took part in it. Therefore, we think it proper to set out fully the reasons for our decision and the processes by which we arrived at it.

Our duty is to weigh carefully and fairly all of the evidence in each case which comes before us to the end that we may arrive at the true facts assembled in their proper relation. We must consider impartially the inferences from these facts that are urged upon us by contending parties, [fol. 550] and, by the exercise of our own judgment, decide upon the action which will advance the purposes of the Congress as embodied in the statutes which we must administer.

It would be unnecessary to set out these obvious principles were it not that the dissenter has, in our opinion, departed from them. He has accepted, apparently without question, all of the evidence and all of the conclusions of one of the two contending parties. As a result, his opinion necessarily has been cast in the mold of a partisan brief, giving a distorted, rather than a factual, picture of the situation. Our reference to "the two contending parties" is to the applicants and to our staff which strongly opposed Colorado's proposal, as it was free to do.[1] However, when our staff assumes an adversary position in a formal proceeding, its evidence and contentions must receive no preferred consideration by reason of their origin.

Commissioner Buchanan has accused us of placing upon the gas consumers of Denver, Cheyenne and the Rocky Mountain area "an unreasonable and unconscionable burden" which, he says, approximates $800,000 a year. Whether this is so depends upon the validity of his assumptions and conclusions and upon the proper disposition of all the problems presented to us by this case. Paramount has been the problem of how best to assure natural-gas service at reasonable rates to consumers dependent upon Colorado's pipeline.

In order to have a clear understanding of the matters presented and considered by the Commission, it is necessary to review historically the relationship between Colorado and Canadian. In 1927, a decade before the Natural Gas Act was passed, Southwestern Development Company (Southwestern) through a subsidiary, Amarillo Oil Company (Amarillo), owned almost 300,000 acres of gas and

[1] Other parties were: Natural Gas Pipeline Company of America; City of Colorado Springs, Colorado; Public Service Company of Colorado; City and County of Denver, Colorado.

oil lands on which there were then about 10 producing gas wells and some gathering pipelines. Cities Service Com-[fol. 551]pany (Cities Service), through two subsidiaries, then owned manufactured gas distribution facilities in the cities of Denver and Pueblo, Colorado, and engaged to and did secure new franchises for the distribution of natural gas in those cities.

To link the gas lands with the markets, a three-way transaction was made between Southwestern, Standard Oil Company of New Jersey (Standard Oil) and Cities Service with the ultimate objective of building a pipeline from the West Panhandle Gas Field to Denver and beyond. Southwestern organized a new corporation called Canadian River Gas Company with all of its capital stock (except qualifying shares) going to Southwestern, which then had its subsidiary, Amarillo, convey all of its gas lands and facilities to Canadian. Canadian then issued $11,000,000 in bonds secured by mortgage upon all of its property, and the bonds were bought by Colorado, which had been organized by Standard Oil at the time Canadian was organized for the purpose of building the pipeline to Denver. The proceeds of the Canadian bond issue were used, first to pay Amarillo $5,000,000 for the gas lands and facilities conveyed to Canadian, and then to finance the drilling of additional wells and the construction of additional necessary facilities for delivery of gas to Colorado Interstate at Clayton, New Mexico. Amarillo reserved certain priorities of service of gas produced from the reserves for the benefit of itself and certain other Texas customers.

Contemporaneously, a ''cost contract'' was made between Canadian and Colorado, but Canadian first exacted as a consideration for entering into such cost contract the issuance and delivery to it (or its nominee) of 42½% of Colorado's common stock (par value $1,000,000) and also one-half of Colorado Interstate's preferred stock (par value $1,000,000).

Under the contract Colorado is obligated to put up all the money Canadian needs for all of its out-of-pocket costs and the building of its facilities, and Canadian owns and will continue to own all of its facilities and gas reserves.

Colorado loans this money for these purposes and is repaid by Canadian over varying periods of time in effect under the contract. Canadian gets its money for such repay- [fol. 552] ment from its sales of gas to Colorado and the Texas customers, but gets to keep no more money than the amount required to meet out-of-pocket financial obligations. These payments of debt to Colorado, along with operating expenses, are the amounts of money which Canadian charges for its gas. Since 1945, however, when the rate order of this Commission[2] against Canadian was finally made effective, the price of gas to Colorado has no longer been computed on the actual cost basis fixed by the contract, but is fixed at 4¢ Mcf for that delivered to Colorado at Clayton, New Mexico, and 3½¢ per Mcf for that which is ultimately delivered to Natural Gas Pipeline Company of America. If the money secured from these rates does not produce sufficient cash, together with Canadian's other receipts, to pay all out-of-pocket expenses and costs, including interest on and repayment of loans, Colorado must make a "below-the-line" payment to Canadian to make up the deficiency. On the other hand, if Canadian through the collection of revenues from its various sales of gas collects more that what is necessary to meet its cash obligations, that is paid by Canadian as "other income" to Colorado and is also accounted for below the line. By the expression "below-the-line" is meant that such payments by Colorado, and such receipts by it, are not operating expenses or operating revenues.

Although under this cost contract Colorado pays for all of Canadian's production, gathering and transmission facilities, Colorado cannot pledge any of these properties as security for funded debt.

Southwestern set up its investment in Canadian's stock at $1.00 on its books and has never revalued that stock. Under Article Fifth of the cost contract, it was also provided that the gas to be delivered by Candian to Colorado should be "natural gas as produced in its natural state

[2] In the Matter of Canadian River Gas Company, Colorado Interstate Gas Company, 3 FPC 32 (1942).

from the wells, except that Canadian may extract or permit the extraction of natural gasoline from its natural gas, * * *'' but that such extraction should not subject the nat-[fol. 553] ural gas to a change in the chemical composition of any of its component parts, or which might dilute the natural gas.

The value of the ownership by Southwestern of Canadian's stock is due in part to certain tax benefits arising by virtue of the filing of consolidated Federal income tax returns since Canadian is a wholly-owned subsidiary of Southwestern. In addition to the tax benefits, there are also reversionary rights that mature after the expiration of the cost contract to the beneficial interest, in all of Canadian's assets.

The cost contract by its terms would continue just so long as Canadian had available for delivery to Colorado quantities of natural gas which Colorado determined were profitable for it to buy under the terms of the cost contract, or until such time as the volume of gas available from Canadian production is sufficient only to supply the requirements of the Texas markets, which have priority over Colorado. The record indicates that this probably will occur by 1972. Canadian would then own, free from the provisions of the cost contract all of the facilities previously constructed and paid for with funds received from Colorado under the terms of the cost contract, together with the remaining gas reserves. Further, the record indicates that continued deliveries of gas to Canadian's Texas customers would then be feasible.

It was in the light of this background that Colorado and Canadian in February 1950 filed a joint application (amended in April 1950) under Section 7 of the Natural Gas Act for authority for Colorado (1) to acquire and operate all of Canadian's properties and facilities presently used for the transportation or sale of natural gas subject to the jurisdiction of the Commission, and to perform the services now carried on by both companies; and (2) contingent upon approval of such acquisition, to construct certain new transmission lines and appurtenant facilities so as to materially increase the delivery capacity of Colorado's transmission system to meet the progressively increasing demands of Colorado's customers and their consumers in the Rocky [fol.554] Mountain area.

This application was based upon an agreement between Southwestern and Colorado under which Southwestern will transfer all of the stock of Canadian to Colorado, which will thereupon cancel the Canadian stock and effect a merger of the two corporations, which automatically will end the cost contract. In consideration for Canadian's stock, Colorado will grant to Southwestern all of the natural gasoline contained in the natural gas in Canadian's acreage, but subject to continued deliveries of raw gas by Colorado to Amarillo and other Texas customers which Canadian is now contractually obligated to make, reserving however such gasoline as is contained in the gas which Colorado will deliver to its customers, the gasoline involved in minor deliveries of raw gas which Colorado may in its judgment hereafter make in the producing field, and gasoline represented by prior royalty interests. Colorado undertakes to extract, in accordance with Southwestern's specifications, the gasoline content of the natural gas, derived from Canadian's acreage, which supplies Colorado's Clayton-Denver line, and to deliver such gasoline to Southwestern at Colorado's Bivins Extraction Plants. Southwestern will market the gasoline at its own expense, which is estimated to be ¼¢ per gallon, and pay over to Colorado an amount equal to 50% of the gross revenues to compensate Colorado for the estimated costs of producing, gathering and extracting the natural gasoline. Colorado further agrees to give Southewestern 85% of the net revenues due to Colorado from the operation of Texoma Natural Gas Company's Fritch plant, where gasoline is extracted from the gas delivery by Colorado to supply one-fourth of the requirements of Natural Gas Pipeline Company of America. Out of its share of the gasoline revenues Colorado will make all royalty payments related to the total gasoline production from Canadian's acreage.

From the evidence adduced during the hearings it appeared that the present and future demands for gas of Colorado's customers in the Denver-Wyoming area had increased to a point where existing transmission facilities [fol. 555] were inadequate to transport the needed additional gas for this area. Colorado's proposal for the construction of a new transmission line with appurtenant facilities provided for a 20-inch pipeline 215 miles in length, extending from a point in the West Panhandle Field northward to connect near Kit Carson, Colorado, with Colorado's existing pipeline from the Kansas-Hugoton Field to the Denver market. The cost of these new facilities was estimated at about $10,000,000, and the evidence also disclosed that Colorado's supplier of gas, Canadian, required about $3,500,000 to defray the cost of drilling new wells in order to augment its supply of gas so as to meet the increasing demands of Colorado.

It was also shown on the record that Colorado had then borrowed approximately $19,000,000 against its net plant of $30,175,887, which was close to the limit to which it could borrow under the loan indenture which restricts its borrowing to two-thirds of its net plant.

Due to this limitation upon its borrowing power, Colorado maintained that it was unable to finance the construction of the new pipeline between the Panhandle Field and its existing transmission line connecting the Kansas-Hugoton Field with the Denver market so as to serve adequately the needs of the consumers in the Colorado and Wyoming Rock Mountain area. Its proposal to acquire the properties and facilities of Canadian, and then to merge them into one integrated operating company, appeared to the Commission to be clearly in the public interest and, after briefs had been filed and oral argument had, the Commission, without any dissent, entered an order on July 20, 1950, to that effect, but reopened the proceeding for further evidence upon the sole question of the reasonableness of the consideration to be paid to Southwestern.

Before beginning a detailed discussion of the natural gasoline revenues and tax benefits or losses which are involved in consideration of this case there should be emphasized that the evidence of record relating to these subjects necessarily consists of estimates and forecasts. From the very nature of the subject matter it is impossible with [fol. 556] certainty to arrive at precise or assured conclusions. The most that we or anyone else can do is to judge the validity of methods used and the reasonableness of estimates produced.

The essence of the contentions expressed in the dissent is that the project will cost Colorado's rate payers a sum which Commissioner Buchanan variously states as $18,087,128, $20,000,000 and $22,500,000. In our view, the record supports the conclusion that, based upon the best estimates available and an assumed average price for natural gasoline of 5¢, the gross gasoline revenues which Southwestern will receive will total $18,087,128 for a 23-year period extending through 1972.[3] Income taxes which must be paid on this sum by Southwestern will, at current rates, reduce it to $9,947,920.

The figure of $22,500,000, advanced by Commissioner Buchanan as the approximate total payments to Southwestern by reason of the transaction, is based upon an assumption that gas will be available from the Canadian acreage for Colorado's Clayton-Denver line after 1972. We think that this assumption is unfounded since the record shows that production from the Canadian acreage will probably have declined by 1972 to such a point that the volume of gas available therefrom will be sufficient only to supply the requirements of the Texas markets, which retain their priority over those in the Rocky Mountain area. Moreover, there will be no deliveries to the Natural Gas Pipeline Company of America after 1966. When such time comes Southwestern will cease to be entitled to any gasoline revenues from the extraction process carried on at the Bivins plant.

Dividing $18,087,128 by 23 gives an average annual gross revenue to Southwestern of $786,397 from gasoline produced by Colorado over the 23-year period from the Canadian acreage. We assume that Commissioner Buchanan

[3] All figures based upon estimated gasoline revenues are overstated in the record, in the dissenting opinion and in this opinion since they include estimates for all of 1950 and 1951, whereas the merger cannot become effective until sometime later this year.

[fol. 557] rounded off this latter figure to reach his conclusion that our decision will deprive gas consumers of approximately $800,000 annually. However, to reach that conclusion he had to make a number of assumptions which we consider unjustified and to ignore certain admitted facts.

First it was necessary to assume that Colorado's present rates will yield at least $18,087,128 in revenues through 1972 in excess of a fair rate of return on investment, for otherwise the impact on Colorado of the gasoline revenue receipts relinquished must be reduced by the amount of the income taxes which would be paid thereon. This is indicated by the testimony of the staff accounting witness. We cannot and we think should not make such an assumption prior to hearing and final determination by us of the formal investigation now in progress of the rates of Colorado and Canadian (Docket No. G-1115). Should the prejudgment of the rate case indulged in by Commission Buchanan be proven incorrect by the Commission's ultimate decision, based upon a more exact and complete record than that in this proceeding, the net diminution of revenues to Colorado by reason of Southwestern's share of the gross gasoline proceeds will be something under the $18,087,128 figure and may range as low as $9,947,920, which latter figure is derived by deducting income taxes computed at the current rate from the gross figure of $18,087,128.

The $9,947,920 figure clearly represents the full benefit Southwestern can expect to receive from gasoline revenues accruing to it through 1972 by reason of the merger agreement. The weight of the evidence indicates that this gain will be offset in large part by a loss to Southwestern of tax benefits estimated at $7,305,000, by reason of its relinquishing its ownership of Canadian. Thus, the net gain to Southwestern from the transaction over the 23-year period, as closely as it can be determined from estimates in this record, will approximate $2,642,920. The tax benefits, on the other hand, which Southwestern will relinquish under the merger transaction result from the fact that, beginning in 1956, Canadian would have substantial income [fol. 558] tax credits which, but for the transfer of Canadian's stock, would be available on a consolidated tax return to its parent, Southwestern. These and other credits now will be -vailable to Colorado.

Commissioner Buchanan has sought to show tax benefits which Southwestern is foregoing will be $2,238,282 less than the estimate which we consider to be supported by the record. He bases this contention solely upon the assumed tax impact of the recent case of Hudson, et al. v. Commissioner of Internal Revenue, 11 U. S. Tax Appeals 1042, affirmed per curiam, 183 F. (2d) 180 F. (2d) 180 (5th Cir.), which is claimed to establish that Southwestern, rather than Colorado, will be entitled to percentage depletion allowance associated with production of natural gasoline from the Canadian reserves.

Aside from the doubtful applicability of the Hudson case to the factual situation before us, we think that the dissenter's contention in this regard can be disposed of shortly and completely by pointing out that the Commissioner of Internal Revenue has officially stated his non-acquiescence in the Hudson decision. This, we understand, means that the case will not be followed by the Bureau of Internal Revenue in administration of the tax laws. Thus, it is probable that the $2,238,282 percentage depletion allowance, said to depend upon whether or not the Hudson case is followed as a precedent, will not be available to Southwestern without litigation. And Southwestern's formal assurance to the Commission that, if it becomes entitled to percentage depletion for gasoline extracted by Colorado it will agree to pass on to Colorado its resulting tax savings, satisfies us that it will not attempt by litigation to obtain for itself the percentage depletion benefits expected to accrue to Colorado from the production of gasoline from the Canadian acreage.

Of far greater importance, however, than the extent to which Southwestern will benefit or lose from the merger transaction is the impact of the merger on the rate payers supplied with natural gas through Colorado's facilities. We already have demonstrated that the estimated $18,087,128 gross gasoline revenues which Colorado will give [fol. 559] up to Southwestern through 1972 cannot be assumed, in the absence of final determination of our rate case, to be the net diminution in Colorado's revenues. This may range anywhere from that figure down to $9,947,920.

As against this cost Colorado stands to gain an estimated $14,324,415 in tax benefits becoming available to the merged company by reason of the transfer to it of the percentage depletion allowance based on the production of both natural gasoline and natural gas from Canadian's acreage. We think that the weight of the evidence supports this forecast in tax savings. Such savings clearly inure to the benefit of Colorado's customers and the consumers of the Rocky Mountain area.

Commissioner Buchanan attacks this estimate of tax benefits expected to accrue to Colorado on the basis of the Hudson case, which we already have discussed, and by giving no weight whatever to the evidence that there is a lieklihood that the percentage depletion allowance available to the merged company will be computed upon a wellhead gas valuation of 5¢ per Mcf rather than the current 3.17¢ valuation. The uncontradicted evidence, however, shows that other companies in the area where Canadian's reserves are located, whose operations are substantially similar to those to be undertaken by the merged company, have received approval of percentage depletion allowances based upon wellhead gas valuations of 5¢ per Mcf. The evidence shows that the comparatively low wellhead valuation accorded Canadian's gas probably has resulted from the proximity of the point of sale of the gas to Colorado to the producing field. This conclusion gains support from Section 29.23(m)-1 of the Commissioner's Regulations 111 which provides:

''In the case of oil and gas wells, 'gross income from the property' as used in section 114(b) (3) means the amount for which the taxpayer sells the oil and gas in the immediate vicinity of the well. If the oil and gas are not sold on the property but are manufactured or converted into a [fol. 560] refined product prior to sale, *or are transported from the property prior to sale, the gross income from the property shall be assumed to be equivalent to the representative market or field price (as of the date of sale) of the oil and gas before conversion or transportation.''* [Emphasis supplied.]

Further, the staff's accounting witness testified that he did not consider the 5¢ wellhead figure to be unreasonable. We cannot and do not here attempt to influence the depletion allowance ruling which will be made by the Bureau of Internal Revenue, but, from this record, we think that the basis upon which the tax savings to Colorado of $14,324,415 was estimated is a reasonable one.

Considerable significance is attributed in the dissent to the fact that the Administration has recommended to the Congress that the present depletion allowances of 27½% of the value at the wellhead be reduced to 15%. It is stated that this would drastically reduce the tax benefits to Colorado from the merger. But we cannot, if we are to be realistic, base any conclusions upon this proposed amendment of the tax laws. It would be just as reasonable for us to assume that the corporate income tax rate will be increased from 45% to 55%, as also has been recommended by the Administration. Such an assumption would greatly increase Colorado's prospective tax savings.

To sum up the probable cost and offsetting tax benefits to Colorado from the merger: Colorado will relinquish net revenues over a 23-year period which, based on estimates which appear to us to be reasonable, may possibly be as much as $18,087,128 or as little as $9,947,920,[4] depending upon the outcome of our formal rate case. Offsetting this will be estimated positive tax benefits, computed upon bases which we consider reasonable, of $14,324,415. Thus, laying aside for the moment all consideration of improved corporate structure, acquisition of physical property, enhancement of borrowing ability and the making available to the [fol. 561] gas consumers of the Rocky Mountain area of adequate supplies of low priced gas, the merger can be expected to involve at the most a cost to Colorado of $3,762,713 spread over a 23-year period, or, in its most favorable light, cash benefits to Colorado over the same period of $4,376,495.

These are the revenue figures which reasonably can be

[4] The spread between these two figures represents 45% income tax on the larger, as explained above.

expected to have an effect upon Colorado's rates. Yet Commissioner Buchanan stated: "The revenues of more than 20 million dollars given up by Southwestern must be made up by the gas consumers for the reason that their cost of gas is increased by an equivalent amount since they enjoyed the credit in the past but will not have it in the future."

By this groundless conclusion the dissenter completely ignores that a very substantial tax saving will accrue to Colorado by reason of the merger, a fact which was freely admitted by the principal witness opposing the joint application. This witness sought only to show that the tax saving would be less than the amount claimed.

* * * * * * *

Upon the record before us, we are convinced that the long-run benefits to the consumers dependent upon Colorado would far out-weigh any costs which could reasonably be expected to follow from the merger. However, to avoid any possible doubt as to the full protection to the gas consumers dependent on Colorado, we conditioned our certificate to provide (1) that any excess of cost to Colorado from its gasoline extraction operations over the revenues accruing to it therefrom, would not be considered as a cost of service to the company's natural-gas consumers and customers; (2) that Colorado should tender to its resale customers service agreements in which it would commit itself not to dispose of the natural-gas reserves to be acquired from Canadian so long as it is economically feasible to produce natural gas from such reserves; and (3) that it would tender to its resale customers service agreements in which it would commit itself not to propose any increase in any resale rate attributable in whole or in part to the acquisition and merger authorized by the certificate. We [fol. 562] also required that Colorado file with the Commission within 30 days its written acceptance of the certificate as conditioned.

* * * * * * *

Now that the acquisition by Colorado of the Canadian properties has been authorized and the future pattern of operation settled, it is appropriate that our rate investigation should be brought to a speedy conclusion. In our order issued March 1, 1951, we required Colorado, within four months of that date, to report to us the completion of the acquisition, the commencement of operation by it of facilities acquired, and proof of dissolution of Canadian. Therefore, we have, by order entered today, fixed the date of hearing in the rate case for August 1, 1951, which is one month after the required -ate for such report.

* * * * * * *

Buchanan, Commissioner dissenting:

I find it necessary to dissent from the decision of the majority[1] in the above docket, because (1) in my opinion the decision unjustifiably deprives the gas consumers of Denver, Cheyenne and the Rocky Mountain area of a saving in gas rates of approximately $800,000 on an annual basis; and (2) the decision is completely at odds with fundamental principles of regulation vigorously espoused by this Commission and approved by the United States Supreme court.[2]

Since the majority, in their order, did not set forth their reasons for approving the Applicants' proposition or state why they found that the merger of Canadian and Colorado is required by the present public convenience and necessity or why, in their opinion, the payments proposed to be made by Colorado to Southwestern Development Company are reasonable and not incompatible with the public in-[fol. 563] terest, it is fair to assume that the majority have accepted as valid the reasons given by the joint Applicants why their proposal should be approved. It is, therefore, necessary for me to set forth in some detail the proposal of the Applicants, and the issues raised during the course of several hearings and in the briefs and oral argument.

Upon analysis, these alleged tax benefits appear extremely indefinite and uncertain. They are based upon the

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[1] Order date February 28, 1951.

[2] Canadian River Gas Co. v. F. P. C., et al., 324 U. S. 581.

unwarranted assumption that the Bureau of Internal Revenue will increase from 3.17¢ per Mcf to 5¢ per Mcf the gross value at the wellhead of natural gas used in computing Canadian's statutory depletion allowance. The 5¢ value was developed by Southwestern's auditor and represents his sole judgment (T. 1128). Furthermore, the record shows (T. 1136) that the sale of gas at the Fritch Plant between Colorado and Natural Gas Pipe Line Company at 3½¢ per Mcf will continue after the merger. In the face of these facts and of the great need of the Federal Government for revenue at this time it does not seem reasonable nor possible to assume that the Government is going to give up tax revenues amounting to $300,000 a year simply because of the elimination of the interdepartmental sale between Canadian and Colorado through a merger.

*   *   *   *   *   *   *

[fol. 564] BEFORE THE FEDERAL POWER COMMISSION

ORDER ISSUING CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY AUTHORIZING ACQUISITION AND OPERATION OF PIPELINE FACILITIES AND AMENDNG ORDER ISSUING CERTIFICATE OF PUBLIC CONVENIENCE AND NECESSITY AUTHORIZING CONSTRUCTION OF NEW PIPELINE FACILITIES—Issued March 1, 1951

Upon further consideration of the joint application filed by Colorado Interstate Gas Company (Colorado) and Canadian River Gas Company (Canadian) on February 13, 1950, as amended on April 4, 1950, for certificates of public convenience and necessity authorizing (a) the acquisition and operation by Colorado of all the properties and facilities of Canadian, and (b) the construction and operation by Colorado of additional pipelines and facilities, it appears from all evidence adduced at the public hearings in this proceeding, the briefs of all counsel submitted at the conclusion of the hearings, and oral argument, that:

On July 20, 1950, following public hearing, submission of briefs, and after the conclusion of oral argument in the above entitled proceeding, the Commission issued a certificate of public convenience and necessity authorizing

Colorado and Canadian to construct and operate certain natural-gas pipeline facilities as fully described in the amended joint application mentioned in the last preceding paragraph.

By said order of July 20, 1950, the Commission found that a merger of the facilities and properties of Canadian with the facilities of Colorado was in the public interest and by paragraph (B) thereof reopened the proceeding for hearing at a date to be fixed by the Commission for testimony limited to the sole issue of the reasonableness of payments proposed to be paid to Southwestern Development Company by Colorado for the acquisition of Canadian's properties and facilities.

Thereafter said order of July 20, 1950, was amended by order dated October 3, 1950, so as to extend to December 20, 1950, the time within which to submit their plan for financing, satisfactory to the Commission, to defray the cost of constructing such proposed additional facilities.

[fol. 565] Pursuant to the Commission's order of November 1, 1950, fixing the time and place of further public hearings herein, evidence has been adduced respecting the reasonableness of the contemplated payments by Colorado to Southwestern Development Company, and of respecting the financing plan of Colorado.

The Commission finds:

(1) All of the properties and facilities proposed to be acquired and operated by Colorado from Canadian, as described in said joint application, as amended, will become and be an integral part of the presently owned and operated properties and facilities of Colorado and will thereafter be used for the transportation and sale of natural gas in interstate commerce, subject to the jurisdiction of the Commission, and such acquisition and operation thereof as an integral part of the pipeline system presently owned and operated by Colorado are subject to the requirements of subsections (c) and (e) of Section 7 of the Natural Gas Act, as amended.

(2) The Commission's order of July 20, 1950 should be amended so as to allow Colorado additional time within

which to commence and complete the construction of the additional pipe lines and appurtenant facilities which were authorized by the Commission's order of July 20, 1950.

(3) Colorado has secured a firm and binding commitment from a responsible lender for a loan of $12,000,000 at an interest rate of 2⅞ precent, conditioned, however, on the consummation of the acquitition by Colorado of Canadian's properties and facilities, the proceeds of which loan will be reasonably adequate to enable Colorado to finance the construction of the additional pipe lines and appurtenant facilities authorized by the Commission's order of July 20, 1950.

(4) Such acquisition will not adversely affect Colorado's supply of gas and will permit Colorado to better serve its customers at present rates. Colorado is able and willing properly to do the acts and to continue to perform all existing services of both companies and to conform to the provisions of the Natural Gas Act, as amended, and the [fol. 566] requirements, rules and regulations of the Commission thereunder.

(5) The acquisition and operation by Colorado of all of the properties and facilities presently owned and operated by Canadian, as they are described in said amended joint application, through the acquisition of all of the capital stock of Canadian from Southwestern Development Company, and the contemporaneous corporate merger of the two operating companies, is required by the present public convenience and necessity.

(6) The payments proposed to be made by Colorado to Southwestern Development Company as the consideration for all of the capital stock of Canadian is reasonable and not incompatible with the public interest and such acquisition should be approved, as hereinafter conditioned.

The Commission orders:

(A) A certificate of public convenience and necessity be and the same is hereby issued authorizing Colorado to acquire and operate the properties and facilities presently owned by Canadian and described in the amended joint application (together with the exhibits therein mentioned and made a part thereof) for the transportation and sale of natural gas as therein set forth, subject to the jurisdiction of the Commission, upon the following terms and conditions:

(i) The authorization herein granted for effectuating the acquisition and operation of Canadian's properties and facilities is upon the express understanding and condition that if, as a result of carrying out the terms and conditions in the transaction proposed as a part of the acquisition and merger of Canadian into Colorado whereby rights to liquid hydrocarbons in place are granted to Southwestern Development Company and whereby Colorado is to receive 50% of the gross proceeds from the sale of certain liquid hydrocarbons and 15% of the net revenues to be received by Colorado from the hydrocarbons resulting from the operation of Fritsch Natural Gasoline Plant of Texoma Natural Gas Company, the costs properly allocable to such hydrocarbons exceed the amounts payable to Colorado pur- [fol. 567] suant to such transaction, then and in that case in any proceeding in which the effective or proposed rates of Colorado are under inquiry such excess shall not be considered as a cost of service to Colorado's natural gas customers and consumers.

(ii) Colorado shall, within 4 months from the date of this order, report to the Commission in writing, under oath, the completion date of the acquisition hereby authorized and also the date at which it commences operation of the facilities so acquired, together with a duly authenticated certificate or other document showing the final dissolution of Canadian River Gas Company by the surrender of its corporate charter.

(iii) The entries in Colorado's books of account respecting the cost of all properties and facilities acquired by it by reason of this certificate shall be subject to the approval of this Commission.

(iv) Colorado shall tender to all of its resale customers service agreements in which Colorado will agree (1) that it will not sell, transfer or otherwise alienate natural gas reserves which it proposes, as part of the acquisition and merger, to acquire from Canadian, so long as it is economically feasible to produce natural gas from such reserves, and (2) that it will not propose any increase in any rate subject to the jurisdiction of the Commission which will be attributable in whole or in part to the acquisition and merger authorized herein.

(v) Colorado shall, within 30 days from the date hereof, file with this Commission a certificate duly authorized by its Board of Directors and duly executed by its executive officers, showing the acceptance of this certificate of public convenience and necessity.

(B) Colorado shall commence the construction of the new additional facilities involved in this proceeding (described in the amended joint application) within six months from the date of the issuance of this order and shall complete such construction within one year from the date hereof.

[fols. 568-592] (C) Colorado shall submit to the Commission, in writing, commencing six months from the issuance of this certificate monthly progress reports which shall generally include statements concerning the purchase of material and equipment and the progress of the construction work, and upon completion advise the Commission of the completion date, together with the date of commencement of operations.

(D) This certificate is not transferable and shall be effective only so long as Colorado continues the services and operations hereby authorized in accordance with the provisions of the Natural Gas Act, as amended, and any pertinent rules, regulations or orders heretofore or hereafter issued by the Commission.

By the Commission. Commissioner Buchanan dissenting and will file a separate statement.

J. H. Gutride, Acting Secretary.

* * * * * * *

And thereafter the following proceedings were had in said cause in the United United States Court of Appeals for the Tenth Circuit:

Order: Cause Argued and Submitted.

First Day, September Term, Tuesday, September 8th, 1953. Before Honorable Sam G. Bratton, Honorable Walter A. Huxman and Honorable Alfred P. Murrah, Circuit Judges.

This cause came on to be heard, James Lawrence White, Esquire, and William A. Daughtery, Esquire, appearing for petitioner, Jacob Goldberg, Esquire, appearing for respondent.

On motion, the City of Colorado Springs, Colorado, was granted leave to intervene in this cause.

Thereupon this cause was argued by counsel and was submitted to the court.

Opinion

[Oct. 29, 1953]

James L. White and William A. Dougherty (John P. Akolt, Sr., John R. Turnquist, Charles E. McGee and Lewis M. Poe were with him on the brief) for Petitioner;

Jacob Goldberg (Bradford Ross, Bernard A. Foster, Jr., and Reuben Goldberg were with him on the brief) for Respondent.

Before Bratton, Huxman and Murrah, United States Circuit Judges.

Huxman, Circuit Judge.

Colorado Interstate Gas Company, herein referred to as Colorado, a natural gas company under the Natural Gas Act, seeks review of the order of the Federal Power Commission, herein referred to as the Commission, entered under the appropriate provisions of the Act,[1] reducing Colorado's rate for natural gas sold in interstate commerce for resale. Nineteen hundred fifty-two was taken as the test period. Based upon Colorado's operations for that year, the Commission found and concluded that the rates established by Colorado in connection with interstate business were unjust, unreasonable and excessive and resulted in an unreasonable and excessive exaction from its customers in the sum of $3,111,187 and that new rates reflecting a reduction of such sum in such revenues would be just and reasonable. Such rates were ordered and this petition for review challenges the correctness and validity of such order.

In arriving at its conclusions, the Commission accepted for the test period of 1952 the total revenues of $19,104,052 as reflected by

[1] 15 U. S. C. A. § 717-717 (w).

Colorado's books and as used by it in its exhibits in the case. Colorado's books reflected a total rate base of $57,200,440, while the Staff used a total rate base of $57,164,666, only $35,794 less than shown by Colorado's books. No issue is raised with respect to this slight difference and it may be disregarded. Colorado's revenues for the year 1952 in the total sum of $19,104,052 were accepted by the Staff and by the Commission. Colorado claims a total cost of service of $19,942,871, while the Staff adopted a cost of service base of $15,549,802. The Commission adopted a cost service base of $14,952,567, of which it allocated $10,273,474 to jurisdictional operations. It adopted 5¾% as a fair rate of return and fixed new rates which it concluded would return to Colorado from jurisdictional operations $10,289,269.

Colorado owns and operates extensive natural gas production gathering and processing facilities in the West Panhandle Field of Texas and also purchases and processes large volumes of natural gas in the Hugoton Field of Kansas. It also owns and operates a transmission pipeline system, extending from such fields to its general market area at Denver, Colorado. Sales are made from such pipelines to distributing facilities for resale and to industrial customers.

This proceeding was instituted on the Commission's own initiative. Extensive and numerous hearings were held. Hearings began on October 1, 1951, before a presiding examiner of the Commission and with intervening recesses were concluded on April 4, 1952. By order of May 23, 1952, the Commission dispensed with the filing of the intermediate opinion of the trial examiner. Briefs were thereafter filed with the Commission. Arguments of counsel were had and on August 8, 1952, the Commission issued its opinion with an accompanying order, directing a reduction of rates as above outlined.

Numerous assignments of error are urged by Colorado. Among others, it contends that dispensing with the filing of the trial examiner's intermediate report constitutes deprivation of due process and voids the order of the Commission. Since this contention, if sustained, would dispose of the case and make unnecessary a consideration of the remaining assignments of error, we consider it first.

5 U. S. C. A. § 1007 (a) in part provides, "In cases in which the Agency has not presided at the reception of the evidence, the officer who presided * * * shall initially decide the case or the agency shall require * * * the entire record to be certified to it for initial decision. Whenever such officers make the initial decision and in the absence of either an appeal to the agency or review upon motion of the agency within time provided by rule, such decision shall without further proceedings then become the decision

of the agency. On appeal from or review of the initial decisions of such officers the agency shall, except as it may limit the issues upon notice or by rule, have all the powers which it would have in making the initial decision. Whenever the agency makes the initial decision wthout having presided at the reception of the evidence, such officers shall first recommend a decision except that in rule making or determining applications for initial licenses * * * (2) any such procedure may be omitted in any case in which the agency finds upon the record that due and timely execution of its functions imperatively and unavoidably so requires."

There are not many decided cases which have dealt with the power of the Commission to dispense with the trial examiner's initial report. In *Kenny* v. *United States,* 103 F. Supp. 971, a three-judge court held that under the Interstate Commerce Act the exceptions embodied in Section 1007 (a) (2) were intended to permit the omission of the intermediary report or tentative decision by a trial examiner where the law contemplated speedy and expeditious proceeding by the agency. While that case arose before the Interstate Commerce Commission under the Interstate Commerce Act providing that the Commission "shall give to the hearing and decision * * * preference over all other questions", we think what was said applies with equal force and logic under the Act in question here.[2] We think it is clear that Congress intended that party contestants before the Commission are as a matter of right entitled to the benefits of the intermediate report save only in the two exceptions noted in Section 1007 (a) (2) but we are of the further view that under the exceptions as noted the Commission may in the exercise of a sound discretion either upon its own volition or upon the application of any party to the proceeding dispense with the filing of the report. In Footnote 3 we have set out some of the

[2] See also *Alabama-Tenn. Natural Gas Co.* v. *Federal Power Commission,* 203 F. (2d) 494.

[3] With respect to this exception, Congressman Walter, one of the co-authors of the bill, explaining the exceptions stated that "the parties will be better served if the proposed decision * * * reflects the views of the responsible officers in the agencies, whether or not they have actually taken the evidence." Senate Docket No. 248, 79th Congress, Second Session, Page 361.

And the Senate Committee said, "The exemption of rule making and determining initial applications for licenses from provisions of Section 5 (c), 7 (c), and 8 (a) may require change if, in practice, it developes that they are too broad. Earlier in this report in commenting upon some of those provisions, the Committee had expressed its reasons for the language used and had stated that, expressions in Congress. Appearing in the record, the reasons assigned by the Commission for its action in this respect are that there was good reason to believe that the rates being exacted were excessive; that an unjust exaction was being demanded from the gas users; that the case had been pending for three years and that it was to the benefit and interest of all that the matter be speedily adjudicated. These are cogent reasons supporting the action of the Commission under a statute vesting it with authority to dispense with the intermediate report in a case such as this.

Colorado, however, strenuously contends that there are present facts which stamp the action of the Commission as arbitrary and that by such action it was denied that due process to which it was entitled as a matter of law. It contends that the proceeding was adversary and accusatory in nature; that the issues of fact were sharply drawn and that there was conflict in the basic facts as well as an issue of the credibility of the witnesses; that the trial examiner who heard and saw the witnesses was best able to appraise and resolve this conflict in the evidence and, having seen the witnesses in the first instance, pass on their credibility, and that therefore dispensing with the examiner's report deprived it of his observations with respect to these matters, which he alone could make.

For support of this contention, Colorado relies in large part on what was said by the Supreme Court in *Universal Camera Corporation* v. *National Labor Relations Board,* 340 U. S. 474. That case involved a charge of unfair labor practices under the Labor Act. The board rejected the examiner's findings and did not take them into consideration in its consideration of the case. This the Supreme Court said was error. But all the court held was that the trial examiner's report constituted evidence which should be considered along with all other facts and circumstances by the board in reaching its conclusion whether there was substantial evidence showing a violation. There was not involved the question under what conditions, if any, the examiner's report might be dispensed

where cases present sharply contested issues of fact, agencies should not as a matter of good practice take advantage of the exemptions." Senate Docket No. 248, 79th Congress, Second Session, Page 216.

"There are, however, some instances of either kind of case (rule making and licensing) which tend to be accusatory in form and involve sharply controverted factual issues." Senate Docket No. 248, 79th Congress, Second Session, Page 262.

"* * * if issues of fact are sharply controverted, or the case or class of cases tends to become accusatory in nature * * *." Senate Docket No. 248, 79th Congress, Second Session, Page 273.

Like and similar statements appear in the reports of the Committees.

with. It is obvious that the issues arising in a labor board case, charging unfair labor practices, differ materially from those arising in a rate hearing case before the Federal Power Commission, such as we have here. In a labor board case the facts are always in sharp conflict and the credibility of witnesses many times involved.

To set out in detail the evidence which in our opinion warrants the conclusion that there was no disputed issue of fact would extend this opinion, which of necessity must be lengthy, to undue length. We, therefore, content ourselves with saying that a careful analysis of the record does not in our view sustain the contention that there was any material conflict in the basic facts or that the credibility of witnesses was an issue. The facts with respect to the financial structure of Colorado, its gross revenues, as well as its expenditures, were all taken from the company's books. With slight variation the facts as revealed by Colorado's books were taken as the basic facts considered by the Commission in reaching its conclusions. The line of cleavage came with respect to the methods to be employed in allocating revenue and expenditures between jurisdictional and non-jurisdictional operations and the proper method by which to fix depletion, as well as other relevant matters. The difference between the parties involved difference of opinion and the inferences and deductions to be drawn from established basic facts. These issues arose in specialized fields calling for the opinion of experts. It was not a question of the credibility of the expert witnesses but rather a question of the weight to be accorded to their opinions. The Commission was as competent to pass on these questions without the examiner's intermediate report as with it because these questions were plainly within the Commission's expert competency.[4]

Colorado makes the further contention that the proceedings are fatally defective because it was not given the notice required by 5 U.S.C.A. § 1003 (a). Its contention in this respect is that it was not notified or advised of the contention of the Commissioner's Staff. It points to the fact that the Staff introduced three cost of service studies relating to the years 1951, 1952 and 1953 and did not definitely state which one it stood on until after the hearings were closed.

But the notice to which Colorado was entitled prior to trial under Section 1003 (a) was not of the position the Staff (the prosecuting agency) would take at the hearing. Under Section 1003 (a) it was entitled to notice of "a description of the subjects and issues involved" in the proceeding and such notice it had. There was never any doubt as to the issues and matters involved in the hearing. Colorado, like the Staff, likewise introduced three alternative cost

[4] *Gloyd* v. *Commissioner of Internal Revenue,* 63 F. (2d) 649, and cases there cited.

of service studies during the hearing. It is without dispute that Colorado's operations in 1952 were taken as the test period and that Colorado at all times knew of the contentions made with respect to such operations and had ample opportunity to meet them and prepare its case.

Jurisdiction of the Commission and Scope of the Review

Before going to a consideration of the substantive issues raised by Colorado, it might be well to set out the basic principles of law delineating the Commission's jurisdiction and our scope of review. The primary purpose of the Natural Gas Act was to protect the users of gas against exorbitant exactions at the hands of the natural gas companies and on the other hand assure to them the right of a fair return from their operations.[5] The duty and jurisdiction to effectuate these broad principles were lodged with the Commission. The Act provides that all rates shall be just and reasonable. It not only empowers but makes it the duty of the Commission, when necessary, to hold hearings to determine just and reasonable rates and fix the same by order. Any aggrieved party may petition the appropriate circuit court of appeals for review. Such court is vested with exclusive jurisdiction to affirm, modfy, or set aside in whole or in part such order. But our scope of review is a limited one. The Act provides that "The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive."[6] In the Jersey City case, cited in Footnote 6, the Supreme Court quoted with approval from the Hope case, as follows: " 'Moreover, the Commission's order does not become suspect by reason of the fact that it is challenged. It is the product of expert judgment which carries a presumption of validity. And he who would upset the rate order under the Act carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences.' " It is in the light of these principles that we examine the entire record to determine whether the Commission's findings are supported by substantial evidence. If they are, we may not set them aside merely because we, as the triers of the facts, might reach different conclu-

[5] *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591.

[6] Section 19 (b); see also *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591; *I. C. C.* v. *Jersey City*, 322 U. S. 503; *Colorado Interstate Gas Co.* v. *Federal Power Commission*, 142 F. (2d) 943; *Cities Service Gas Co.* v. *Federal Power Commission*, 155 F. (2d) 694.

sions. We will consider the assignments of error in the order set forth in Colorado's brief. They are as follows:

The Commission Failed to Make Adequate Findings Between Jurisdictional and Non-Jurisdictional Sales

Under this heading Colorado contends that the Commission did not show an allocation of cost of service among petitioner's several classes of customers and did not make findings as to the determinants necessary for it to verify that it will be able to earn under the several rate schedules prescribed by the Commission the fair return allocated by the Commission. In the first place, Colorado does not contend that there is no evidence in the record that it will be able to earn the sum of $10,289,269 under the new rates fixed by the Commission. Table II of the Commission's opinion does show the allocation of the total cost of service broken down as to well mouth, gathering and products extraction, with respect to direct sales, total transmission, systems, leased transmission facilities and other operations. Tables III, IV and V of the opinion show additional details as to such allocations. In the absence of any claim or showing that the revenues found by the Commission under its allocations will not accrue, Colorado may not complain because the cost of service is not further broken down.

Not much need be said with respect to the contention that no findings were made with respect to the determinants necessary for Colorado to verify that it will be able to earn under the several rate schedules the return allowed by the Commission. It seems to be conceded that both parties used billing demand and commodity value as determinants and that they were also used by the Commission. By the application of these two determinants to the rate schedules, the rate of return can be ascertained. It was, therefore, not necessary for the Commission to make specific findings with respect to these determinants, which admittedly were used by it as well as the parties to the litigation.

The substantive issues in conflict center around three items which must be considered in determining total cost of service. While the cost of service found by the Commission was $3,484,784 less than that found by Colorado, it challenges only $2,827,778 thereof. To resolve the issues in dispute, it is not necessary to make detailed computations of the items making up this amount. We do not understand that Colorado challenges the correctness of the computations if it be conceded that the treament accorded these items by the Commission is correct. These three items are (a) loss, if any, from gasoline extraction, (b) percentage depletion allowance, and (c) fair rate of return.

Gasoline Operations

Prior to this proceeding, Colorado sought and obtained permission to merge the properties of Canadian River Gas Company. Under the merger it was proposed to transfer from Canadian River to Southwestern Development Company, or its nominee, the liquid hydro-carbons in the gas production by Canadian River from the West Panhandle Field. Colorado was to continue to process the wet gas to remove the liquid hydro-carbons. Under this arrangement the revenues derived by Canadian River from the extraction and sale of natural gasoline, which had theretofore been used to reduce the cost of gas purchased by Colorado from Canadian River,[7] would be lost upon the consummation of the merger. The authorization for the merger was granted upon the express condition that whereas rights to liquid hydro-carbons in place were granted to the Southwestern Development Company and whereas Colorado was to receive 50% of the gross proceeds from the sale of certain liquid hydro-carbons and 15% of the net revenue was to be received by Colorado from the hydro-carbons resulting from the operation of Fritch Natural Gas Plant of Texoma Natural Gas Company, that if the cost properly allocable to such hydro-carbons exceeded the amounts payable to Colorado pursuant to such transactions then and in that case *in any proceeding in which the effective or proposed rates of Colorado are under inquiry such excess should not be considered as a cost of service to Colorado's natural gas customers and consumers.* The Commission determined that there was a loss from such operations and deducted the amount it found as the loss from the cost of service. Colorado on the other hand contends that there was a net profit from such operations. Whether there was a loss depends upon whether the methods of allocation of certain costs of operation adopted by the Commission were proper.

All parties recognized that since the liquid hydro-carbons are contained in the wet gas stream the cost of producing and gathering such wet stream to the inlet of the gasoline plants is a joint cost which must be allocated upon some reasonable basis between dry gas and gasoline. The Staff's method of relative market value was adopted by the Commission as a proper method of allocation. Under this method the joint costs were apportioned to the dry gas and gasoline on the basis of the relative market value of the finished products. The direct costs to make each product fully marketable was deducted from the respective market values of the finished prod-

[7] See *Colorado Interstate Gas Company* v. *Federal Power Commission,* 324 U. S. 581.

ucts, so as to determine relative market values at the point of processing, where operations cease.

For the respective market value the Staff recommended and the Commission used 5 cents per Mcf as the value of dry gas, and as the value of gasoline the total gasoline revenue for 1952, as estimated by Colorado, less the direct cost to make the gasoline marketable, and other direct gasoline costs. The treatment to be accorded the costs within the plants will be discussed later in the opinion. Colorado on the other hand allocated the well mouth and gathering cost on what is termed a volumetric method, based on the shrinkage of the wet gas volume while being processed.

Colorado's contention that the Commission did not approve the relative value method as a proper method of allocation finds no support in the record. True, it did say that neither method was entirely satisfactory, but the same could be said with respect to any method which might be proposed. Mathematical exactness in the apportionment of cost is an impossibility. Because a method may have some infirmities does not of itself condemn it as a proper method.[8] It is the duty of the Commission to select that method which in its considered judgment more nearly reaches a just and sound result. The Commission did approve and apply the relative value method, and without extended discussion, we think its conclusion with respect thereto finds support in the record and is, therefore, approved.

Colorado's contention that there is no evidence in the record supporting the Commission's valuation of 5 cents per Mcf for dry gas and, if that method were to be employed, that 10 cents should have been fixed as its value, is without merit. Without setting out the evidence in detail, it is sufficient to say that the evidence on which the Commission relied in fixing the value at 5 cents is a least as convincing, and perhaps more so, than the merger testimony of one witness on which Colorado relies to fix the value at 10 cents.

The more difficult question is whether the Commission correctly eliminated the loss from these gasoline operations from the cost of service. The gasoline operations were as much a part of Colorado's business as any other operation. Save for the provision in the merger order hereinbefore italicized, the total costs of the operation of this department would have of necessity been considered as a part of the total cost of service. The Commission seeks to justify its elimination of the loss from the cost of service under the provision in the merger order that such loss should not be taken into account in establishing new rates.

[8] *Colorado Interstate Gas Co.* v. *Federal Power Commission,* 324 U. S. 581.

Throughout all the decisions runs the basic principle that the important and deciding factor in rate hearings is the end result. They emphasize that a reviewing court is more concerned with the end result than with the multiple detailed mechanics employed in reaching it. This was emphasized by us in *Colorado Interstate Gas Company* v. *Federal Power Commission,* 142 F. (2d) 943, and in *Colorado Interstate Gas Company* v. *Commission,* 324 U. S. 581, 603, where the Supreme Court again stated, "It is not the theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry * * * is at an end." Conversely, if the total overall effect of the rate order is to deprive the utility of the opportunity to earn a fair return, it cannot stand.

It would seem that the elimination of the loss of the gasoline operations from the cost of service deprives Colorado of earning the fair rate of return to which it is entitled. It means that this loss must come out of the net profits of the stockholders notwithstanding that it is an element of cost of service. Nor is it an answer to say that this was a condition of the merger order and that, therefore, Colorado's stockholders are bound and saddled with this loss. We are dealing here with a business affected with a public interest. Parties in such businesses are not free to contract as they choose. They are subject to regulation by proper Governmental authority. In the exercise of its jurisdiction, such authority must be fair, both to the public and to the utility. It is the statutory duty of the Commission to establish on the one hand rates that are fair and just to the utility and on the other hand to strike down rates that demand an unlawful and unreasonable exaction. A rate based upon the exclusion from the cost of service, no matter for what reason, of a subsantial amount of admitted operative cost does not and cannot reach a just end result and may, therefore, not stand.

The provision in the merger order that such operative costs as we are considering here should be eliminated from the cost of service base in subsequent rate hearings does not alter these basic principles. When that proceeding was before the Commission, it was its statutory duty to determine whether the plan was fair and just to Colorado's gas users. If it found that it might result in an unjust burden on them, it had power to disapprove it. It could not predicate its approval thereof upon a condition which it could not adopt in a rate hearing and which would thereafter deprive Colorado of the opportunity to earn a fair return upon its investment.

Costs Within the Gasoline Plants

The Commission did not adopt in whole the method championed either by its Staff or Colorado for allocating costs within the gasoline plants. In some respects it agreed with Colorado's contentions and made an allocation based thereon. In others it adopted a method proposed by its Staff. Since no issue is raised in the petition for review with respect to these allocations, we do not deem it necessary to further notice or discuss this element of allocation of joint costs.

Percentage Depletion

Under the Tax Code, a producer of natural gas is allowed an annual deduction for depletion of 27½% of the well head value of the gas, not to exceed 50% of the net income. The treatment of this item is one of the major points of conflict in this case. It is, of course, obvious that the greater the amount of deduction for depletion the less remains of income in which to pay an income tax and correspondingly less will be the amount of the income tax which may then be included as an element of cost of service. The Commission fixed the value of the well head gas for this purpose at five cents per Mcf and then used that sum in determining the depletion allowance to be deducted from gross income for the purpose of computing income taxes. The income taxes so computed were then included as an element of the total cost of service. Colorado contends that the only proper value for this purpose was 3.17 cents. It asserts that the erroneous use of 5 cents per Mcf had the effect of increasing Colorado's percentage depletion deduction for federal income tax purposes by $938,449, which in turn had the effect of reducing the allowance of federal income taxes as an element of cost of service by $1,016,653.

Colorado's contention that the 3.17 cents is the only correct value which may be fixed on the gas at the well head is based on the fact that in 1946 the Bureau of Internal Revenue fixed this value on the gas for income tax computation purposes for Canadian River and that it has been thus used ever since. It argues with some force that if it is required to compute percentage depletion on a 5 cents valuation for rate fixing purposes and thus received a lower rate because of a greater depletion from the cost of service based and, when it then later files its income tax return is permitted to deduct depletion allowances on a value of only 3.17 cents, its actual income taxes will be measurably higher than those computed in determining its rate base and that thus the rate so fixed will result in an unfair rate of return.

The Commission contends that Colorado is estopped to deny that 5 cents is the proper value to place on the well head gas by reason of the fact that its application to the Commission for authority to merge with Canadian River it represented that a saving would be effected in Federal income taxes by the fact that Colorado's depletion allowance would be based on a 5 cents value instead of 3.17 cents and that this representation was accepted by the Commission and was a factor inducing it to grant the merger order. Since we do not rest our decision on estoppel, it is not necessary to resolve this question.

We have already said there was substantial evidence supporting the Commission's finding of a 5 cent well head gas value. The question then is should it have surrendered its considered judgment with respect to this value and have adopted a value of 3.17 cents, because that was the value fixed in 1946 by the Internal Revenue Department for depletion allowances for Canadian River. To do so would in our opinion constitute an abdication and surrender of a duty placed upon the Commission by the Act. It could discharge its functions of ascertaining a fair rate of return only by considering all relevant factors necessary for such a determination as of the time of the inquiry. This it is obvious included the present value of the well head gas for depletion purposes. In fixing this value, it was required to exercise its own judgment rather than fix a value merely because it had been adopted by another agency for another purpose and at another time.

Government is carried on through many more or less independent, although correlated, agencies which must work together toward a common objective. It can function efficiently and without injury to its citizens in many instances only if there is proper cooperation and recognition of interdependent relations between these various departments. It is not to be assumed in advance that the Internal Revenue Department will disregard a finding by the Commission in this respect without good cause and will arbitrarily adhere to a fixed depletion value for gas, adopted six years before, which will work serious injury to Colorado but, if so, and as pointed out by the Commission, it would then become a matter for future consideration. It is no reason to ask the Commission to not discharge its duty in finding the fair present marketable value of the gas in question.

Rate of Return

Colorado contended for a 6½% rate of return. The Commission fixed 5¾% as a fair rate of return. It found that such a rate of return would produce a return for the common stock equity of Colorado of 8.45%, after allowing ½% for cost of financing, after servicing of Colorado's debt and preferred stock requirements and after allowing for all income taxes. From this the Commission concluded that such rate of return was wholly adequate to insure confidence in the financial soundness of the utility to maintain its credit and to enable it to attract capital necessary for the proper discharge of its public duties. The capital structure of Colorado considered by the Commission is set out in its opinion as follows:

		Amount	Percent
"Long-term Debt		$29,600,000	53.9%
Preferred Stock		2,000,000	3.6%
Common Equity			
Common Stock			
(1,711,016.6 shares)	$ 8,555,000		
Surplus	14,759,000		
		$23,314,000	42.5%
		$54,914,000	100.0%

The outstanding long-term debt of Colorado consists of four issues of long-term serial notes as follows:

2% Notes, due $400,000 semi-annually May 1, 1952 through May 1, 1954	$1,200,000[14]
2¾% Notes, due $400,000 semi-annually November 1, 1954 through November 1, 1964	8,400,000
3⅛% Notes, due $250,000 semi-annually October 1, 1952 through April 1, 1969	8,000,000
3¾% Notes, due $400,000 semi-annually February 1, 1955 through August 1, 1969	12,000,000

[14] Excludes $800,000 of such notes due within one year included in current liabilities."

From this the Commission found that the weighted average cost of the debt was 3.25% for all of its outstanding long-term debt; that the preferred stock bore a dividend rate of 6%.[9] The Commission noted that the most recent issue of notes sold by the company bore a rate of 3¾% interest which rate exceeded the average rate on all the outstanding long term debt. Considering Colorado's contention that this indicated that future interest charges would exceed the weighted average cost of the entire outstanding debt, the Commission said, "But Colorado's contention presupposes that rate making is not a continuing process and that appropriate adjustments of rates cannot be made when experience demonstrates that adjustment is required. We find that the actual cost of the company's outstanding long-term debt and preferred stock is a proper measure of the cost of borrowed money and of preferred stock funds in determining a fair rate of return for Colorado in this case."

[9] Colorado had stated to the Securities and Exchange Commission that this debt would be retired on or before December 31, 1952.

While the Commission in its opinion states that there was "in this record an abundance of evidence on the subject of rate of return including average yields for bonds of public utilities, railroads and industrials as well as U. S. Treasury bonds; data on public offerings of natural gas bonds, preferred and common stocks; earnings-price ratios of various natural gas companies' common stocks; natural gas companies' capitalization ratios and data as to Colorado's outstanding securities, its earnings and financial requirements.", it is clear to us that no consideration was given by the Commission to factors other than the financial history of nine natural gas companies subject to the Commission's jurisdiction, whose common stock was held by the public, and seven natural gas companies, whose common stock was traded on recognized exchanges, and the data with respect to Colorado's outstanding securities, its earnings and financial requirements.

From an objective study of the investor's appraisal of the common stock of nine natural gas companies held by the public during the five year period ending August, 1951, the Commission found that investors had required a return on the average on the issues sold to the public of 8.3%. Colorado calls attention to the fact that the exhibit reflecting this study does not contain the names of these companies nor does their name appear in the record. They are, however, the nine gas companies reporting to the Federal Power Commission and it is not contended the information reflected in the exhibit is not correct or that Colorado did not in fact know or could not ascertain which companies were included in the study. The Commission further found that the average earnings price ratio of the outstanding common stock of seven natural gas companies traded on recognized exchanges for the same period to be 8.2%, with the average for the last twelve months of the period of 7.5% and decreasing to 6.4% as of October, 1951, and that at the latest date shown by the record, July, 1951, the yield varied from 3.5% to 6.4%. The Commission also found persuasive evidence as to the cost of equity capital in the experience of Colorado itself. It alluded to the fact that two principal stockholder groups had offered 966,000 shares of its common stock for sale to the public; that this was the first public offering ever made of Colorado's common stock and represented 56% of the total stock; that the book value of the stock was $13.63 per share; that it was offered at $26.75 to net the selling stockholders $25.25 per share; that based on earnings for 1951 of $1.88 per share the earnings—offering price ratio was 7.03%, and the earnings—net price to the selling stockholders was 7.44%; that the public offering of this stock was oversold. Whether the Commission's finding as to fair rate of return is supported by that substantially required by the decisions must be determined from a consideration of these facts.

While it is true that the Commission allowed as an item of cost of service only the weighted average cost of Colorado's outstanding debt of 3.21% and allowed nothing additional because the most recent borrowing reflected a higher interest rate of 3.75%, we do not think this constitutes basic error. The 3.75% issue was included in reaching the weighted average of 3.21%. Sufficient was allowed as a cost of service to retire the entire outstanding debt. Of course, if there was evidence establishing an upward trend in interest rates, it should have been taken into consideration but apparently this one borrowing is all of which there is evidence in the record and of itself is not sufficient to establish a reasonable expectation of a future upward trend. We are of the further view that the record amply supports the Commission's finding that Colorado has no plans for and does not presently contemplate a refinancing program in the near foreseeable future. Under these circumstances, the Commission did not err in refusing to give consideration to the higher interest rate in this one note issue.

While as pointed out in *Power Commission* v. *Hope Gas Company*, 320 U. S. 591, and related cases, there is no single formula or combination of formulae which may or can be used in determining rates, and as further pointed out, pragmatic adjustments are of necessity involved in rate making procedure, there is a well settled basic principle concerning which there can be no dispute. The rate must be fair and reasonable and, as pointed out in the Hope case, such a rate is one that will produce enough revenue to pay operating expenses, provide for the capital costs of the business, and for a return to the equity owners "commensurate with returns on investments in other enterprises having corresponding risks." As stated by the Supreme Court in the Hope case, "By that standard the return to the equity owners should be commensurate with returns on investments in other enterprises having corresponding risk." The court there approved the method employed by the Commission in reaching its conclusion. It pointed out that the Commission had "considered the financial history of Hope and a vast array of data bearing on the natural gas industry, related businesses, and general economic conditions."

It would seem that the history and experience of other successful companies engaged in the production, transportation and sale of gas would furnish the best guide as to what was fair and adequate. True, there are many companies engaged in the production and transportation of natural gas which apparently were not considered. Most of these are not subject to the Commission's jurisdiction, no doubt because they are local in their operations and not engaged in interstate operations. The record warrants the statement that the Commission gave consideration to all interestate gas companies subject to its jurisdiction and comparable in operation to Colorado and to all such companies whose common stock was traded on recognized exchanges, as well as to Colorado's outstanding securities, its earnings and financial requirements. It also attached significance to Colorado's experience in the public offering for sale of 56% of its common stock. The fact that this offering was promptly oversubscribed is evidence of the standing of Colorado with the investing public and, if we must as urged by Colorado take into account that the eagerness to purchase this stock was induced in the belief of the future development of Colorado's resources, we must on the other hand not be unmindful that that manifested interest was in the fact of a rate hearing which might well, as it did, result in a decrease of rates.

We believe that the experience of other comparable gas utility companies, having a sound financial structure and long experience of successful operation, is a better criteria by which to gauge and determine the adequacy and fairness of rate of return than that of railroads, power transmission companies or other like utilities engaged in other fields and under other conditions and circumstances, or the rate of return on Government bonds or industrial bonds in unrelated enterprises. We do not say that such factors are not proper for consideration but on the other hand failure to give them weighty consideration does not in our opinion constitute reversible error on the record before us in light of the factors that were considered in this case.

While the rate of return of 5¾% is lower than any rate heretofore established which has been called to our attention, that in itself is not suspect nor may we overturn it merely because we as the trier of the facts might have established a higher rate. From the record we cannot say that a rate of return of 5¾% properly computed is unreasonable and therefore confiscatory.

The late case of *State Corporation Commission of the State of Kansas* v. *Federal Power Commission,* decided by the Eighth Circuit on July 20, 1953, in which the findings and order of the Commission were reversed and remanded in part for further consideration with respect to making additional findings, has been called to our attention. It is sufficient to say that in our opinion the two cases are distinguishable and that the facts in this case do not warrant similar treatment other than above indicated.

Summarizing, it is our conclusion that the Commission's findings and order based thereon are supported by the record save only with respect to its findings relating to the loss from the gasoline operations. The disapproval of its treatment of this item makes necessary further consideration by the Commission of the proper base of cost of service. It will also require further consideration of the item of federal income taxes as an element of the cost of service.