Service Date: December 19, 2024

BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Petition of ARROW LAUNCH SERVICE, INC., Petitioner, For An Order Requesting Less than Statutory Notice, Requesting Deferred Accounting Mechanism and Associated Surcharge.	DOCKET TS-240930 ORDER 01 GRANTING LESS THAN STATUTORY NOTICE; PETITION FOR ACCOUNTING ORDER; AND APPROVING SURCHARGE SUBJECT TO CONDITIONS

BACKGROUND

1 On November 26, 2024, Arrow Launch Services, Inc. (Arrow or Company) filed with the Washington Utilities and Transportation Commission (Commission) a petition requesting permission to defer recovery of assets and for the authorization of a surcharge (Petition). The Company serves marine vessels throughout the Puget Sound. The Company's last general rate case became effective in March 2023.

2 Arrow provides launch service to marine vessels throughout the Puget Sound and has a fleet of 13 boats used to provide this service. These vessels range in age, with the oldest being built in 1957 and the newest in 2001. The average age of Arrow's boats is 50 years, and all its boats have original engines. The original engines are Detroit Diesel Series 71 engines. These are two-stroke, tier zero diesel engines which were manufactured from 1938-1995. Tier zero diesel engines are also known as unrestricted diesel engines as they have no emission controls.

3 The Environmental Protection Agency has granted money through the Diesel Emissions Reduction Act (DERA), to assist in the replacement of tier zero diesel engines to either tier three or tier four diesel engines. Receiving DERA funding covers 40 percent of the cost to re-power. To qualify for the DERA funding a private company must have an approved sponsor. In this case Arrow has teamed with the American Lung Association, their approved sponsor.

4 Arrow's Petition has two requests. The first is for permission to defer recovery of costs associated with the re-power project to a future rate case. The second request is for authorization of a surcharge during the re-power project. The surcharge would have special accounting requirements and would be adjusted as the project progresses or if Arrow files for rates during the project. The timeline of the surcharge would match the timeline of the re-power project and is expected to last four to five years. Arrow's plan is to re-power three boats per year until the fleet has been completely re-powered.

5 The deferral for recovery is to make sure the assets are adjusted when the assets are added to tariff rates. There is no interest being carried against these assets for ratemaking purposes. The formula below lays out how the assets will be added to the Company asset listing when tariff rates are revised in a future general rate case:

Amount to be recovered = original cost – federal funding – principle from surcharge

6 The threshold for granting an accounting petition is extraordinary circumstances. Arrow contends that replacing the entirety of their fleet in a relatively short period, qualifies as such a circumstance.

7 The surcharge will be adjusted every year when a new line of credit is established and the previous loan is finalized, after receiving federal funds. Additionally, the amount of the surcharge will vary depending on the loan terms, loan amounts, fuel and maintenance cost savings. The surcharge is meant to provide adequate cash flow to service the capital line of credit during the project.

8 Each year a new construction loan will be used to finance the re-power project for that year. The construction loan will have a varying amount drawn on the loan during the year. The surcharge for this will be estimated at the average interest cost for the year, as during construction no principle is owed, just interest. At the end of the year when the boats are complete, and the federal funding received the loan will be finalized. The finalized loans will use a term of 30 years, matching the expected useful life of the engines. Below is an illustration of the financing of the project.

Year 1: Open construction loan only interest due to bank.
Year 2: Open loan interest + payment from finalized loan in year 1.
Year 3: Open loan interest + payment from finalized loan of years 1 & 2.
Year 4: Open loan interest + payment from finalized loan of years 1, 2, & 3.
Year 5: Open loan interest + payment from finalized loan of years 1, 2, 3, & 4.

9 Six months after the last loan is finalized Arrow must file for rates. This would remove the surcharge, allowing normal rates to recover the value of the assets not already recovered through the surcharge. Arrow may file for rates during this project, which may adjust the surcharge, but will not remove the requirement to file for rates six months after the last loan is finalized.

10 Calculating and updating the surcharge will have to happen throughout the project as interest rates will change, as new financing occurs each year. Finalized loans are for the project cost minus federal funds. The basic formula for calculating the surcharge is below:

Surcharge for open loan = average amount of interest due per month / average monthly operating hours.

Surcharge for finalized loan (construction cost – federal funds) = (loan monthly payment – fuel savings – maintenance savings) / average monthly operating hours.

Total surcharge = surcharge for open loan + surcharge for closed loan.

11 Commission staff (Staff) recommends that the Commission grant the Petition, subject to conditions. Staff believes that this project is prudent as the Company has a unique opportunity to replace its aged and inefficient power units with the aid federal funding which will cover approximately 40 percent of the project cost. This federal funding will be treated as contributions in aid of construction, reducing the asset cost to be recovered through rates. As mentioned previously, the tier zero diesel engines used in the Company's fleet are on average 50 years old and lack the emissions controls and fuel efficiency of modern engines. These engines are no longer in production and will become more expensive to service as time goes on. With the first boat already re-powered, testing is showing that fuel burn has reduced by approximately 20 percent. Also, the Detroit Diesel engines had an 8-year overhaul maintenance schedule. The new John Deere engines have a 15-year overhaul maintenance schedule, reducing operation and maintenance over the life of the engine. Lastly, the emissions from the tier 3 engines are drastically lower than tier zero emissions and would decrease by more than 60 percent. Given the age of the boats and their original engines, which are 50 years old on average, and considering the cost savings from the receipt of federal funds, along with the operational savings identified, Staff believes this project is prudent.

12 However, Staff believes some conditions are necessary, and recommend that Arrow shall be required to:

a. Account for project costs, federal funding, and funds received through any approved surcharge; this will allow the assets to be placed in service when a general rate case is filed.
b. Six months after the project is finalized, file a rate case and any rate filing during this project does not remove this requirement.
c. Account the surcharge revenue separate from general revenue. The surcharge can be updated throughout the project.

i. The surcharge for the open construction loan will cover only interest and will be calculated at the average interest due for the year.
ii. Any surcharge amount approved for a finalized loan will be for principal and interest, minus operational savings.
iii. Any principle recovered through the surcharge mechanism will offset the asset cost, just like any federal funding received, when the asset is recovered in general rates.

d. Set the amortization period of the re-power assets is 30 years.

e. File a report each year that the surcharge is in place, reporting the amount of revenue received from the surcharge, a listing of which assets were completed, and the most recent 12-months' maintenance and fuel costs.

13 The Company filed a request for less than statutory notice on December 9, 2024, along with its customer notice. Staff recommends that the Commission grant the request for less than statutory notice.

DISCUSSION

14 The Commission's long-time standard is that deferred accounting is an exceptional regulatory treatment, typically reserved for costs (or revenues) meeting the following conditions: (1) extraordinary circumstances beyond the Company's control; and (2) generating costs with material impact on the Company's financial results.[1]

15 First, we note that the opportunity to make this upgrade is dependent on grant funding, which will cover 40 percent of the project's costs. The availability of this funding is temporal, and not within the Company's control.

16 Second, we note the scope of this project involves making changes to the entirety of its fleet, and will unquestionably generate costs with material impacts on the Company.

17 In conjunction with the surcharge and its conditions, the Commission agrees with Staff that the Company's Petition, as filed on November 26, 2024, meets both conditions for an accounting deferral.

18 Generally, surcharges as they apply to regulated companies, including water companies, are designed for companies which have insufficient funds to respond to emergencies, to

[1] Wash. Utils. & Transp. Comm'n v. Pacific Power & Light Co., Dockets UE-050684 and UE-050412, Order 04, 123, ¶370.

replace or upgrade failing infrastructure, or to add plant to accommodate growth. A surcharge provides a commercial ferry company with a source of capital, provided by customers, to fund capital needs.[2] We find adoption of this framework as it applies to water companies is appropriate here. The surcharge proposed here is intended to cover the short-term cash flow needs of the Company while its engines are being replaced, with the majority of the assets' costs, net of federal funds and surcharge amounts received, to be recovered in a future general rate case. No company may collect a surcharge except by Commission order or approval.

19 We agree with Staff that the Company's ageing fleet is infrastructure in need of upgrades. We agree that the availability of the federal grant funds through the DERA program presents the Company with a unique opportunity to replace its aging infrastructure while mitigating the impact to ratepayers, which we weigh heavily in our decision. This proposed investment will lower emissions and operating costs, while increasing the fleets fuel efficiency and improving environmental impacts. The surcharge is designed to address the Company's short-term financing impacts during the pendency of the engine replacement project, and appropriately addresses offsetting factors. We find that, in consideration of these factors, the proposed surcharge, with the conditions proposed by Staff, are reasonable and in the public interest.

FINDINGS AND CONCLUSIONS

20 (1) The Commission is an agency of the state of Washington vested by statute with the authority to regulate the rates, rules, regulations, practices, accounts, securities, transfers of property, and affiliated interests of public service companies, including commercial ferry companies.

21 (2) Arrow is a commercial ferry and public service company regulated by the Commission, providing launch services to marine vessels throughout the Puget Sound.

22 (3) The Commission has jurisdiction over the subject matter of this proceeding and over Arrow.

23 (4) WAC 480-07-370(3) allows companies to file petitions including that for which Arrow seeks approval.

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[2] *See, e.g.*, WAC 480-110-455 describing the requirements for implementing water company surcharges.

24 (5) WAC 480-51-080 allows companies to file surcharge tariffs including that for which Arrow seeks approval. No company may collect a surcharge, or facilities charge except by Commission order or approval.

25 (6) Staff has reviewed the Petition, including related attachments.

26 (7) Staff recommends the Commission grant Arrow's Petition, subject to conditions.

27 (8) This matter came before the Commission at its regularly scheduled meeting on December 19, 2024.

28 (9) After reviewing Arrow's Petition filed on November 26, 2024, and giving due consideration to all relevant matters and for good cause shown, the Commission finds that the proposed surcharge is fair, just, reasonable, and sufficient and should be approved, subject to the conditions set forth in paragraph 12 of this Order.

ORDER

THE COMMISSION ORDERS:

29 (1) Arrow Launch Services, Inc. 's Petition for an Accounting Order is granted, subject to the conditions set forth in paragraph 12 of this Order.

30 (2) This Order shall not affect the Commission's authority over rates, services, accounts, valuations, estimates, or determination of costs, on any matters that may come before it. Nor shall this Order granting Petition be construed as an agreement to any estimate or determination of costs or any valuation of property claimed or asserted.

31 (3) The Commission retains jurisdiction over the subject matter and Arrow Launch Services, Inc., to effectuate the provisions of this Order.

DATED at Lacey, Washington, and effective December 19, 2024.

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DAVID W. DANNER, Chair

ANN E. RENDAHL, Commissioner

MILTON H. DOUMIT, Commissioner