



# Appropriateness of Rate and Service Regulation of Commercial Ferries Operating on Lake Chelan

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Report to the Legislature  
Pursuant to ESB 5894

**January 14, 2010**

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Thank you also to Senator Linda Evans Parlette, Representative Mike Armstrong, and Washington State Transportation Commissioner Elmira Forner for attending and helping focus the discussion at the public meeting in Chelan, and for their continued interest in the work of the UTC. The views expressed in this report are not necessarily theirs.

## **I. INTRODUCTION**

In 2009, the Legislature required the Utilities and Transportation Commission (UTC or Commission) to conduct a study of the existing state of commercial ferry regulation on Lake Chelan. Specifically, the Legislature stated: “Within its existing resources, the utilities and transportation commission shall study the appropriateness of rate and service regulation of commercial ferries operating on Lake Chelan. The commission shall report its findings and recommendations to the legislature by December 31, 2009.” (Chapter 557, Laws of 2009, §6 Chapter 557, Laws of 2009 (ESB 5894)). This report contains the Commission’s findings and recommendations, as directed by the Legislature.

In preparing this report, the Commission:

- Reviewed, by reference to historical documents, the history of regulation of ferry service on Lake Chelan;
- Reviewed the current legal framework for Commission jurisdiction over ferry service on Lake Chelan, including options for the Commission under existing law;
- Reviewed the current tariff and operations of the Lake Chelan Boat Company, the current operator of ferry service on Lake Chelan;
- Conducted two public meetings to receive the views of people in the Stehekin and Lake Chelan communities on the issues relating to rate and service regulation of commercial ferry operation on Lake Chelan;
- Solicited and reviewed written comments from the public, both by letter and by electronic mail, relating to rate and service regulation of commercial ferry operations on Lake Chelan;
- Reviewed recent correspondence between Stehekin residents and the Commission regarding ferry service and proposing a competing service; and
- Conducted interviews or otherwise solicited information from various stakeholders, including Lake Chelan Boat Company and various users of the ferry service.

This report first reviews the history of regulation of commercial ferry service on Lake Chelan and the legal framework within which such regulation takes place. It then summarizes findings relating to the current service, the views of stakeholders, and possible alternatives to the existing service. Finally, it provides the Commission’s recommendations.

## **II. HISTORY OF REGULATION OF FERRY SERVICE ON LAKE CHELAN – A CHRONOLOGY**

Lake Chelan is a long and comparatively narrow lake in Chelan County, Washington, located between mountain ranges amid beautiful scenery and idyllic surroundings. The unincorporated community of Stehekin, located on the northern end of the lake, is home to about 75 year-round

residents, and, for more than 100 years, has been a popular summer resort for Washington residents as well as tourists from outside the state. Holden Village is a community of similar size located 12 miles from Lucerne, a boat landing on the lake's eastern shore.

From the earliest days, there have been passenger ferries on Lake Chelan, operating between the city of Chelan, Washington, and Stehekin and Lucerne, and there have been numerous controversies about whether there should be competitive ferry service on the lake. This brief history is derived from the official reports of the UTC or its predecessor agencies.

### **1911 to 1929**

Regulation of passenger and freight ferry operations on Lake Chelan began in 1911, the year the Legislature created the Public Service Commission of Washington (replacing the Railroad Commission of Washington).

In Chapter 117, Laws of 1911, the Legislature defined both passenger and freight steamboat operations for hire as common carriers. The legislation:

- Required that “all charges made for any service rendered or to be rendered in the transportation of persons or property shall be just, fair, reasonable and sufficient”;
- Required ferries to “construct, furnish, maintain and provide safe, adequate and sufficient service facilities to enable them to promptly, expeditiously, safely and properly receive, transport and deliver all persons and property”; and
- Charged the new Public Service Commission to adopt rules and enforce the requirements of the statute.

The annual reports reveal some details about early passenger and freight steamboat companies operating on Lake Chelan.

In the early years after the 1911 legislation, the only carrier operating on Lake Chelan appeared to be the Columbia & Okanogan Steamboat Company, based in Wenatchee.<sup>1</sup> On September 30, 1912, the Public Service Commission ordered that company “to make Chelan Landing a regular scheduled landing point for passengers and freight from and after October 1, 1912.”<sup>2</sup> By 1914, another company was operating on the Lake, the Lake Chelan Transportation Company.<sup>3</sup> The following year, the Commission reports note the first appearance of a Lake Chelan Boat Company, based in Chelan, though the Columbia & Okanogan Steamship Company was no longer mentioned.<sup>4</sup>

According to Commission records, by 1921 a controversy arose among competitors for ferry traffic on Lake Chelan. Four companies, the Lake Chelan Boat Company, Lake Chelan Freight Company, Perry Boat Company, and Mohawk Boat Company, all reported as regulated

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<sup>1</sup> See *Third Annual Report of the Public Service Commission of Washington* 204-211 (1913).

<sup>2</sup> *Second Annual Report of the Public Service Commission of Washington* 98 (1912).

<sup>3</sup> *Fourth Annual Report of the Public Service Commission of Washington* 325 (1914).

<sup>4</sup> *Fifth Annual Report of the Public Service Commission of Washington* 254 (1916).

companies. Only one, the Lake Chelan Boat Company, had been operating (since 1918) year-round service. The others provided service only in the more remunerative summer months. In Docket No. 5254, the Department of Public Works (the latest incarnation of the Commission) commenced a proceeding naming all four boat companies as parties. The Lake Chelan Boat Company challenged the reduced summer rates of the other three boat companies, and the Commission found that reductions would result in rates that were “unjust, unfair, unreasonable, and unremunerative.”<sup>5</sup> In its opinion in this case, the Department summarized its analysis of the economics of ferry service on Lake Chelan:

The question was asked by some of the witnesses at this hearing and by counsel for the Perry Boat Company and the Mohawk Boat Company, “Why should the Department of Public Works refuse to permit these reductions: why should not the patrons of these companies be permitted to secure service as cheaply as possible?” This department has often been confronted by situations similar to that existing on Lake Chelan. Boat traffic in almost every part of the State of Washington is largely seasonal. A very large proportion of the traffic occurs during the summer months for the benefit of campers and tourists who desire to visit various points of interest and who ride the boats for the mere pleasure which it affords. There is a certain amount of traffic, however, which must be cared for by some carrier during the winter months and after the tourist and camping travel has ceased. If we were to permit companies to come upon the routes of the boat lines who furnish year-round service and skim off the cream of the business during the summer months when the traffic is heavy and the operation of the boats cheap and pleasant, it would result in bankrupting the boat lines that assume the duty of furnishing an all-year-round service. The testimony in this case was uniformly to the effect that the Lake Chelan Boat Company had furnished good, dependable and continuous service. Their boats are swift, and well adapted to the carrying of passengers. Their treatment of their patrons has been courteous and they have furnished an all-the-year-round service regardless of unfavorable conditions of weather and scarcity of traffic. If we were to permit a summer rate war at unremunerative rates it would in all probability result in bankruptcy to the boat lines, or at least a substantial deterioration in service and equipment, and the farmers and other residents residing along the shores of Lake Chelan would soon find themselves without a regular or dependable service of any character. While some of them seem to desire the lower passenger fare, yet when they consider that it might result in ultimately depriving them of an all-the-year-round service, we feel they will realize that the refusal of this department to permit rate cutting during the summer months is to their interest.<sup>6</sup>

In 1927, the Legislature revised the public service laws relating to ferry service, requiring ferry companies to seek from the Department of Public Works a certificate declaring that “public convenience and necessity” required their service.<sup>7</sup> The new law grandfathered existing companies by requiring that a certificate be granted if the company “was actually operating in good faith over the route for which such certificate [was] sought” as of January 15, 1927.

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<sup>5</sup> *First Annual Report of the Department of Public Works of Washington* 216 (1921) (containing copy of order in Docket No. 5254).

<sup>6</sup> *Id.*

<sup>7</sup> Chapter 248, Laws of 1927.

However, the law provided that in the event two or more steamboat companies were operating on that date, the Department must “determine after public hearing whether one or more certificates shall issue.” In making that determination the Department was directed to “consider all material facts and circumstances including the prior operation, schedules and services rendered by either of said companies, and in case more than one certificate shall issue, the department shall fix and determine the schedules and services of the companies to whom such certificates are issued to the end that duplication of service be eliminated and public convenience furthered.”<sup>8</sup>

The Department’s 1927 annual report lists Lake Chelan Boat Company among its regulated companies, with a footnote indicating that this company “ceased operations in 1927,” so it is not included in the report’s list of certified passenger and ferry steamboat companies. However, on October 4, 1927, the Department issued Certificate No. 34 to L. A. Moore and D. F. Harris for a passenger/freight ferry operation on Lake Chelan.<sup>9</sup> Less than two years later, on April 27, 1929, the Department of Public Works issued Order S.B.C. No. 81 authorizing the transfer of rights under S.B.C. Certificate No. 34 from L. A. Moore and D. F. Harris to Lake Chelan Boat Company.

### **1930 to 1980**

Since S.B.C. Certificate No. 34 was transferred to Lake Chelan Boat Company in 1929, there have been a few other applications for a certificate of public convenience and necessity to provide ferry service on Lake Chelan. In each instance the Commission has denied these applications for several reasons, as discussed below.

By mid-century, there were renewed efforts to inject competition into the ferry service market on Lake Chelan. In 1953, Harlan J. Eggleston, d/b/a Stehekin Ferry, applied for a certificate of public convenience and necessity to operate vessels for auto and truck ferry service between Twenty-five Mile Creek and Stehekin via Railroad Creek or Lucerne. Lake Chelan Boat Company, Inc. protested the application. There was support for both sides of the dispute. Testifying in support of the applicant was Mr. Gene Latimer, rear commodore of the Lake Chelan Yacht Club and chairman of the Recreational Development Committee of the Wenatchee Chamber of Commerce. Testifying against opening up the lake to new competitors were Mr. Ansel N. Snodgrass, Chelan agent for the Howe-Sound Company, which operated the mine at Holden, Washington, and Mr. Curtis M. Courtney, operator of a restaurant, tavern and U-drive establishment at Stehekin.

The Public Service Commission determined that Mr. Eggleston had only moderate financial ability, equipment, and experience to operate a ferry service and that his evidence was vague and inconclusive as to proper and adequate dockage and loading facilities. It concluded that neither Mr. Eggleston nor his witness provided evidence that the public convenience and necessity required authorization of his proposed service. The Commission determined that the territory he

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<sup>8</sup> *Id.*

<sup>9</sup> *Seventh Annual Report of the Department of Public Works of Washington* 344 (1928).

sought to serve was already being served reasonably and adequately by Lake Chelan Boat Company, and denied his application.<sup>10</sup>

In 1972, North Cascades Marine Travel, Inc., applied for a certificate of public convenience and necessity to operate vessels furnishing passenger and freight service between Twenty-five Mile Creek and Stehekin, serving intermediate points as well. The applicant argued that the proposed service was justified because there was, at that point, only one scheduled boat trip on Lake Chelan each day during the summer months; from November until April there was boat service only three days per week; more boat service was needed to serve persons using and living along Lake Chelan; that Holden Village could not be fully useful without more access for its constituents, and that more frequent boat service would be needed as the North Cascades National Park developed.

Again, the Lake Chelan Boat Company protested the application. Supporting Lake Chelan Boat Company at the hearing were a representative of the North Cascades National Park Service, the district ranger for Chelan Ranger District of the Wenatchee National Forest, and Mr. A. S. Buckner, a 60-year resident of Stehekin and operator of a grocery store at the upper end of Lake Chelan. In addition, several witnesses from the general public testified that the Lake Chelan Boat Company provided adequate service with an eye to expanding service when needed. Upon cross-examination, the applicant conceded that he was uncertain about its future finances and had not considered insurance, parking facilities, boat maintenance and storage. He also conceded that the number of passengers he estimated to carry was just an estimate based on “a general feeling” from watching lake travel, and, according to the hearing examiner, did not adequately answer questions regarding wages and sufficiency of staff.<sup>11</sup> The examiner issued an order denying the application, and the Commission affirmed his findings and conclusions, thereby denying the application.

Four years later, in 1976, another applicant, Virgil M. and Frances M. McClosky, d/b/a Wilderness Boat Company, sought a certificate to operate passenger and freight ferry service between Chelan and Stehekin, stopping at intermediate points. Lake Chelan Boat Company again protested the application. In 1975, and well into 1976, the applicant provided service for passengers, their baggage and some freight without seeking authority from the Commission. The McCloskys testified before a hearings examiner that they applied for a certificate so they could advertise their schedule. They claimed ignorance of having to obtain authority from the Commission before they could operate ferry service, although they were told previously by a Commission investigator that their operations were unlawful.

On March 23, 1977, the hearings examiner issued his findings of fact, conclusions of law, and proposed order denying the application. He found “many confusions and contradictions” in the testimony and different balance sheets filed in the two sessions of the hearing, and that he could

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<sup>10</sup> *In re Application of Harlan J. Eggleston, d/b/a Stehekin Ferry*, Order Denying Application, Order S.B.C. No. 290, Hearing No. SBC-135 (Feb. 1954).

<sup>11</sup> *In the Matter of the Application of North Cascades Marine Travel, Inc.*, Examiner’s Proposed Order Denying Application, Order S.B.C. No. 356, Hearing No. B-260 (June 1972).

not ascertain facts as to the financial condition of the applicants with any degree of certainty. Although the applicants claimed they carried insurance, they produced no insurance policy for the period up to the hearing dates and an insurance witness for the applicants later conceded that the policy had expired. Moreover, the hearing examiner heard expert testimony that the applicant's boat was unsafe for operation on the lake during certain weather conditions.

The testimony made clear that while Lake Chelan Boat Company did not fully satisfy some passengers' expectations, no one denied that its service was at all times dependable and reasonable. The Commission, in affirming the hearing examiner, commented on the economics of ferry service on the Lake: "Free enterprise as expressed by two witnesses . . . would render the established boat company a much weaker enterprise endangering its ability to serve; and while it has a large, safe and costly vessel, it would lose any opportunity to break even financially, thus greatly weakening the service to the people on the lake. All of the witnesses admitted it is vital to the area."<sup>12</sup>

### **1981 to present**

In October 1983, the Commission approved the transfer of S.B.C. Certificate No. 34 from Lake Chelan Boat Company to Lake Chelan Recreation, Inc. d/b/a Lake Chelan Boat Company, the company that holds the certificate today. Though Mr. Jack Raines, president of Lake Chelan Recreation, Inc., had two partners in the business when Certificate No. 34 was transferred to Lake Chelan Recreation, Inc., within two years he became sole owner of the business.

In 1997, Mr. James Courtney d/b/a Stehekin Boat Service, filed an application with the Commission for a certificate of public convenience and necessity to operate a commercial ferry service between points on Lake Chelan. Lake Chelan Boat Company protested the application because the authority requested overlapped its own under Certificate No. 34. As always, the burden of proof was upon the applicant to prove that the existing certificate holder had failed or refused to furnish reasonable and adequate service or had failed to provide the service described in its certificate or tariffs, to prove the existence of public necessity and convenience for additional ferry service in an area already being served, to prove financial ability and resources to run a new ferry operation for at least twelve months, and to provide safe service for all passengers.

The UTC held a prehearing conference in Olympia, followed by a public hearing in Chelan at which 18 witnesses testified. On June 22, 1998, a Commission administrative law judge entered an initial order denying the application, finding that the applicant did not meet its burden of proof on any points. On August 3, 1998, the UTC issued a 28-page order denying review and affirming the initial order point by point.

The Commission found lack of evidence to show that Lake Chelan Boat Company failed to provide reasonable and adequate service and lack of evidence of any unmet need for service on the lake. Instead, some testimony indicated support of the Applicant's proposal based on the idea

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<sup>12</sup> *In re Application of Virgil M. and Frances M. McClosky, d/b/a/ Wilderness Boat Co.*, Proposed Order Denying Application, Order S.B.C. No. 362, Hearing No. B-262 (March 1977).



that the proposed service would be “Stehekin-based” and “firm belief in competition.” “Speculation that some overnight Stehekin visitors might find Applicant’s proposed scheduled useful, and testimony by several Stehekin residents that they might sometimes prefer, and use, Applicant’s proposed service is not adequate evidence.”<sup>13</sup> In fact, “substantial competent evidence” was found to show that the company provided reasonable and adequate service to meet existing and foreseeable needs of travelers on Lake Chelan.

Regarding proof of financial fitness, the Commission determined that Stehekin Boat Service failed to demonstrate that it was financially fit and financially able to operate the proposed service for at least twelve months, in part because “Applicant’s ridership and revenue forecasts and other financial estimates were inaccurate, incomplete, and highly speculative. As well, the Applicant does not suggest the addition of its service will materially expand, or expand at all, current market demand for service. [It’s] financial analyses and general business plan depend on taking business from Lake Chelan Boat Company.”<sup>14</sup>

Ten years later, in late 2008, Mr. Clifford Courtney of Stehekin contacted UTC Executive Director and Secretary David Danner to describe various possible scenarios of boat transportation service and to ask various questions about services that he might provide that would not be subject to Commission regulation. Mr. Danner, on behalf of the Commission’s staff, responded, giving his opinion that the possible services Mr. Courtney described would require a certificate.

### **III. COMMISSION JURISDICTION OVER COMMERCIAL FERRIES**

#### **Legal framework**

*Certificate requirement and exemptions* - By statute, every person who wishes to operate a passenger vessel in Washington waters “for the public use for hire between fixed termini or over a regular route” must first obtain a certificate from the Commission “declaring that public convenience and necessity require such operation.”<sup>15</sup> The Commission may order any person operating without a certificate to cease and desist,<sup>16</sup> and if necessary, the Commission may enforce its order by petitioning the superior court for an injunction.<sup>17</sup>

Before granting a certificate, the Commission must find that the person or entity applying for the certificate is financially able to provide the service.<sup>18</sup>

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<sup>13</sup> *In the Matter of the Application of James Courtney d/b/a Stehekin Boat Service*, Commission Decision and Order Denying Review; Affirming and Adopting Initial Order, S.B.C. Order No. 549, Hearing No. B-78659 (Aug 1998).

<sup>14</sup> *Id.*

<sup>15</sup> RCW 81.84.010.

<sup>16</sup> RCW 81.04.510.

<sup>17</sup> RCW 81.04.260, RCW 34.05.578.

<sup>18</sup> RCW 81.84.020(2).

Various exemptions apply, some of which are explicit in the statute, and some of which are implied. Explicit exemptions include vessels under five tons gross,<sup>19</sup> and vessels primarily engaged in transporting freight.<sup>20</sup> The implicit exemptions include what might be termed “private carriers” and “excursions.” Because the statutory language only requires a certificate when a vessel is operated “for the public use,” the Commission has not required a certificate for services provided under private charter party agreements.<sup>21</sup> Similarly, boat tours or excursions that do not provide transportation either “between fixed termini” or “over a regular route” are also excluded from regulation.

The Commission advises caution when looking to the Commission’s rule on exemptions from the certificate requirement.<sup>22</sup> The reason is that the rule reflects a now-expired statutory scheme. In 1995, the legislature expanded the commercial ferry certificate requirement to include “excursions” (*i.e.*, a boat trip in which all passengers depart from, and return to, the same point), and also adopted an elaborate set of exemptions for certain types of excursions.<sup>23</sup> For example, one of the exemptions was for excursions operating in the waters of San Juan County with 49 or fewer passengers.<sup>24</sup> This excursion certificate requirement, including its exemptions, was repealed (by a sunset provision) effective January 1, 2001.<sup>25</sup> Consequently, a vessel operator describing its service as an “excursion” is only exempt to the extent that it avoids providing passenger transportation “between fixed termini” or along a “regular route.”

*Rate and service regulations* - Once granted a certificate for the provision of commercial ferry service, the operator’s rates and services are subject to regulation by the Commission.<sup>26</sup> This means that the operator must file with the Commission a tariff reflecting its fares and terms of service and must charge only in accordance with that tariff.<sup>27</sup> If the operator wishes to change its rates or terms, it must file an amendment to its tariff on 30 days notice to the Commission and the public.<sup>28</sup> The Commission may audit the company’s books and records and if the Commission is not satisfied that the rates reflected in the tariff are fair, just, reasonable and sufficient, the Commission may suspend the operation of the tariff amendments and initiate an adjudication to determine the rates and terms of service.<sup>29</sup>

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<sup>19</sup> RCW 81.04.010(12).

<sup>20</sup> RCW 81.84.010(1).

<sup>21</sup> *But see Kitsap County Transp. Co. v. Manitou Beach-Agate Pass Ferry Ass’n, et al.*, 176 Wash. 486, 30 P.2d 233 (1934) (enjoining an alleged charter party arrangement under which members of an association of passengers desiring automobile ferry service between points already served by a certificated passenger-only ferry).

<sup>22</sup> See WAC 480-51-022 (exempt vessels and operations).

<sup>23</sup> Laws of 1995, ch. 361.

<sup>24</sup> *Id.* § 3.

<sup>25</sup> *Id.* § 4.

<sup>26</sup> RCW 81.28, RCW 81.04.

<sup>27</sup> RCW 81.28.040, 080.

<sup>28</sup> RCW 81.28.050.

<sup>29</sup> RCW 81.04.130.

The Commission may revoke an operator's certificate if the operator fails to provide the service described in its tariff or if it fails to comply with the statutes and rules governing commercial ferry service.<sup>30</sup>

Protection against competition - Certificated commercial ferries enjoy considerable protection from competition as long as they continue to provide satisfactory service and comply with regulations. If a person applies for a certificate to initiate a new ferry service on a route or in an area already served by an incumbent certificate holder, the incumbent must be afforded notice and an opportunity to be heard.<sup>31</sup> More importantly, the Commission may not grant a certificate to operate in an area already served by an existing certificate holder, unless the existing certificate holder has failed or refused to furnish reasonable and adequate service, or the existing certificate holder does not object.<sup>32</sup> This statutory protection from competition applies not only against other private operators, but also against competition from new publicly-owned ferry services. Public agencies initiating service on the same route or between districts already served by a certificate holder must first acquire the rights granted under the certificate.<sup>33</sup>

### **Rationale for regulation**

The combination of statutory protection from competition, on the one hand, and stringent regulation of rates and terms of service, on the other, has historically been adopted for industries believed to have characteristics of a “natural monopoly.”<sup>34</sup> Such industries typically have very high capital costs, benefit from economies of scale, and provide an indispensable service to the public. With respect to these industries, the legislature has made a judgment that the public's interest in reliable and affordable service is best served by a single, economically regulated provider whose owners can make the sizeable investments needed to initiate and maintain service without the threat of having customers drawn away by a competing provider.<sup>35</sup> Other industries regulated under this model in Title 81 RCW are solid waste (garbage) collection companies under RCW 81.77, and auto transportation (fixed terminus bus) companies under RCW 81.68. The rate and service regulations that apply to these industries are intended to provide a surrogate for the pricing discipline that would be exerted by a competitive marketplace.

### **Options for regulation within existing framework**

Although the statutory framework favors a single, economically regulated provider, the Commission has some discretion as to how strictly it chooses to protect an incumbent provider from potential competitors. There are three ways for the Commission to allow some limited

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<sup>30</sup> RCW 81.84.060.

<sup>31</sup> RCW 81.84.020.

<sup>32</sup> *Id.*

<sup>33</sup> RCW 81.84.010(3).

<sup>34</sup> See, Charles F. Phillips, Jr., *The Regulation of Public Utilities*, pp. 49-73 (3<sup>rd</sup> Ed. 1993).

<sup>35</sup> See, *Kitsap County Transp. Co. v. Manitou Beach-Agate Pass Ferry Ass'n, et al.*, 176 Wash. 486, 489-91, 30 P.2d 233 (1934).

competition with an incumbent provider's service: (1) by defining an incumbent's protected geographic territory in a narrow fashion, (2) by concluding that the incumbent has failed to meet a public need that the applicant proposes to meet, or (3) by declining to require a certificate for certain types of boat transportation services that are arguably private rather than for public use. Any such conclusion must be supported by expert testimony in an adjudicative hearing. Applying these theories on Lake Chelan, it seems unlikely that under existing law any of these theories could be relied upon to authorize competing services on Lake Chelan.

Defining the incumbent's protected geographic territory - Shortly after the 1911 enactment of the incumbent provider protections of RCW 81.84.020, the Washington Supreme Court explained the type of factual inquiry it expected the Commission to make when determining whether an applicant's proposed service is "between districts and/or into any territory already served by an existing certificate-holder." Referring to the Commission's predecessor, the Department of Public Works, the court said:

The department has power to grant a certificate of necessity under certain conditions. Under certain other conditions, the department "shall not have power to grant a certificate." The question, what is territory already served, is a question of fact. Before that fact can be determined, it requires consideration of economic conditions, oftentimes involving expert testimony; a consideration of the kinds, means, and methods of travel; the question of population warranting additional facilities for transportation, or the possibilities of the additional means of transportation increasing the population so as to ultimately make the venture a success.<sup>36</sup>

In *State ex. rel. Puget Sound Nav. Co. v. Dept. of Public Works, et al.*, 165 Wash. 444, 6 P.2d 55 (1931), the court upheld a department order granting an application for a new certificate for a ferry route across Puget Sound. Despite the fact that the applicant's proposed terminus on the west side of Puget Sound, Port Ludlow, was already served by an incumbent certificate holder, the agency nonetheless concluded that the applicant's proposed service was not "between districts or into territory already served." The record at the hearing before the department apparently contained extensive analysis to support the conclusion that the new route and the competing route served distinct markets, despite the fact that the proposed route and the existing route shared the Port Ludlow terminus on the west side of Puget Sound and the two carriers' respective eastside termini, Ballard and Edmonds, were separated by a 10 mile trip by highway. The court reasoned:

Because a large, extensive, and populous territory is being served by a single ferry, such ferry does not thereby necessarily have a monopoly upon the whole of such territory to the extent that it must be held to be serving that territory to the exclusion of the establishing of some new ferry service at some other place therein advantageous to the public.<sup>37</sup>

Thus, while the Commission has some leeway to define separate markets based on

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<sup>36</sup> *Puget Sound Nav. Co. v. Dept. of Public Works*, 152 Wash. 417, 421-22, 278 P. 189 (1929).

<sup>37</sup> *Id.* at 452.

economic testimony, the court's willingness to uphold the Commission's finding appears predicated on the existence of a "large, extensive and populous territory" containing distinct markets and large population centers, including Seattle and Everett, on at least one end of the proposed route. By comparison, it seems doubtful whether any economic analysis could convincingly be advanced that the Lake Chelan Boat company, which appears to serve all available docking locations at both ends of the lake, has failed to serve some portion of a "large and populous territory."

Determining whether that the incumbent has failed to meet a public need that the applicant proposes to meet - Another way for the Commission to grant a certificate to an applicant that proposes to compete with an incumbent certificate holder is for the Commission to find that "the existing certificate holder has failed or refused to furnish reasonable and adequate service." No such finding regarding a commercial ferry has ever resulted in an appellate decision. However, in *Pacific Northwest Transportation Services, Inc. v. Washington Utilities and Transportation Comm'n*, 91 Wash. App. 589, 959 P.2d 160 (1989), the court upheld a Commission determination based on similar language in RCW 81.68 pertaining to auto transportation (bus) companies. The auto transportation statutes allow the Commission to grant a certificate over the protest of an incumbent provider only when the incumbent "will not provide service to the satisfaction of the Commission." The *Pacific Northwest Transportation Services* case concerns a challenge to a Commission order granting a certificate to operate a new bus service between Thurston County and Sea-Tac Airport with no intermediate stops in Pierce County. The application was protested by a certificate holder that already served between Thurston County and Sea-Tac, but whose route included intermediate stops at a hotel in Tacoma as well as door-to-door stops in Pierce County. The incumbent argued that a direct service between Thurston County and the airport, as proposed by the applicant, was not economically feasible. However, the incumbent presented no evidence in support of the contention. The Commission concluded:

Absent convincing evidence that it is not economically feasible to provide direct, expedited service between the Olympia area and Sea-Tac Airport, the Commission will conclude that Capital Aeroporter's failure to offer such service makes its service not to the satisfaction of the Commission.<sup>38</sup>

On this basis, the Commission granted the certificate over the incumbent's protest and the court upheld the Commission's order. Based on this case, it appears that the Commission could grant a certificate for a competing ferry service if there were convincing evidence that the incumbent was failing to meet a need for a particular kind of service (e.g., direct versus local service) and the incumbent was unable to present evidence showing that the proposed service was not economically feasible. However, unlike in this single case involving bus service in an urban or suburban environment, the geography of Lake Chelan and the economics of year-round passenger ferry service along a fifty-mile (one way) route with few potential docking locations

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<sup>38</sup> *Id.* at 593.

may offer little practical opportunity for different types ferry service on Lake Chelan (such as express versus local, or “door-to-door” versus fixed terminus).

Determining whether a ferry is operated “for the public use” – Still another way in which the Commission could potentially allow some degree of “competition” with the services of an existing certificate holder concerns its interpretation of the phrase “for the public use” in RCW 81.84.010(1):

No commercial ferry may hereafter operate any vessel or ferry *for the public use* for hire between fixed termini or over a regular route upon the waters within this state, including the rivers and lakes and Puget Sound, without first applying for and obtaining from the commission a certificate declaring that public convenience and necessity require such operation . . . .

Only common carriers – i.e., those who offer their services for public use – are required to obtain a certificate and submit to economic regulation by the Commission. Private carriers are excluded from regulation.

In transportation industries in which market entry is restricted, there have often been attempts by business owners or groups dissatisfied with the services of the public carrier to offer a private alternative to the regulated public service. One common scenario involves a hotel or resort providing transportation services for the exclusive use of its guests, either with its own vehicles or by arranging a “private charter.”<sup>39</sup> Another involves a third party (such as a travel agent) assembling a “private” group for the purpose of “chartering” a means of transportation.<sup>40</sup> The only court case concerning the limits of this sort of arrangement under the commercial ferry statutes is *Kitsap County Transp. Co. v. Manitou Beach-Agate Pass Ferry Ass’n*, 176 Wash. 486, 30 P.2d 233 (1934). In the *Kitsap* case, residents of Bainbridge Island unhappy with the services

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<sup>39</sup> *Terminal Taxicab Co. v. Kutz*, 241 U.S. 252, 60 L.Ed. 984, 36 Sup. Ct. 583 (1916) (holding that taxicab company that contracted with hotel to provide exclusive service to the guests of the hotel nonetheless came within regulatory statute applicable to common carriers for the conveyance of persons for hire); *Terminal Taxicab* was cited with favor on this point in *McDonald v. Irby*, 74 Wash. 2d at 436 (holding that owner of airport parking facility that also transported its parking customers to the airport terminal by van was a “common carrier” despite argument that it was primarily engaged in parking business); *Las Vegas Hacienda, Inc. v. Civil Aeronautics Board*, 298 F.2d 430 (9<sup>th</sup> Cir. 1962) (resort hotel that furnished air transportation to and from another city that in a manner that was only incidental to the promotion and operation of the resort hotel was, nonetheless, properly determined to be within regulatory statute applicable to “carriage by aircraft of persons . . . as a common carrier for compensation or hire.”); *M&R Investment Co., Inc. v. Civil Aeronautics Board*, 308 F.2d 49 (9<sup>th</sup> Cir. 1962) (Hotel-casino that sold “tours” to the public, including flights between Los Angeles and Las Vegas exclusively its guests was engaged in “carriage by aircraft of persons . . . as a common carrier for compensation for hire” and subject to regulation as such).

<sup>40</sup> *Horluck Transportation Co. v. Eckright*, 56 Wash. 2d 218, 352 P.2d 205 (1960) (enjoining a voluntary association or “club” of individuals that collectively owned a bus from operating between fixed termini without an auto transportation certificate under RCW 81.68 on the grounds that the law requires a certificate for transportation of persons for compensation between fixed termini); *Monarch Travel Services, Inc. v. Associated Cultural Clubs, Inc.*, 466 F.2d 552 (9<sup>th</sup> Cir. 1972) (a “social club” whose real business was selling tours and air transportation on chartered aircraft was required to have a certificate as an air carrier with the Civil Aeronautics Board); *Iron Horse Stage Lines, Inc. v. Public Utility Commission of Oregon*, 125 Or. App. 671, 866 P.2d 516 (1994) (holding that as long as the group of passengers contracting for “private” carriage is assembled by a third party agent, even if the only purpose for assembling as a group is to take a trip on the carrier’s bus, the carrier is deemed to be engaged in private carriage.)

of the incumbent certificate holder approached a second ferry company to enter into a charter party agreement for the use of an automobile ferry to carry members of their “private” association between Manitou Beach, on Bainbridge Island, and Seattle. Membership in the association was not restricted in any manner and there was only a nominal membership fee. The court enjoined the “charter” as a public ferry service infringing on the statutory right of the incumbent to be protected from competition unless it fails or refuses to provide reasonable and adequate service.

Despite the *Kitsap* case, there may be flexibility within the law for the Commission to take an expansive interpretation of the private carrier exemption from commercial ferry regulation. For example, the Commission might reasonably conclude that a boat service offered on Lake Chelan (and elsewhere) in conjunction with lodging at a particular hotel or resort, and which is not otherwise open to the public, does not require a certificate under RCW 81.84. However, if such an interpretation were shown to significantly threaten the regulated carrier’s ridership, revenue, and ability to provide reliable and affordable service, the Commission could also decide not to adopt that interpretation. In other words, the decision could be similar to a determination under RCW 81.84.010(2) as to whether the Commission should forbear from regulating a commercial ferry service that does not “serve an essential transportation purpose and is solely for recreation.” Under that provision, the Commission must determine that “the proposed service would not adversely affect the rates and services of any existing certificate holder.”

### **Obligation to ensure service if the certificate holder declines to provide service**

There is no legal obligation for state or local governments to provide ferry service if an investor-owned, regulated service provider declines to provide service. The regulatory scheme depends on the initiative of private investors to provide the service. As an inducement or encouragement for the private investment, the law affords a limited protection against competition as long as the private provider continues to provide a satisfactory public service. However, the fares charged and the terms of service are subject to regulation.

As suggested above, if a would-be ferry operator believes that a certificated commercial ferry is not providing service that is sufficient in terms of frequency, convenience, capacity, or other criteria, that person can apply for a competing certificate and thereby force the carrier to come forth with evidence as to why it is not feasible for the carrier to provide the service.<sup>41</sup> The burden of proof is on the competing applicant to show that the incumbent’s service is not sufficient.

Similarly, if the Commission believes that a commercial ferry service is inadequate or insufficient, it is empowered to conduct a hearing to determine what constitutes adequate and sufficient service, and may then order the carrier to provide that service.<sup>42</sup> However, it is a fundamental tenant of constitutional law that the Commission cannot require a carrier to provide a service on which it is unable to earn a reasonable return.

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<sup>41</sup> See, *Pacific Northwest Transportation Services, Inc. v. Washington Utilities and Transportation Comm’n*, 91 Wash. App. 589, 959 P.2d 160 (1998).

<sup>42</sup> RCW 81.28.240.

## IV. DESCRIPTION OF CURRENT FERRY SERVICE ON LAKE CHELAN

### Description of Current Service

**Summer Service** - During the summer months, the Lake Chelan Boat Company runs two boats from the city of Chelan to Stehekin – the Lady of the Lake II (Lady II) and the Lady Express. Tables 1 and 2 show the relevant schedules. Both boats depart from the company’s docks in Chelan and travel up-lake to Lucerne (Holden Village) and Stehekin. Passengers whose ultimate destination is Stehekin make up 76 percent of the company’s customers during the summer months.

The Lady II is the largest vessel in the company’s fleet. Launched in 1976, the Lady II can accommodate up to 285 passengers with a crew of four. The Lady II is also the only boat in the company’s fleet that makes intermediate flag stops along the lake.<sup>43</sup> Flag stop customers are typically campers and cabin owners (see Appendix 1 for complete route map).

#### **Lady II Itinerary; Summer Schedule**

<i>May 1 through October 15 Daily</i>	
Leave Boat Company Dock	8:30am
Fields Point	9:45am
Prince Creek	11:00am
Lucerne (Port of Holden)	11:45am
Moore Point	12:15pm
Arrive Stehekin	12:30pm
90 Minute Layover in Stehekin	
Leave Stehekin	2:00pm
Moore Point	2:15pm
Lucerne (Port of Holden)	2:30pm
Prince Creek	3:15pm
Fields Point	4:45pm
Arrive Boat Company Dock	6:00pm

**Table 1; Lady II Summer Schedule (current tariff)**

The Lady Express provides non-stop service between Chelan and the final destinations of Lucerne and Stehekin. The Lady Express cruises at about twice the speed of the Lady II and completes the trip up-lake in two hours. The boat can accommodate 150 passengers with a crew of three. It was added to the fleet in 1990 after a \$1 million investment by the company.

#### **Lady Express Itinerary; Summer Schedule**

<i>May - Saturday &amp; Sunday only June 1 through September 21 - Daily</i>	
Leaves Boat Company Dock	8:30 am
Fields Point	9:20 am
Arrive Stehekin	11:00 am

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<sup>43</sup> A *flag stop* refers to an on-demand stop selected by a passenger or passengers to be either dropped off or picked up.



60 Minute Layover in Stehekin	
Leave Stehekin	12:00 pm
Lucerne (Port of Holden)	12:20 pm
Fields Point	1:45 pm
Arrive Boat Company Dock	2:45 pm

**Table 2; Lady Express Summer Schedule (current tariff)**

**Winter Service** – Table 3 below contains the company’s winter schedule. The only boat that operates after October 15 is the Lady Express. In the winter, the Lady Express provides service to the ports of Lucerne and Stehekin, on certain days of the week, and with no flag stops. In March, the Lady Express resumes daily service. Customers of the company during the winter are primarily Stehekin residents, who comprise between 80 to 90 percent of passengers in those months. About a third of all of the full-time residents of Stehekin are National Park Service (NPS) employees and their dependents. Because most of the lodging in Stehekin is closed for the winter, very few tourists venture to Stehekin in these months. Passengers traveling to Lucerne in the winter are almost entirely – about 98 percent – Holden Village visitors and staff. During the winter, the company makes only about 15 percent of its annual revenue from passenger fares.

**Lady Express Itinerary; Winter Schedule**

<i>October 16 - October 31 - Mon, Wed, Fri, Sat, Sun</i>	
<i>Nov 1 - Mar 14 - Mon, Wed, Fri, Sun</i>	
<i>Mar 15 - Apr 30 - Daily Service</i>	
Leave Boat Company Dock	10:00 am
Fields Point	10:50 am
Lucerne	12:00 pm
Arrive Stehekin	12:30 pm
60 Minute Layover in Stehekin	
Leave Stehekin	1:30 pm
Lucerne (Port of Holden)	1:50 pm
Fields Point	3:10 pm
Arrive Boat Company Dock	4:00 pm

**Table 3; Lady Express Winter Schedule (current tariff)**

**Lady Cat** – The Lady Cat is a reserve boat in the company’s fleet with a passenger capacity of 49 and a crew of two. It is a high-speed catamaran capable of making the 51-mile voyage to Stehekin in a little over an hour. The Lady Cat was in service from 1999 to 2005, at first making two runs a day from Chelan to Stehekin and later only one run a day prior to going out of service. The company discontinued service due to dwindling passenger counts that made operation of three boats uneconomical.

**Freight and Mail Service** – Besides passengers, the company carries freight and mail, revenues from which comprise about 10 percent of the company’s annual revenue. The company has a contract with the United States Postal Service to transport mail between Chelan and the uplake

destinations of Lucerne and Stehekin. The mail contract was renewed in July 2009 and is in effect through June 2013. The annual value of the contract is \$68,025.<sup>44</sup>

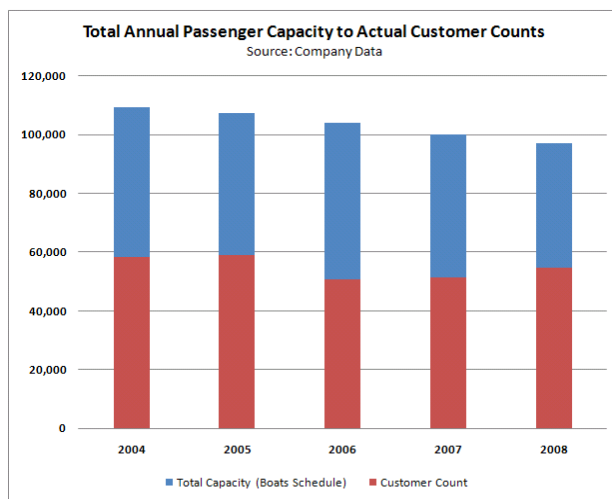
Freight for the last four years has averaged almost 1,800 tons per year. The company does not provide barge service. (Unregulated barge service is available on the lake to transport large items like vehicles and building supplies.) Combined, freight and mail comprise only about 11 percent of the company’s total annual revenue.

One interesting aspect of freight service provided by the company for up-lake residents (including Stehekin) is grocery delivery.<sup>45</sup> When up-lake residents need grocery items, they send a list and signed blank check with the down-lake boat. The Safeway in Chelan fills the order and the company sends an employee pick up the boxed orders daily. In the summer, the company averages five or six orders per week, with more during the holidays.

***Passenger Data*** – As required by state regulation, WAC 480-51-100, the company provides the Commission with an annual report that includes data on customer counts. It also provides data regarding its operations as part of the rate-setting process. From this data, it is possible to determine ridership by month and destination.

Figure 4 below illustrates total company capacity adjusted for changing time schedules and number of boats in service. Since 2004, capacity has been reduced by 11 percent in response to reduced demand. As Figure 4 illustrates, there is enough boat capacity remaining to handle additional passengers if increased ridership materializes.

Figure 5 illustrates capacity used by month. As expected, during the winter months only between 40 and 50 percent of capacity is used.



**Figure 4; Passenger Capacity to Customer Counts**

<sup>44</sup> Ray Luke, Acting Manager, Transportation Contracts, Seattle Branch Area Office, United States Postal Service.

<sup>45</sup> Lake Chelan Boat Company, Tariff Item 170

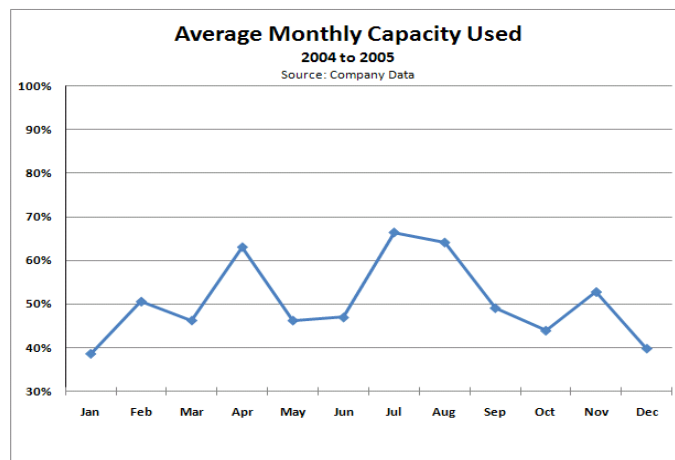


Figure 5; Average Monthly Capacity Used

**Financial Data** – The average annual revenue for the company since 2004 is just under \$1.5 million with 80 percent revenue generated from fares (the remaining 20 percent of revenues are generated by freight and other services such as parking, food, and souvenirs). Fuel, labor, and vessel depreciation comprise about 75 percent of the costs to provide service on the lake. Fuel costs alone comprise about 22 percent of the company’s expenses.<sup>46</sup> The Lady II and the Lady Express both consume over 200 gallons of diesel each in making the round trip up and down the lake.

From the data on passenger counts, capacity and finances, it appears that the company is challenged by relatively high fixed costs. Changing the configuration of the fleet with different boats is not a feasible option considering the large up-front capital costs and the company’s significant investment in its existing fleet. Table 4 shows the company’s round trip fare history.<sup>47</sup> Figure 6 and Table 4 provide a comparison between fares and actual company financial performance.

<i>Boat &amp; Destination</i>			Round Trip Fare History			
			2004	2005	2006 & 2007	2008 to present
Lady II Summer & Lady Express Winter	Stehekin		\$28.00	\$32.00	\$38.00	\$39.00
	Lucerne		\$25.00	\$29.00	\$33.75	\$35.50
	Commuter		\$21.00	\$24.00	\$28.50	\$31.20
Lady Express Summer	Stehekin	Regular	\$47.00	\$51.00	\$57.00	\$59.00
		Commuter	\$35.30	\$38.25	\$42.75	\$47.20
Lady Cat (service ended 2006)	Stehekin	Regular	\$92.00	\$96.00	\$105.00	n/a

<sup>46</sup> In the company’s most recent UTC rate proceeding, in Docket TS-090381, the commission on May 28, 2009, issued a “complaint against rates” to allow the commission to review the company’s rate structure. That matter is pending.

<sup>47</sup> While comparisons of passenger fares among different kinds of transportation services are difficult in this unique environment, one useful comparison may be the Internal Revenue Service’s mileage reimbursement rates. If Lake Chelan were a paved road, at \$.55 per mile, a round trip from Chelan to Stehekin by car would be reimbursed at \$56.10.

		<b>Commuter</b>	\$69.00	\$72.00	\$84.44	n/a
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Table 4; Lake Chelan Recreation, Inc. Fare History

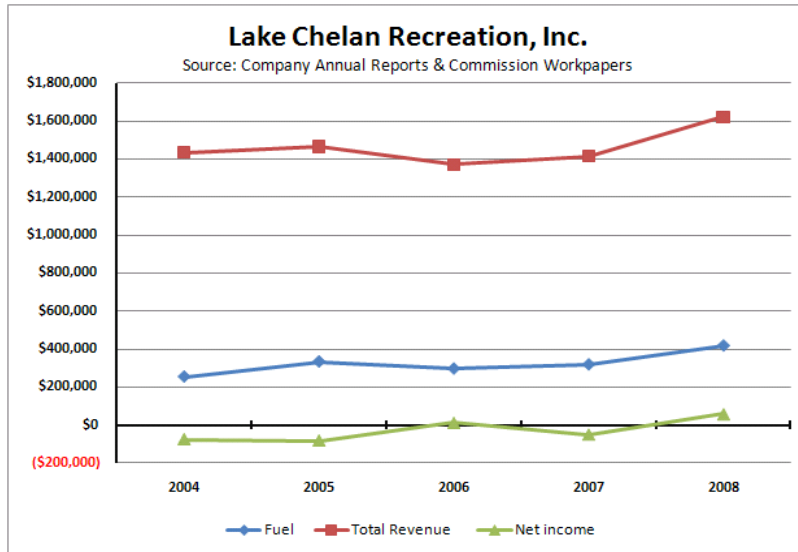


Figure 6; Lake Chelan Recreation, Inc. Financial Data

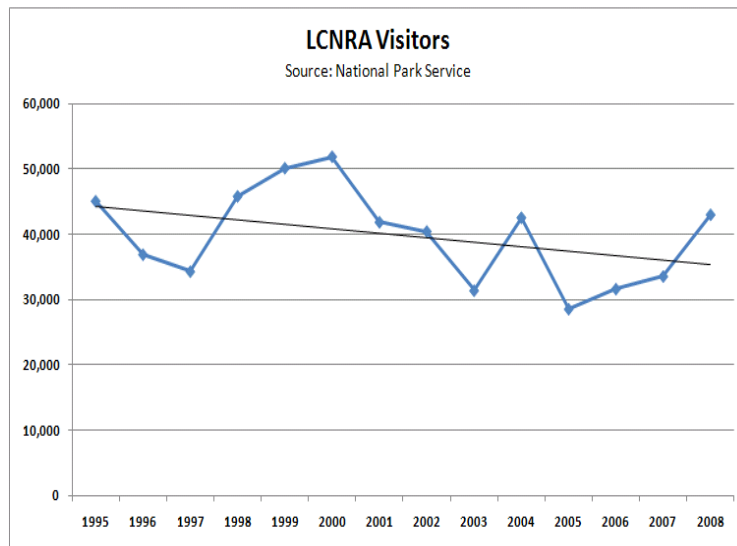
### Potential Factors Affecting Future Ferry Operations

It is difficult to predict future demand for ferry service on Lake Chelan. However, because so much of the ferry business, both passenger and freight, is related to up-lake land-based activity, we discuss possible activities involving the NPS and Holden Village.

The Lake Chelan National Recreation Area (LCNRA) is one of three units that make up the North Cascades National Park Complex. The other units are the North Cascades National Park and Ross Lake Recreation Area. More than 90 percent of the North Cascades National Park Complex sits within the protected lands of the Stephen Mather Wilderness, created by the Washington Park Wilderness Act of 1988 (Public Law 100-668). The Act excluded from the wilderness area a 100-foot corridor for the road that started at Stehekin Landing and went along the Stehekin River Valley for 23 miles, providing limited vehicle access to trails and campgrounds in that portion of the wilderness. According to the NPS, about 1,300 people a year access the upper portions of the road for camping and hiking.<sup>48</sup>

The community of Stehekin itself is inside the 62,000-acre LCNRA and more than a third of its year-round residents are NPS employees. According to the NPS, the LCNRA received almost 43,000 visitors in 2008. These visitors primarily traveled to the LCNRA on the Lake Chelan Boat Company's vessels. As Figure 7 illustrates, there is a downward trend in the number of visitors to LCNRA (about 10,000 fewer since 1995).

<sup>48</sup> National Park Service website, <http://nps.gov/noca>



**Figure 7; LCNRA Visitors**

In 2003 and 2006, major flooding along the river severely damaged large sections of the upper Stehekin Valley Road, making it impassable to vehicles. The NPS decided that it would not rebuild the road due to the expense and environmental damage that would result.<sup>49</sup> This decision by the NPS, while controversial to some, is not expected to have a significant impact on Lake Chelan Boat Company’s operations as access to the upper valley is still possible on foot for hikers and campers.

Since 2004, travel spending, according to the NPS, has remained constant in the LCNRA/ Stehekin area at about \$1.3 million annually. Annual travel spending for LCNRA/Stehekin comprises 0.42 percent of the total spending in Chelan County.<sup>50</sup>

*Future Activity at Holden Village* – In 1939, the Howe Sound Mining Company completed construction of its company town that would house 450 workers and their families. The town was named after James Henry “Harry” Holden, who first made mining claims in the Railroad Creek Valley in 1896. In 1961, the mining company turned the site and town over to the Lutheran Church, which converted it into a retreat through a special use permit with the National Forest Service (NFS).

Holden Village, or Holden, hosts an average of 6,000 guests and staff each year. All travel there on the Lake Chelan Boat Company’s vessels. Holden accounts for 23 percent of the company’s passengers and 7 percent of the total cargo tonnage hauled each year.

By 2011 or 2012, the NFS and Rio Tinto/Intalco, the successor to the mine’s original owner, expect to begin remediating the mine site where Holden is now located. During the two years that heavy construction is expected at the remediation site, Holden will remain open and host

<sup>49</sup> See National Park Service Project website at <http://parkplanning.nps.gov/projectHome.cfm?parkID=327&projectId=15383>

<sup>50</sup> Washington State Department of Commerce, Washington State County Travel Impacts 1991-2008, September 2009 shows Chelan County travel spending growing at an average rate of 6.8 percent per year.

workers from the project along with their own staff, who will be working on renewing the village's infrastructure. The project manager said he expects Lake Chelan Boat Company will not see any negative impacts to freight or passenger activity due to this activity.

### **Views of Stakeholders**

As part of this study, the Commission sought public comment regarding regulation of commercial ferry service on Lake Chelan. UTC staff compiled a mailing list of 50 people, including the president of Chelan Recreation, Inc., individuals who had commented on previous filings by the ferry company, local business owners, a director at Holden Village, city, state and county officials, and interested residents of the Lake Chelan area.

On Sept. 17, 2009, UTC staff mailed a letter to the list describing the study and report required by the Legislature. Recipients were notified of opportunities to comment at community meetings scheduled at Stehekin and Chelan, as well as the opportunity to submit written comments to the UTC. In addition, staff publicized opportunities to provide oral and written comments through a media advisory sent Oct. 9, 2009, to 20 radio stations and newspapers in the Lake Chelan/Wenatchee area. Staff prepared the following questions to assist people in formulating their comments:

1. Value provided from regulating exclusive operating rights, rates and service
  - a. What are the advantages and disadvantages to UTC regulation of ferry service on Lake Chelan?
  - b. What alternatives exist to UTC regulated ferry service on Lake Chelan?
2. Satisfied or not with the existing status quo
  - a. If you could change anything about the ferry service on Lake Chelan, what would it be and why?
  - b. What is it about the ferry service on Lake Chelan that you would want to see remain the same and why?

The Commission held two public meetings. The first took place at the community hall in Stehekin at 11:00 a.m., Oct. 19, 2009. The second took place in city council chambers in Chelan the same evening. The Commission accepted written comments until Nov. 6, 2009. Seventy-two people provided comments.

Comments came from people representing six geographical areas:

- Stehekin;
- Holden Village;
- Up-lake (areas and properties along the lake between Chelan and Stehekin that are inaccessible by road);
- Manson;
- Outside the general Lake Chelan area; and
- Chelan.

Advantages and disadvantages to UTC regulation of ferry service on Lake Chelan. Residents of Stehekin offered differing viewpoints on ferry regulation. Many supported the notion of an additional boat serving the lake. Several others said they would prefer all ferry service on the lake to be regulated. According to one Stehekin resident:

We fear that if transportation on Lake Chelan were cut loose from state oversight and regulation, the public service element would dwindle. Schedules, fares, baggage and freight rules all would be determined with both eyes on the dollar instead of with one eye on the common good.

Many people who expressed the need for competition did not say whether they thought the service should be regulated.

In Stehekin, some persons argued strongly for deregulation and competitive boat services. One said he has a 40-foot boat that can carry up to 20 passengers. He said the residents in Stehekin and along the lake have diverse needs and require a variety of services to meet those needs. He said;

I would recommend for consideration that Lake Chelan be deregulated, letting it be a free enterprise area that will thrive in the future.

Another proponent for deregulated services said the current service is inadequate and is depriving Stehekin of potential business. He said:

This system not only hampers the ability of the one certificated operator to run efficiently or make wise market-driven decisions, but it also excludes any competition which is the refining fire of the free market system.

He said he believes it is the U.S. Postal Service contract that currently keeps winter service running, not regulation. He continued:

I do not believe the state of Washington or any subdivision thereof needs to regulate the schedules or fees... demand will regulate the schedule and competition will regulate the price and the degree of excellence.

He said that running a smaller boat out of Stehekin will not hurt the current company, and that

By deregulating the lake the present company can be relieved of excessive regulation and become more agile in the marketplace and thrive in a competitive market if it will rise to the challenge.

The NPS sent written comments expressing concern about whether there could be more than one viable ferry service on the Lake. The NPS uses the boat to get to and from Stehekin. Its employees and their dependents account for about 34 of the approximately 75 year-round Stehekin residents, and many seasonal employees and volunteers. The NPS is responsible for the recreation areas that are a major reason for tourists to travel to Stehekin.

The NPS said “there is value in having regulated services on Lake Chelan” and that regulation “ensures some level of consistent service by which NPS can coordinate visitor activities.” It said:

[it is] unclear to us that there is sufficient business and demand to support more than one sustainable, financially viable commercial ferry operation. We are concerned that a

change in the current situation would not ensure reliable, dependable year-round service to Stehekin. Until an analysis satisfactorily demonstrates otherwise, the NPS believes regulation of these services is necessary to ensure visitor, park and NPS employee needs are met.

The Public Works manager of Holden Village spoke at the community meeting in Stehekin and sent written comments. He expressed skepticism about whether the demand for ferry service could support two ferry services. Stating that Holden Village accounts for at least 25 percent of the company's ridership, he recommended that the Commission consider future needs on the lake, and talked about a mine cleanup effort that is scheduled for 2011–2014, at an estimated cost of \$80 to \$140 million. Holden Village will remain open during the mine cleanup and will also be conducting renovations of some of its buildings in 2018–2019.

Regarding regulation and competition, he wrote:

Holden Village believes that competition is healthy and can result in improved services. Our caution with ESB 5894 is that Holden could be potentially the most negatively affected by the consequences of competition. It is easy to imagine that poorly regulated, competition could pick the low hanging fruit and not provide the scale of services Holden, in particular, needs, or can at least take advantage of at an affordable cost year round. Further, if competing services reduce the profitability of the service for the larger carriers, it can be speculated that they could improve their profitability by reducing off season service (or eliminate it) or increase their off season rates.

Regarding disadvantages of regulated boat services, he said:

Competition is limited, adjustment to service markets may not be done quickly and adjustments may not be considered if there is no competitive pressure.

The NFS commented that Lake Chelan provides access to hundreds of thousands of acres of national forest and national park lands that are accessible only by boat or float plane. Holden Village operates under a special use permit on national forest land and is one of the main gateways to wilderness areas in the Chelan Valley and to trails that connect to the Lake Wenatchee area and the Mount Baker-Snoqualmie National Forest. NFS employees travel on the lake to provide resource management activities including trail building, trail maintenance, fire fighting, and weed control. The NFS expressed concern that deregulating boat service on the lake could put it in a position of regulating the use of its docks, and said:

Our mission is to manage the natural resources on the public lands and not to be regulating public transportation. That is a role that is best handled by state or county governments.

The Commission received comments from a number of people outside the Lake Chelan area, who travel to or have traveled to Stehekin via the ferry. A few of these people mentioned that they would like all boat service on the lake to be deregulated. Two said they want competition, and all ferries operating on the lake should be regulated.

An employee of the boat company said that adding boat services on the lake would cut into everyone's ability to be profitable, drive rates up, and reduce services. The president of the boat company said that a mix of regulated and unregulated boats on the lake would require active



enforcement to ensure that the unregulated boats only served the ports it would be allowed to serve. He added that before boat service on Lake Chelan became regulated, there were many passenger boats that provided service and failed. Since being regulated, he said, “It has remained a dependable service.”

Alternatives to existing UTC-regulated ferry service on Lake Chelan. Several people from different areas suggested an exemption to regulation, similar to one that applies to some ferries in San Juan County.<sup>51</sup> The Public Works manager of Holden Village said some options to consider include a special district or county service, or state ferry service. A Stehekin resident asked whether the Link Transit system that serves Chelan and Douglas counties had been considered as a potential regulatory agency for the ferry service.

If you could change anything about the ferry service on Lake Chelan, what would it be and why? Many Stehekin residents said they would like to have a boat based in Stehekin. The main reason they gave is that the winter schedule makes it necessary for Stehekin residents to spend an extra day or two in Chelan for something as simple as a visit to a doctor or family member. Stehekin residents also mentioned the difficulty high school students (who must attend high school in Chelan) experience trying to come home to Stehekin on weekends. The current winter schedule requires students to leave school early on Friday and to miss school on Monday if they rely on the boat to commute home on weekends. Many Stehekin residents also said they are not pleased that the current winter schedule adds a day or two of travel time for visitors from outside the area.

Other suggestions included a desire for changes to tariff rules governing commuter discount ticket packages, greater accessibility for persons with disabilities, increased dock safety, and the ability to take pets into the passenger compartment of the boat.

Five up-lake property owners commented that they want flag stops in the winter. Three of them said allowing another boat to provide service would take care of the issue. One proposed a service charge for flag stops.

Six Manson residents commented that they want the boat to make a regular stop in Manson. Three said they thought allowing competition would accomplish this, though they did not say whether the service should be regulated.

Of the 29 out-of-area commenters, 20 said they had traveled to Stehekin on the ferry. Almost all said they would like to see more boat service on the lake, and many said regulated competition is needed. A few people mentioned that they would like all boat service on the lake deregulated.

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<sup>51</sup> The commenters’ reference apparently is to WAC 480-51-022 (4) (a) that exempts from the application of the rules in chapter 480-51 WAC, excursion services that: “*Originate and primarily operate at least six months per year in San Juan County waters and use vessels less than sixty-five feet in length with a United States Coast Guard certificate that limits them to forty-nine passengers or less.*” The term “excursion service” is defined in WAC 480-51-020 (13) as: “*carriage or conveyance of persons for compensation over the waters of this state from a point of origin and returning to the point of origin with an intermediate stop or stops at which passengers leave the vessel and reboard before the vessel returns to its point of origin.*” The commercial ferry service on Lake Chelan does not meet the definition of an excursion service.

What is it about the ferry service on Lake Chelan that you would want to see remain the same and why? The president of Lake Chelan Recreation said existing service is more than sufficient during all months, and that there is “over-service” in May, June, September and October. He said:

The months with over-service are the months with the greatest potential for growth. During most of these months Stehekin businesses are open. During the other months, facilities are closed or offer very minimal services.

Regarding safety issues, he said the Lake Chelan Boat Company

operates with the mindset that there is always a vessel at the dock (fueled and ready to go), and/or another vessel on the water running a schedule that could assist a vessel in distress.

Regarding the need for more boats to provide service to Stehekin in the winter, a boat company employee said Stehekin has not been open for winter activities in the 20 years he has worked for the company. He explained that the steel-hulled boat that is able to facilitate flag stops is not a good boat for the winter runs because it takes four hours each way, and would have to run in the dark; a safety issue.

A representative from the US Army Corps of Engineers said:

Our agency uses the current transportation system when we have work in the Stehekin area. We would want the system to always have regularly scheduled safe public transportation to Stehekin. The current system works well as far as scheduling for our needs.

## **V. DISCUSSION AND RECOMMENDATIONS**

The question of whether and how to regulate commercial ferries on Lake Chelan has been before the Commission repeatedly since 1927. In each case, the Commission has sought to ensure that residents who rely on ferry service have access to safest, most regular, and most reliable service possible.

Under current law, the Lake Chelan Boat Company has an exclusive right to provide commercial ferry service on Lake Chelan. That right, in the form of a certificate issued by the UTC, cannot be revoked as long as the company provides “reasonable and adequate” service and complies with law and Commission regulations.

We have reviewed the comments submitted, the testimony taken at two public meetings, and the Commission’s cases since 1927 addressing ferry service on Lake Chelan. We acknowledge that some customers of the Lake Chelan Boat Company, and some prospective customers, have legitimate desires for service levels above those now offered. These include:

- People who live along the lake and would like additional “flag stops”;
- Residents in or near Manson who would like a regular stop at Manson, and

- Residents of Stehekin who, from time to time, seek to take advantage of services available only in the city of Chelan, and who would like to avoid the two or three-day trip to access those services.

We also acknowledge a lack of consensus as to whether ferry service on the lake should be deregulated, and as to whether accommodation should be made for an additional ferry service provider to operate there. While some Stehekin residents and visitors argue for minimal regulation, others there, including residents, the National Park Service (the up-lake area's largest employer), and the National Forest Service, as well as residents and employees of nearby Holden Village, argue for continued regulation to ensure the continuation of current service levels, which they say are reasonable and adequate, though perhaps not optimal.

As discussed above, whether a service is "reasonable and adequate" depends on a number of factors, including the company's potential customer base, its costs, its actual and potential revenues, and the service to be provided. The small population of the communities along Lake Chelan, the long distances involved, and the costs of commercial ferry operations all suggest that it is not possible at this time for the Lake Chelan Boat Company to increase services without a significant increase in rates or ridership or both.

Because the Commission would likely find the company under these circumstances to be providing "reasonable and adequate" service, it is likely not possible under current law to carve out room for another operator to provide the higher level of services some residents and prospective customers would want.

Moreover, as a matter of economics, it is not desirable to suggest a change in legislation or regulations that would allow other entrants into the Lake Chelan ferry market. It is unlikely that another commercial venture could operate profitably providing niche services without also taking customers from the incumbent ferry operator, thereby putting at risk the incumbent's ability to provide essential, albeit basic, services.

Specifically, we envision three scenarios in which competitors would operate.

*Scenario 1: Niche services provided by competitors*

In the first scenario, a competitor would be allowed to operate a niche service, for example, a summer-only or a holiday-only service. In this case, the new entrant would be at a competitive advantage over the incumbent, who is burdened with the obligation to operate year-round and provide basic, essential service, including service at times when ridership is low and not remunerative. This obligation is not shared by the new entrant. As a result, the incumbent would lose customers and revenues to the new entrant, but would have to continue to meet its obligations under its tariff.

To make up the lost revenue and still provide basic service, the incumbent would have to petition the UTC to raise fares for remaining customers or further reduce the number of trips. That would create its own set of problems. Higher rates would likely result in hardship for the incumbent's captive customers – those who require services not provided by the niche provider and for whom the incumbent's service is the only available option. NPS, NFS, and Holden Village officials all commented that they relied on the year-round, regularly-scheduled service. The likely effect of allowing additional companies to “cherry pick” the most lucrative parts of the incumbent's service offerings would be to raise costs or reduce the availability of the incumbent's remaining services for those without other service options. The incumbent could also see reduced discretionary travel, both among Stehekin residents who, deterred by costs, would make fewer trips to Chelan, and tourists, also deterred by costs, who would forego visits to Stehekin in favor of visits to more convenient locales.

Moreover, as we have seen with other kinds of regulated service, areas with small customer bases are at higher risk of seeing a “death spiral” of repeated rate increases (and service reductions) followed by reduced ridership followed by more rate increases (and more service reductions). Eventually, the incumbent may be forced to raise rates to a level above what its customers can bear and may cease operation entirely. While another provider may be willing to step in to provide year-round, regularly-scheduled service, it would face the same economics if faced with competition from niche providers.

#### *Scenario 2: Full service by a second provider*

In the second scenario, the UTC (or Legislature) would authorize a second service provider subject to the same obligations as the first. Because the UTC would set the rates and imposes the same minimum service requirements on both certificated ferry services, competition would largely be based on other factors, such as convenience of schedule, on-board amenities, good will or other intangibles.

This scenario would be uneconomical for both companies and their customers. First, the new entrant would have to duplicate the infrastructure of the incumbent, and these capital and operating costs would be reflected in rates. Unless ridership were to double, an assumption we would not be willing to make given the distances involved and small population of the up-lake communities, both companies would see ridership below what the incumbent currently serves. Under this scenario, revenues for both companies would be insufficient to cover expenses, even with significant rate increases for both companies. One or the other company would cease operations, and face high stranded costs in doing so. It is unlikely the UTC would find the certification of a second provider in this scenario to be in the public interest.

As discussed above, the UTC has never granted a certificate to an applicant proposing competitive commercial ferry service. However, the Commission did once grant a certificate to an auto transportation applicant proposing to compete with an incumbent certificate holder on the grounds that “the existing certificate holder has failed or refused to furnish reasonable and adequate service.” That facts of that case were unique, and in

our minds, distinguishable from those on Lake Chelan. There, the incumbent made no attempt to provide evidence that it was economically unfeasible to provide the service proposed by the new applicant. That case involved airport bus service, for which the smaller start-up costs and lower operating costs mean a considerably lower risk that customers would be left without any service if a provider ceased operations. The companies operated in a highly-populous and growing urban and suburban territory, where both companies had potential to increase ridership.

By contrast, the geography of Lake Chelan and the economics of year-round passenger ferry service along a fifty-mile (one-way) route with few potential docking locations may offer little practical opportunity for non-exclusive regulated ferry operations. While we are not prepared to evaluate the reasonableness or adequacy of the incumbent's service outside of a full evidentiary proceeding, at first blush we believe the conditions on Lake Chelan are far different from those present in the airport bus case.

### *Scenario 3: Full deregulation*

In the third scenario, the UTC would fully deregulate passenger ferry service on the lake and, as one commenter phrased it, let Lake Chelan “be a free enterprise area that will thrive in the future.”

Economists and policy makers have debated the merits of regulating transportation services since the nineteenth century, and the discussion continues today. In 1921, the Washington State Department of Public Works, the predecessor agency to the current UTC, discussed the rationale for ferry regulation on Lake Chelan this way:

Boat traffic in almost every part of the State of Washington is largely seasonal. A very large proportion of the traffic occurs during the summer months for the benefit of campers and tourists who desire to visit various points of interest and who ride the boats for the mere pleasure which it affords. There is a certain amount of traffic, however, which must be cared for by some carrier during the winter months and after the tourist and camping travel has ceased. If we were to permit companies to come upon the routes of the boat lines who furnish year-round service and skim off the cream of the business during the summer months when the traffic is heavy and the operation of the boats cheap and pleasant, it would result in bankrupting the boat lines that assume the duty of furnishing an all-year-round service.<sup>52</sup>

To this day, this rationale still underpins the UTC's continued regulation of transportation services.

In the 1970s and 1980s, economists and policy makers at the federal level advocated for the elimination of regulation of transportation services. They argued that deregulation would lead to a healthy competitive environment, with increased service offerings and pricing and service

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<sup>52</sup> *First Annual Report of the Department of Public Works of Washington* 216 (1921), supra note 5.

options. Congress responded by deregulating a number of transportation services, including airlines, intercity buses, and railroads.

While it is not the purpose of this report to discuss the success or lack of success of those efforts, we do note a general consensus that deregulation has had the most adverse effect on smaller communities and rural areas, which lack economies of scale to attract risk capital or generate revenue sufficient to ensure profitability. One report stated, “While deregulation has created a class of beneficiaries, consumers in small towns and rural communities are not among them. Today, in many instances, they pay much higher prices for poorer service.”<sup>53</sup> It cited research showing that in the five years following the Bus Regulatory Reform Act of 1982, more than 4,500 small towns lost service, while fewer than 900 gained it. In the decade after the Staggers Rail Act of 1990, more than 1,200 communities lost rail service.<sup>54</sup> Even the leading proponent of transportation deregulation, Alfred Kahn, warned against removing economic regulation of services to small towns, saying “I’m not sure I ever would have deregulated the buses because the bus is a lifeline to many small communities for people just to get to the doctor or to the Social Security office.”<sup>55</sup>

Like buses prior to deregulation, the ferry services provided by the Lake Chelan Boat Company provide a lifeline to the communities of Stehekin and Holden Village. Faced with the question posed in 1921 – would these communities be adequately served by unregulated passenger ferry operators? – the present Commission could not say with confidence that they would.

In the short term, it is conceivable, and perhaps likely, that during the busy summer months customers would enjoy the benefits of competition among boat operators, who would lower fares and improve service to make their offerings more attractive to potential customers. During these periods, tourism may even increase as prices fall.

But we agree with our predecessors that, just as the intercity bus operators did in the 1980s, ferry operators would cease all unprofitable activities. With no legal obligation to serve, they would reduce or eliminate services during the winter months, or during times when fuel prices are high, or during times when more attractive business opportunities arise for the use of their boats or docking facilities. Even if revenues during the summer months would allow the operators revenue to serve year-round, they could not be expected to do so if such activities were unprofitable and they were under no obligation to provide them. In any event, it is not clear that summer operations would subsidize winter service if the operators were to lose market share during those months to seasonal competitors.

Moreover, the issue of safety must be considered. Because the purchase, maintenance and operation of ferry service is a costly venture (the purchase of the Lady Express alone was a \$1

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<sup>53</sup> Dempsey, *Flying Blind: The Failure of Airline Deregulation*, Economic Policy Institute (1990) at 37.

<sup>54</sup> Dempsey, at 79, n. 133.

<sup>55</sup> *Id.*, citing Kahn, Statement before the Aviation Subcommittee of the House Public Works and Transportation Committee on H.R. 11145, 8 (Mar. 6, 1978). *Aviation Regulatory Reform, Hearings before the Subcomm. on Aviation of the House Comm. on Public Works and Transportation*, 95<sup>th</sup> Cong., 2d Sess. 124 (1978), at 6337.

million transaction) we doubt that the opportunity to provide ferry service on Lake Chelan will attract more than a few operators that the Commission would deem “fit, willing and able” to provide service under current standards. While one commenter mentioned the availability of a 40-foot that could carry 20 passengers, the operation of ferry service must also take into account proper training, adequate insurance, drug testing for crew members, the ability to handle freight, and legal agreements to access docks and landings.

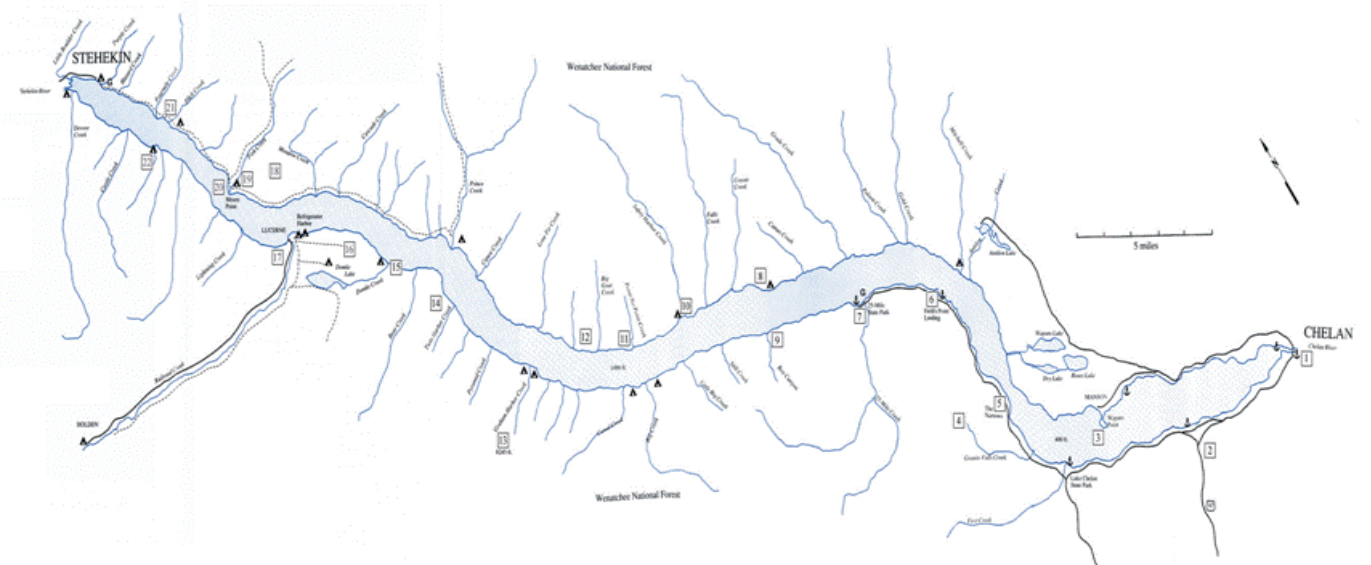
For these reasons, the Commission does not recommend at this time any changes to the state laws dealing with commercial ferry regulation as it pertains to Lake Chelan. The current system ensures that basic, year-round passenger transportation is provided between Chelan and the communities of Stehekin and Holden Village, the residents of which have no reasonable alternatives to ferry service for travelling to other locales.<sup>56</sup>

It may be that increased traffic in the future will enable the incumbent to provide more frequent service to customers and potential customers. The Commission should continue to monitor the company’s operations on a periodic basis and make recommendations for such expanded service where appropriate.

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<sup>56</sup> The commission also heard suggestions from commenters on possible ways the Lake Chelan Boat Company could improve customer service. These included changes to tariff rules governing commuter discount ticket packages, greater accessibility for persons with disabilities, increased dock safety, and the ability to take pets into the passenger compartment of the boat. The commission will explore these matters with the company.

# Appendix 1, Lake Chelan Boat Company Route Map (includes flag stops)



Up Lake Mileage			
7	Wapato Point	35	Point No Point
9	First Creek	31	Graham Harbor
11	Narrows	35	Pilinos Creek
18	Fields Point	37	Domika Falls
19	25 Mile Creek	43	Lucerne
22	Deer Point	48	Moore Point
28	Safety Harbor	51	Stehekin