

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In re Application of

MEI NORTHWEST LLC

For a Certificate of Public Convenience and  
Necessity to Operate Vessels in Furnishing  
Passenger Ferry Service

DOCKET TS-160479

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POST-HEARING BRIEF OF  
PACIFIC CRUISES NORTHWEST

April 12, 2017

## I. INTRODUCTION

1. MEI Northwest, Inc. (“Applicant” or “MEI”) requests a Certificate of Public Convenience and Necessity (“CPCN”) to provide launch service in Puget Sound at the Port of Anacortes.<sup>1</sup> This Commission has no authority to grant a CPCN to MEI under RCW 81.84.020(1) unless MEI proves that the existing certificate holder, Arrow Launch Service, Inc. (“Arrow”) “has failed or refused to furnish reasonable and adequate service.” Consideration of competition, as a broad public policy concept, is irrelevant in making this determination. MEI has provided no admissible evidence on its threshold requirement under RCW 81.84.020(1), so its application must be denied.

## II. ARGUMENT

### A. The Standard in RCW 81.84.020(1) is Limited to Adequate Service Consideration and Does Not Include Competition as a Factor.

1. *RCW 81. 84.020 reflects the Legislature’s Conclusion that the Public Interest is Best Served by Preserving Exclusive Service Territories for Certain Providers of Marine Transportation Such as Arrow.*
2. This Commission has found that launch services are regulated under RCW 81.84.010 in Order S.B.C. No. 364, *In re Application B-263 of Island Mariner, Inc.*, (Sept. 1977) Ex. No. SS-3. According to *Island Mariner*, because RCW 81.84.010 requires an operator of a “commercial ferry” between “fixed termini or over a regular route” to obtain a CPCN, a launch service provider like MEI needs a CPCN. That is because launch service providers meet the definition of a “commercial ferry” operator because they own “vessels” that operate a “launch service.” WAC 480-51-020. Launch service providers are regulated under RCW 81.84.010 *et seq.* the

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<sup>1</sup> Randy Esch, MEI’s president, testified that he thought his application was to provide service throughout the entire Puget Sound. TR 78:8-13. This contradicts the geographic scope set forth in the Commission’s published docket on June 28, 2016. Mr. Esch’s testimony on cross established MEI apparently really only seeks to serve the Port of Anacortes. TR 139:4-13. This intent is obvious because MEI excluded all costs of serving lower Puget Sound in its analysis. TR 136:24-25.

same way as the passenger-only ferry service offered by Pacific Cruises Northwest, Inc. (“Pacific Cruises”) because both operate “vessels” upon the waters of this state, albeit for different purposes. Hence, the experience and observations of Pacific Cruises, as expressed by Captain Drew Schmidt, DS-1T, provide relevant evidence for this Commission in ruling on MEI’s application.

3. No party in this proceeding contests that RCW 81.84.010 et seq. applies to MEI’s launch service operations. The Commission Staff’s analysis followed RCW 81.84.020. SS-1T. Accordingly, this proceeding should be resolved pursuant to the criteria of RCW 81.84.020(1), which forecloses competition for “commercial ferry” operators, including launch service providers operating between fixed termini, as long as the incumbent CPCN holder (Arrow) is furnishing reasonable and adequate service.
4. The legislative intent behind RCW 81.84.020(1) can guide the Commission in interpreting and applying RCW 81.84.020(1). *Rental Hous. Assn. of Puget Sound v. City of Des Moines*, 165 Wn.2d 525, 536, 199 P.3d 393 (2009). This can be ascertained by the plain language of the statute and by examining other provisions of the same act and related statutes. *In re Det. of Coffin*, 157 Wn.App. 537, 552, 238 P.3d 1192 (2010).
5. The plain language of RCW 81.84.020(1) expresses a preference for monopoly services not found in other provisions of Title 81, which govern the regulation of transportation providers in Washington. For instance, RCW 81.68.040 (auto transportation companies) and RCW 81.77.040 (solid waste collection companies) authorize competition in service areas if a certificated provider does “not provide service to the satisfaction of the Commission.” This standard is much broader than that of RCW 81.84.020(1):

[T]he commission may not grant a certificate to operate ..... into any territory .... already served by an existing certificate holder, unless the existing certificate holder has failed or refused to furnish reasonable and adequate service.

6. The Commission has found that these differences in standards were “intentional”<sup>2</sup> meaning that the Legislative direction in each calls for distinct considerations. The Commission found that the “satisfaction of the Commission” standard in RCW 81.77.040 did not limit its authority to the consideration of circumstances of inadequate service in *Stericycle*.<sup>3</sup> In that case the Commission approved competition for services for the disposal of biomedical waste based upon evidence that biomedical waste generators needed an alternative to the incumbent and marketplace benefits would result from competition in the unique, developing biomedical waste industry. [No such evidence was provided in this case, even if competition was a relevant consideration]. The incumbent’s service record was not a major factor. The affirming court carefully noted, however, that RCW 81.77.040 would continue to protect the exclusive service territory paradigm for neighborhood solid waste collection providers because “sound policy and economic reasons exist in favor of exclusive authority for typical residential or commercial collection in a specific territory.” 190 Wn. App. at 79.<sup>4</sup>
7. In contrast, RCW 81.84.020(1), by its terms limits the Commission’s consideration of MEI’s application only to whether the incumbent is providing adequate service, irrespective of the many public policy factors that might impact “the satisfaction of the Commission”, such as competition.
8. While RCW 81.84.020(1) may create a conditional monopoly it represents the legislative determination that competition in the commercial ferry business would be inimical to the best interests of the public at large unless the incumbent is not providing “reasonable and adequate

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<sup>2</sup> See *In re the Matter of the Application of Waste Management*, 2013 WL 3486911 (Wash. U.T.C. at \*3 (Docket TG-120033, Order 10, *aff’d Stericycle of Washington, Inc. v. Washington Utilities and Transportation Commission*, 190 Wn. App. 74, 359 P. 3d 894 (2015) (“*Stericycle*”).

<sup>3</sup> *Id.*

<sup>4</sup> Citing *Ryder Distrib. Res.*, Order M.V.G. No. 1596 at 6.

service.” The Washington Supreme Court explained this in *Kitsap County Transp. Co. v. Manitou Beach-Agate Pass*, 176 Wash. 486, 30 P.2d 233 (1934). There, the court construed the predecessor to RCW 81.84.020, in a case involving a request for a second CPCN to the predecessor to the Commission, from an association that wanted to run a second vehicular ferry service between Seattle and Manitou Beach on Bainbridge Island. The plaintiff held a CPCN to run the only Bainbridge Island-Seattle vehicular ferry. The court reasoned that no entity would be willing to serve the public and devote time, labor and money for a ferry operation unless it would derive revenues sufficient to support the operation. This investment would be jeopardized by competition unless the market could support more than one operator. In *Kitsap County Transp. Co.*, the court found that there were not enough revenues to support two ferry operations. In order to operate, the second ferry company would have to take revenues needed for the first company to operate, which would jeopardize all ferry service operations between Seattle and Bainbridge Island. The court enjoined the second CPCN saying:

To allow a competitor to enter the field would be to encourage ruinous competition which would be not only destructive of respondent’s rights under its certificate of convenience and necessity, but inimical to the best interests of the traveling public at large.

176 Wn.2d at 495.

9. *Kitsap County Transp. Co.* recognizes that because some services needed by the public may be natural monopolies, competition is not a viable regulatory option.<sup>5</sup> The same situation is present in this case so the same result should follow—denial of MEI’s application.

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<sup>5</sup> Judge Posner in “*Natural Monopoly and Its Regulation*,” 21 Stan. L. Rev. 548 (1969), explained: “Natural monopoly,” ... does not refer to the actual number of sellers in a market but to the relationship between demand and the technology of supply. If the entire demand within a relevant market can be satisfied at lowest cost by one firm rather than by two or more, the market is a natural monopoly, whatever the actual number of firms in it. If such a market contains more than one firm, either the firms will quickly shake down to one through mergers or failures, or production will continue to consume more resources than necessary. In the first case competition is short-

10. Having presented no evidence to satisfy RCW 81.82.020, MEI simply contends that competition is always good in support of its application. TR 190:14-20. Not only is this irrelevant to the factors this Commission must consider, it ignores the very real possibility of “ruinous competition”.
11. *Kitsap County Transp. Co.* identifies “ruinous competition.” *Id.* So does this Commission. *In the Matter of the Application of McNamara, Sean d/b/a Bellingham Water Taxi*, 2013 WL 1282511 (Wash. U.T.C.) (Docket TS-121253, Order 03), the ALJ refused to allow three operators of ferry services to serve the Bellingham-Friday Harbor route at the same time because it “could result in ruinous competition and threaten the economic viability of all operators.” *Id.* at \*11. In that case, a second commercial ferry operator, Pacific Cruises, offering a different type of service sought a CPCN for a direct Bellingham-Friday Harbor route. Pacific Cruises was not seeking an overlapping certificate within the meaning of RCW 81.84.020(1), unlike MEI.<sup>6</sup> At the time the incumbent certificate holder, Island Mariner, was not even operating but was in a state of Commission-approved discontinuance of service. Order 03 in Docket TS-121253 recommended *conditional* grant of CPCNs for the two applicants. The conditions were recommended because of the “inherent riskiness of start-up ferry operations and the economic realities in maintaining a profitable marine transportation business.”<sup>7</sup> *Id.*
12. Even with the conditions imposed in *Bellingham Water Taxi*, “ruinous competition” resulted. Captain Schmidt testified that neither Island Mariner nor another competitor, San Juan Islands

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lived and in the second it produces inefficient results. Competition is thus not a viable regulatory mechanism under conditions of natural monopoly.

<sup>6</sup> MEI’s application and proposed tariff shows that it plans to offer the same service as Arrow and in the same territories over time. RSE-4; RSE-10CX.

<sup>7</sup> 2013 WL 1282511 at \*11.

Shuttle Express, continued to operate on the Bellingham/Friday Harbor route. DS-1T 3:1-22. TR 325:22-362:13.

13. Captain Schmidt testified that two commercial ferry services cannot operate in competition due to the slim margins and extensive capital investment involved. DS-1T 3:23-4:3. In short, the market cannot sustain two “commercial ferry”/launch service providers serving the Port of Anacortes, which means that one or both providers could fail if MEI’s application were to be granted.
14. Hence, even if the Commission took into consideration the possibility of competition in the Puget Sound for launch service providers this case provides no factual basis for assessing the market for such competition. An inadequate market will lead to ruinous competition. Mr. Esch testified that the numbers of service providers that should be allowed in any service area depends upon “if the market can support it.” TR 94:3. MEI did not do a proper market analysis. MEI determined market demand based on the request of one customer only – Crowley Petroleum Services – and on an examination of Arrow’s financials. TR 94-96. Yet Mr. Esch rendered the self-serving conclusion that the Puget Sound market could support two launch service providers – but not three – in which case increased competition would have a harmful effect of decreasing service. TR 94-97:10.
15. Commission staff conducted no analysis as to whether market demand existed for additional launch services in Puget Sound or even the Port of Anacortes.
16. In sum, competitive considerations have no place under RCW 81.84.020(1). Even if they did, the record shows that increased competition in the marine transportation industry in Puget Sound has failed. DS-1T; TR 325:22-326:13, 328:8-14. There is no reliable, objective analysis in the record to establish a demand in the Puget Sound market for marine launch services

sufficient to support two successful launch service providers or that competition will benefit anyone but MEI.

17. MEI's application here illustrates the wisdom in the legislative choice made in RCW 81.84.020(1) to protect regulated "commercial ferry" operators from "ruinous competition" conditioned upon the provision of reasonable adequate service. This statute recognizes that the commercial ferry market demands significant outlay of capital for necessary infrastructure and that the market must provide the means to recover that investment, or no prudent entity would enter that market. The public interest is best served by ensuring that a provider of services of benefit to the public receives the assurance that it will be allowed to recover its capital investment. RCW 81.84 020(1) provides that assurance.
18. In turn, rate regulation provides the necessary protection for ratepayers that competition might otherwise provide for different services in different markets.

## *2. MEI's Cherry-Picking Does Not Serve the Public Interest*

19. MEI's applications presents a textbook example of cherry-picking.<sup>8</sup> Mr. Esch testified MEI selected the lower-cost, higher-revenue territory, Port Anacortes, to serve. TR 137: 1-6; 139:4-12. He identified the only customer MEI would serve as Crowley Petroleum Services, currently served by Arrow. TR 139:10-13. He said that this would result in a diversion of up to \$500,000 in Crowley revenues from Arrow to MEI. TR 142:1-5.
20. Mr. Esch acknowledged that a new competitor in a select, high-demand section of an existing provider's territory could impact negatively the existing infrastructure investment of that provider. TR 91:13-19. He did no analysis of this impact on Arrow or other customers in areas

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<sup>8</sup> Staff witness Scott Sevall testified generally that this term means that a competitor would only service during the high revenue portion of a season seeking only the most lucrative work leaving the less lucrative work to the incumbent. TR 252:12-253:1. While Mr. Sevall had no opinion as to whether MEI was "Cherry-picking" TR 254:3-4, MEI clearly intends to only serve low-costs, high revenue Port of Anacortes without assuming any obligations to serve higher costs areas.



MEI would not serve. TR 92:1-93:1. Mr. Esch testified MEI would be willing to operate at a loss for at least three years with a first year loss of \$93,000. TR 98:3-11.

21. The net effect of MEI's cherry-picking strategy would be to increase costs for customers outside of the Anacortes area that need to be served. A significant decrease in Arrow revenues, but the same level of expense to serve the entire service area, can only result in a rate increase for Arrow's customers for the areas not served by MEI. TR 253. MEI's willingness to operate at a loss for three years and to not raise its rates would force Arrow to match MEI's rates where MEI provides service. Ultimately, MEI's tactics could force Arrow into a death spiral, and Arrow, or possibly MEI, would close, leaving entire areas of Puget Sound unserved and launch service customers in the lurch.

**B. MEI Has Failed to Prove that Arrow has "Failed or Refused to Furnish Reasonable and Adequate Service."**

22. No one disputes that MEI bears the burden of proof in this case. TR 187:10-14, TR 268:4.<sup>9</sup> This burden requires MEI to prove that Arrow "has failed or refused to furnish reasonable and adequate service" under RCW 81.84.020(1), MEI's case-in-chief, Mr. Esch's testimony, contains only unsupported hearsay<sup>10</sup> statements from unidentified "clients that Arrow Launch is not providing the level of service" they want. RSE-1T 6:18. "Hearsay evidence is inherently weak; when it is as vague and incomplete as it is in this case, it cannot be relied upon as the basis for a decision." *In re Application E-75076 of Pro Transport, Inc.*, 1992 WL 12789783 (Wash.U.T.C.) at \*5.

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<sup>9</sup> "When it is said that a party has the burden of proof on any proposition, or that any proposition must be proved by a preponderance of the evidence, or the expression "if you find" is used, it means that you must be persuaded, considering all the evidence in the case [bearing on the question], that the proposition on which that party has the burden of proof is more probably true than not true." 6 Wash. Prac., Wash. Pattern Jury Instr. Civ. WPI 21.01 (6th ed.).

<sup>10</sup> See, e.g., RSE-1T 3:22-23; 4:23-24; 9:4-5; 10:1-4; 15:6-8; 16:6-8; 16:18-19; 18:22-24; 19.

23. On cross-examination, Mr. Esch said that his testimony about customers, other than Crowley, is no longer relevant. TR 198:10-18. He said that the only proof that he has to establish inadequate service is from MEI customer Crowley. TR 198:19-22. Mr. Esch then provided as “Crowley proof” a Shipper Support Statement signed by Marc Aiken. RSE-8.
24. Upon cross-examination, Mr. Aiken actually denied that Arrow has failed or refused to provide Crowley with adequate service:

Q So, basically, you’re not here today to state that Arrow has failed or refused to provide Crowley with adequate service so that this Commission would take action to allow another certificate-holder to serve in the marketplace?

A No. In fact, we have a very strong relationship with Arrow. We’ve used Arrow for many years. We’ve been happy with their service. There are periodic problems that we’ve had. Those are just problems of operation. I don’t want in any way this [sic] to slander or blind my relationship with Arrow Launch. No, I don’t have that knowledge.

TR. 383:14-25. Mr. Aiken testified that

- The Shipper Support Statement was based upon hearsay information from another Crowley employee, Lindy Evans. TR 348:7-15; 349:10-12.
- Arrow never failed to provide service to Crowley. TR 350:1-11.
- Mr. Aiken does not know if delays in launch service to Crowley were due to Arrow, as opposed to other factors, such as delays caused by others like ship chandlers. TR 368:1-8; TR 372:2-4.
- Crowley’s real motivation in supporting MEI is to get reductions in Arrow rates for ancillary services, such as forklifts and cranes, that are not regulated by the Commission. TR 350:14-22; TR 373:20-374:10.
- Crowley’s statements about its vendor’s need to provide prompt and reliable service on a 24-hour basis was no criticism of Arrow, which offers such service. TR 359:19-22.

- Crowley believes that competition is always better in a market assuming the market can support more than one provider, but Crowley does not know if that is the case for Puget Sound. TR 381:4-14, 21-25; TR 382:1-5.
- The source of Crowley's position was Lindy Evans, who became frustrated with Arrow's charges for ancillary services. TR 390:11-24; 391:1-23; 39:12-13.

25. In sum, nothing in RSE-8, as explained by Mr. Aiken, remotely establishes that Arrow "failed or refused to furnish reasonable and adequate service" to Crowley. The genesis of Crowley's issues with Arrow seems to arise from Lindy Evans, who MEI did not produce as a witness, leaving only hearsay evidence which never establishes any Arrow service quality issue.
26. The record contains no other evidence refuting Arrow's good service quality. MEI tries to argue that a 15-year-old personal injury case arising out of a one-time lease of a non-Arrow vessel bears on Arrow's service quality. RSE-6. This incident is irrelevant on several grounds. First, the time period for judging whether the current carrier provides service is the date of the application. *Pacific Northwest Transp. Services, Inc. v. Washington Utilities and Transportation Commission*, 91 Wn.App. 589, 598, 959 P.2d 160 (1998). So what occurred 15 years ago, even if it bore on Arrow's service quality, cannot be considered. Second, as a fair, practical evidentiary matter, the offer of a 15-year-old trial brief to prove the truth of the matter asserted (Arrow's poor service quality) about this remote, isolated incident should be disregarded under ER 401, 402, and 801.<sup>11</sup>
27. Staff presented no evidence of any Arrow service failure or refusal because no such record exists at the Commission, which has received no complaint against Arrow. SS-1T 6:1-16. Staff selected six Arrow customers and called them "about their experience with Arrow." SS-1T

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<sup>11</sup> ALJ Freidlander sustained an objection to the questioning of Captain Schmidt about this incident, finding that it was too remote to be relevant. TR 319:1-5.

7:1-16. Two were positive; three had no issues; and one was dissatisfied. *Id.* The dissatisfied customer was Lindy Evans from Crowley, who provided no basis for her dissatisfaction with Arrow. TR 249:1-12. Mr. Sevall testified, “Nobody here knows potentially what Crowley’s complaint is.” TR 266:17-18. Staff has not taken a position on whether Arrow has failed or refused to provide reasonable and adequate service under RCW 81.84.020, stating, “We will let the record stand as it is and let the judge interpret it and come to her conclusion without staff’s conclusions.” TR 268:13-15.

28. The only conclusion that can be reached is that this record contains no evidence that satisfies MEI’s burden of proof under RCW 81.84.020. There is no admissible evidence of even one customer complaint about how Arrow provides its regulated services.<sup>12</sup> Crowley’s Mr. Aiken joined the chorus of Arrow fans. Arrow presented first-hand, non-hearsay testimony from three customers establishing that Arrow provides reasonable and adequate service. Exs. DC-1T; VW-1T; DSC-1T. MEI fails on the dispositive element under RCW 81.84.020 and its application must be denied.<sup>13</sup>


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<sup>12</sup> An indication of dissatisfaction from one customer hardly establishes inadequate service. In *Superior Refuse Removal, Inc. v. Washington Utilities and Transportation Commission*, 81 Wn. App. 43, 9130 P. 2d 818 (1996) the court affirmed a Commission decision denying a second CPCN to a garbage collection provider under RCW 81.77.040 even though the record contained significant evidence that the incumbent had many customer complaints, violated its tariff and had serious billing problems.

<sup>13</sup> Mr. Sevall identified six purported examples where the Commission issued overlapping certificates. SS-2. These occurred 40 years ago as a result of the *Island Mariner* decision. Arrow president, Jack Harmon, explained the aberrational nature of the CPCNs due to the companies’ “grandfathering in” of operating rights as a result of *Island Mariner*. JLH-9T, 6-8. No Commission precedent since then supports issuance of overlapping certificates for launch services.

DATED this 12th day of April, 2017.

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**CERTIFICATE OF SERVICE**

I hereby certify under penalty of perjury of the laws of the State of Washington that on this date I caused to be served the original and one copy of the foregoing document to the following address via FedEx:

Steven V. King, Executive Director and Secretary  
Washington Utilities and Transportation Commission  
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I further certify that I have also provided to the Washington Utilities and Transportation Commission's Secretary an official electronic file containing the foregoing document via the WUTC web portal and served a copy via email to:

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DATED April 12, 2017, at Seattle, WA.

  
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