Memo

To: HHG Industry Participants in Tariff 15-C Rate Study (TV-190664)

From: Danny Kermode, Assistant Director for Water and Transportation
Greg Hammond, Regulatory Analyst

Date: Oct. 29, 2019

Subject: Tariff 15-C Review – Ratemaking Approach and Necessary Financial Data.

Commission staff is reviewing the current rates and charges in Tariff 15-C to determine what adjustments need to be made to account for increased expenses absorbed by the industry. For staff to determine the necessary adjustments to applicable rates and charges, staff recognizes the total cost of any move is driven by two main factors: an area's cost profile and the unique cost requirements of the move.

The cost profile of the area, e.g., High Cost Area or Low Cost Area, refers to areas having either a high cost of living, such as the metro Seattle area, or areas with a low cost of living, such as rural areas in Eastern Washington.

The second cost factor is the specific requirements of the move, *e.g.*, High Cost Move or Low Cost Move. Certain moves may only require basic equipment and entry-level workers, whereas, some moves may demand unique requirements such as specialized trucks or highly experienced workers resulting in high cost moves. For example, high cost moves can occur when the customer lives in an older home with non-standard doorways or stairs, or moves in neighborhoods with narrow streets or other vehicle restrictions.

Table 1 - Cost Matrix

Total Costs		Cost Area	
Matrix	Costs	Low	High
Cost Move	Low	Low	Average
	High	Average	High √

Of the four different cost combinations shown above in Table 1, only one is relevant for the purpose of staff's review, household good moves that are both in a high cost area and demand expensive equipment, apparatus, or labor resulting in a high cost move. The remaining three scenarios result in either average or low cost moves, which are not relevant to the determination of a maximum rate band adjustment.

This memo provides an accounting and audit plan to measure if the current tariff is providing maximum rates high enough to allow companies to recover costs and earn a profit when providing high-cost household good moves. After a review and analysis of the costs of selected services found in Tariff 15-C, staff will compare the computed costs, including allocated overhead, to the charges currently allowed.

Importantly, staff recognizes that companies will only accept certain jobs if the current rates for the service are sufficient, which limits staff's ability to use aggregated historical cost data because any analytical outcome would be skewed towards lower cost moves. Staff will instead use cost estimates using high cost scenarios or hypotheticals to estimate costs to provide services.

The selected rate item approach will be used to determine the direct costs of providing the various services, while the income statement approach will be used to determine the indirect costs, or overhead, as well as ensuring that companies are earning a reasonable return overall.

(A) Selected Rate Items Approach

Staff will use a sample approach to analyze the impact of cost increases since the last rate adjustment to Tariff 15-C. Staff will be working with three representative large moving companies[1] serving high-cost areas to analyze cost data from either actual high-cost moves or, if

[1] **Apex Moving & Storage, Hansen Bros. Transfer & Storage Company, and Mountain Moving & Storage**

not available, hypothetical high-cost moves. With the large number of individual tariff items, staff will focus on selected rate items that are both commonly used and material in amount.

Once each selected rate item's analysis is complete, the cost information will be compared to its related maximum rate band to determine the implied increase.

Working with the companies that agreed to provide data, staff will use the audit outline below to collect the cost information it needs to derive the direct costs portion of the selected tariff items.

(B) Selected-Rate Items Audit Outline

1. Mileage Rates (Item 200)
    a. These rates are used to compensate the company for the transportation (including loading and unloading) portion of a Long-Distance (Over 55 miles) HHG move.
    b. Costs include use of truck, employee hourly wages, fuel, and overhead.
        i. Traffic Congestion is the key variable on long-distance moves. The maximum rates should be set to allow recovery of costs when travelling through highly congested areas. Companies would then be able to estimate drive times based on past experience and charge the appropriate mileage rate.
        ii. In some cases, moves may require overnight stays, which would then add hotel costs and per-diem fees that would need to be recovered through these rates.
2. Hourly Rates (Item 230)
    a. Per hour charges that include packing and transportation of goods for moves under 55 miles.
    b. Costs include use of truck, employee hourly wages, fuel, and overhead
        i. Rates are based on the length of the job (Over or under 3 hours) as well as the number of workers.
3. Warehouse Handling Charges – Storage in Transit (SIT) (Item 100)
    a. Used to compensate for the cost of placing and removing goods in warehouse storage
    b. Costs include hourly wages and overhead
4. SIT Storage Rates (Item 100)
    a. Used to compensate company for using space in warehouse or storage facility
    b. Costs are primarily overhead
5. Container Rates (Item 196)
    a. Container prices should be easily verifiable by gathering invoices for the various types of packing materials. The container rates should also reflect a reasonable profit margin on top of the cost of the containers.
6. Packing Charges (Item 195)
    a. Rates include the cost of the carrier packing and unpacking the goods, as well as cartons and packing materials.
    b. Costs include cartons and other packing materials, direct labor, and some overhead.

(C) Income Statement Approach

To appropriately apply overhead costs to the rate bands, staff must examine the most recent income statements of the sample companies. Overhead, or costs that support the business operations as a whole, are not directly associated with specific moves. Those costs, often referred to as indirect costs, must be allocated to the various company divisions or functions and then to specific services using a rational activity measure such as employee or truck hours. Because many household goods companies also have non-regulated activities, such as interstate moves and permanent storage, allocations must be made to separate out non-regulated revenues and expenses.

Below is the audit outline staff will use to collect information needed to derive the appropriate overhead factor for the selected tariff items that are being reviewed.

(D) Income Statement Audit Outline

1. Total Revenues for the most recent year, separated by:
    a. Regulated and non-regulated revenues,
    b. Tariff rate item *e.g.*, Hourly rated moves, long-distance moves, packing charges, storage-in-transit, etc.
2. Schedules of overhead expenses for the most recent year should clearly reflect:
    a. Overhead separated between regulated and non-regulated expenses,
    b. Regulated overhead separated between function,
    c. Separation of general costs not clearly regulated or non-regulated should be accomplished by using:
        i. Direct allocation, or
        ii. Rational allocation factors, which may include:
            1. Employee Hours,
            2. Truck Hours,
            3. Shipment Weights,
            4. Miles Driven.
        iii. Revenue is never an allocator.
3. Proper allocation of costs will help properly apply indirect costs to the tariff items under review.
4. Staff will use allocators provided by the company to compute the appropriate portion of overhead costs to include in each rate unless it is clear the allocator does not result in a fair allocation of costs.

(E) Allocation of Overhead and Return on Investment

Once the company's direct costs and overhead are determined, staff will compare the total costs to the rate bands of those tariff items under review. This will also include recovery of credit card processing fees, as directed in Order 01 in docket TV-180245

Finally, staff will calculate a reasonable rate of return to be applied to each of the rates under review. Staff intends to apply the industry standard operating ratio of 93 to derive the return on investment and revenue requirement.

(F) Summary

The described financial and cost analysis of selected household goods movers and key tariffed items is expected to produce valid results within a short time frame using limited resources. We expect the results of the analysis to provide a sufficient range for the tariff rate bands, for all tariffed items, allowing recovery of costs and providing a return on high-cost moves in high-cost areas while allowing competition to drive fair consumer prices.