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June 21, 2024

SENT VIA WUTC WEB PORTAL

Jeff Killip
Executive Director and Secretary
Washington Utilities and Transportation Commission
621 Woodland Square Loop SE
Lacey, WA 98503

UW-240151
Received
Records Management
Jun 21, 2024

Re: ***In the Matter of Cascadia Water Tariff Revision (General Rate Increase),
Docket UW-240151***

Dear Director Killip:

The Public Counsel Unit of the Washington State Attorney General's Office (Public Counsel) respectfully submits these comments in advance of the June 27, 2024, Open Meeting of the Washington Utilities and Transportation Commission (UTC or Commission). These comments address Cascadia Water LLC's (Cascadia Water or Company) proposed general rate increase, effective July 1, 2024. Public Counsel participated in discussions with UTC Staff (Staff) and Company representatives regarding this case. We appreciated the Company's responses to informal data requests and willingness to discuss the issues in the case.

The Company requested an overall increase in revenues of \$1.8 million, or 75 percent, split between its Island (\$1 million), Peninsula (\$0.5 million), and Pelican Point (\$0.3 million) systems. Public Counsel understands that Staff and the Company are in discussions to file revised tariffs, but any agreement to do so would not substantially affect the recommendations offered in these comments.

Public Counsel's Recommendation

Public Counsel recommends that the Commission reject the Company's tariff filing, given that it derives from a return on equity (ROE) for which the Company has not produced affirmative evidence. The 12.0 percent ROE applied to the Company's proposed revenue requirement does not take into consideration its financial stability, unique ownership structure, and prevailing water industry conditions. If the Commission decides to approve the Company's filing, it should do so with a three-year phased rate approach and a rate base disallowance of \$793,082. Additionally, the Commission should re-evaluate the calculation of return on equity for water companies in a policy docket, stakeholder collaborative, or rulemaking.

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Failure to Produce Necessary Affirmative Evidence

Cascadia Water is a well-capitalized water utility operating in financial conditions far removed from the early 2000s. The Company's failure to make an affirmative showing justifying a 12.0 percent return on equity or a cost of debt of 10.5 percent is fatal to its filing. The Commission should reject the tariff amendments.

It is black letter law that a utility bears the burden of proof in any proceeding to rate increases.¹ This burden requires a utility to make an affirmative showing justifying a rate increase even in the absence of a challenge.² For justifying a rate of return and a return on equity, this means producing analysis and evidence of current conditions. Where the Commission extended a return on equity with a record that, "lack[ed] the depth and breadth of data analysis...on which the Commission customarily relies" it was a legal error for the Commission to approve a return on equity.³ This is consistent with *Bluefield*, where the court noted "a rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally."⁴

Here, the Company has made no attempt to propose a capital structure that was consistent with its underlying cost of capital. Instead, the Company's filing relied on Commission defaults, proposing a cost of debt of 10.50 percent (a 200 basis point premium on the prime rate in January 2024) and a return on equity (ROE) of 12.0 percent.

While the 10.50 percent cost of debt derivation is consistent with the Commission's policy on affiliated debt established in Docket UW-980072,⁵ the company offers no affirmative evidence that its proposed weighted cost of debt is consistent with the debt actually on its books. Meanwhile, the cost of equity proposed relies on a 22-year-old Commission precedent that the ROE for water companies is set at 12.0 percent.⁶ The Company has produced no affirmative evidence justifying this return on equity and the precedent in question does not account for current market conditions or the Company's financial stability and unique ownership structure.

¹ RCW 80.04.130(4).

² *Wash. Util. & Transp. Comm'n v. Puget Sound Power and Light Co.*, Dockets UE-920499 & UE-921262, Eleventh Supplemental Order, 19 (Sept. 21, 1993) (generally describing burden of proof).

³ *In re Puget Sound Energy & NW Energy Coalition*, Dockets UE-121697 & UG-121705 (*consolidated*), Order 15, 8, ¶14 (acknowledging a superior court order directing remand).

⁴ *Bluefield Water Works and Improvement Co. v. Pub. Serv. Comm'n of W. Va.*, 262 U.S. 679, 692 (1923).

⁵ *Wash. Utils. & Transp. Comm'n v. American Water Resources, Inc.*, Docket UW-980072, Sixth Supplemental Order, at 6 (Jan. 21, 1999).

⁶ *Wash. Utils. & Transp. Comm'n v. Rainier View Water Co.*, Docket UW-010877, Sixth Supplemental Order, ¶ 105 (July 12, 2002).

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The *Bluefield*⁷ and *Hope*⁸ standards require that a fair ROE should be (1) comparable to what investors expect on investments of similar risk in a competitive environment, (2) adequate to maintain financial integrity, and (3) sufficient to attract capital. With this in mind, it is critical that the authorized ROE for all regulated utilities, including water utilities, reflect current market conditions. Market risk and overall conditions have shifted since the Commission set the 12.0 percent ROE in Docket UW-010877 in 2002.⁹ Thus, applying the 12.0 percent ROE in this case without re-evaluation of market conditions is neither just nor reasonable.

Additionally, the Company's unique ownership structure insulates it from risk and reduces the need for a high ROE to attract capital. Cascadia Water, LLC, is a wholly-owned subsidiary of NW Natural Water Company, LLC, which itself is a wholly-owned subsidiary of Northwest Natural Holding Company. NW Natural Water currently serves 180,000 people through approximately 74,000 meters and provides operation and maintenance services to an additional 20,000 connections.¹⁰ It continues to expand through acquisitions, and as recently as June 5, 2024, announced the acquisition of another company that will add an expected 19,000 connections to its system at full buildout.¹¹ NW Natural Holdings is a publicly-traded company with a market capitalization of \$1.34 billion (as of June 20, 2024) and annual revenue of \$1.17 billion (for the 12-month period ending March 31, 2024).¹²

Cascadia Water itself demonstrates its financial stability through continued acquisitions. Since the Company was formed in 2018, it has acquired six other water systems which combine to make up more than 70 percent of the company's 4,001 connections. The Company's most recent acquisitions of Aquarius Utilities, LLC, and Northwest Water Services (both in August 2022) added around 1,400 connections to its system. In this case, the Company reaffirmed that it is "open to expansion and is continuing to look for the acquisition of other assets to further spread [improvement] costs."¹³ This is also supported by comments submitted by Goss Lakeridge Acres Association in this Docket, with an example of the Company seeking to acquire a small water system at distressed prices.¹⁴

In this context, given the Company's demonstrated stability, its financial backing, and changes in the Washington water industry since 2002, it is neither reasonable nor just for the Company to be

⁷ *Bluefield Water Works and Improvement Co. v. Pub. Serv. Comm'n of W. Va.*, 262 U.S. 679 (1923).

⁸ *Fed. Power Comm'n v. Hope Nat. Gas Co.*, 320 U.S. 591 (1944).

⁹ *Wash. Utils. & Transp. Comm'n v. Rainier View Water Co.*, Docket UW-010877, Sixth Supplemental Order, ¶ 105 (July 12, 2002).

¹⁰ NW Natural Holdings, *NW Natural Water Announces Acquisition of Puttman Infrastructure and Infrastructure Capital Holdings* (June 5, 2024) <https://ir.nwnaturalholdings.com/news/news-details/2024/NW-Natural-Water-Announces-Acquisition-of-Puttman-Infrastructure-and-Infrastructure-Capital-Holdings/default.aspx>.

¹¹ *Id.*

¹² Yahoo Finance, *Northwest Natural Holdings Company (NWN)*, <https://finance.yahoo.com/quote/NWN/>

¹³ Attachment 1 (Northwest Natural Response to Public Counsel Informal Data Request No. 4).

¹⁴ Comments from Consumer Goss Lakeridge Acres Association (GLAA) (filed June 20, 2024).

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allowed a 12.0 percent return on equity based on a 22-year-old precedent without its providing any affirmative evidence to justify such a return. Public Counsel does not propose a revised return on equity at this time; the burden is on the Company to provide affirmative evidence to justify one. Accordingly, in the absence of such evidence, the Commission should reject the Company's filing.

Phased Rate Approach

If the Commission decides to approve the Company's filing, it should do so with modifications that mitigate rate shock for customers. Under the Company's current filing, revenues increase by 75 percent, resulting in a similar increase in average monthly bills across the system as a whole.¹⁵ For customers in Cascadia's Island system (making up 38 percent of its customer base), average monthly bills would increase by 101 percent under these tariffs.¹⁶

In order to avoid rate shock and mitigate the impact on customers if this filing is approved, Public Counsel strongly recommends the Commission adopt a phased approach for this increase designed to gradually introduce the rate increase to water customers over the next three years, while also providing the Company with the rate relief it needs. This phased approach would be useful even if Staff and the Company reached an agreement to reduce the overall revenue requirement requested.

In developing our recommendation, Public Counsel examined the Commission's guidance contained in its Order 01 in Docket UW-180801. In that docket, Summit View Water Works had not submitted a rate increase in the 12-years since it had come under Commission regulation, and filed a proposed 34.4 percent rate increase to cover costs the Commission found to be just and sufficient. In its discussion and decision, the Commission stated:

The request for increased rates presented in this docket presents us with a difficult dilemma. The Company has demonstrated that it has experienced increased costs and made necessary investments that justify an increase in rates, rates that would be just and sufficient for the Company. However, as the Company has not requested an increase in rates in the 12 years since it came under Commission regulation, the resulting increase in rates is significant and could result in rate shock for customers. Under our guiding statutes, we must establish rates that are fair, just, reasonable and sufficient for both the Company and its customers.¹⁷

¹⁵ Under this analysis, systems with bimonthly bills are normalized to estimate monthly equivalents.

¹⁶ Attachment 2 (Average Monthly Bills).

¹⁷ *Wash. Utils. & Transp. Comm'n v. Summit View Water Works*, Docket UW-180801, Order 01: Allowing Revised Rates to Become Effective Subject to Conditions, ¶ 9 (Oct. 22, 2018).

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The percentage increase in the current docket is much larger than that sought by Summit View, and would likely still be larger under any agreement between Staff and the Company. In the Summit View case, the Commission expressed that it was “keenly aware of the impact the proposed 34.4 percent increase would have on domestic water customers.” The Commission identified rate shock as a primary concern when considering requested rate increases. To address potential rate shock, the Commission implements rate changes gradually to avoid rate shock.¹⁸ The Commission stated: “Concern about rate shock to the domestic water customers of Summit View is warranted in this case. An immediate 34.4 percent increase to the rates of these ratepayers is inconsistent with the Commission’s long-standing consideration of gradualism in rates.”¹⁹

If the Commission decides to approve the current filing, it should consider the need for gradualism and require the Company to phase in the rate increase requested. Public Counsel recommends adopting the same methodology used in the Summit View general rate case, with 55 percent of the rate increase incorporated in the first year of the effective tariffs and the outstanding increase recouped almost equally in the second and third years.

Applying this approach to the current Docket results in the revenue increases graphed in Attachment 3.²⁰ Using the overall revenue requirement from the Company’s current filing in this docket, the revenue requirement would increase by \$984 thousand (41 percent) in the first year, \$1.2 million (36 percent) in the second year, and \$12 thousand (0.3 percent) in the third year, and then decrease by \$426 thousand (9 percent) in the fourth year once the increase had been fully implemented. This phased approach would result in carrying costs of \$36 thousand, less than one percent of the Company’s proposed revenue requirement.

If Staff and the Company reached an agreement to reduce the revenue requirement requested, a one-time rate increase would likely still exceed a level consistent with the Commission’s consideration of gradualism. Additionally, a phased increase approach shorter than three years, like a 12-month approach, would be insufficient to mitigate rate shock, as it would require customers to pay rates even higher than without a phased approach within a year of the effective tariff date. An increase in rates greater than the one the Commission found troubling in the Summit View case would then be stretched over only a handful of months at the start of the 12-month period. Customers would not have time to adjust to these sharp increases. Finally, any agreement to reduce the revenue requirement would reduce the carrying costs associated with a three-year phased approach and make it an even more effective rate implementation option.

¹⁸ *Id.*, ¶ 10.

¹⁹ *Id.*, ¶ 11.

²⁰ Attachment 3 (Phased Rate Approaches).

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Public Counsel also submits examples of longer phased approaches, taking place over five and 10 years.²¹ Under these plans, though customers have more time to adjust to rate increases, there are a greater number of years in which they pay rates in excess of the original rates requested, and carrying costs are substantially larger.

In consideration of these factors, the Commission should be aware that the Company plans significant future infrastructure investment. Currently, of the Company's total \$9.9 million net plant in service, \$6.9 million, or 70 percent, was added to service since the Company's last general rate case three years ago in Docket UW-200979. Responding to a data request by Public Counsel, the Company indicated that it projects spending an additional \$15-20 million over the next five years solely to bring its systems' source and storage components into compliance.²² By the Company's own admission, this does not include additional expenses related to water main line replacement or investment needed for PFAS filtration or changes to standards for maximum contaminate levels. As evidenced in this case by projects including the \$793 thousand investment into the Del Bay mainline, which only serves around 40 customers, such additional expenses can be costly. In these conditions, the Commission should encourage the Company to be very thoughtful about staging its capital improvements so as to avoid unsustainable rate increases.

Del Bay Mainline Improvement Disallowance

As previously observed, the Company has made significant investments into the system's infrastructure in a short period of time since its last general rate case. Public Counsel reviewed much of this investment and in most cases has not found evidence suggesting imprudence. The one exception to this may be the Company's improvements to its Del Bay mainlines, which were placed into service on November 1, 2023, at a cost of \$793,082. The Del Bay mainline improvements are included in the rate base of the Company's Island system in this rate increase request.

Public Counsel identified seven major infrastructure improvements with a significant effect on the Company's rate increase request in this case. For each of those seven, Public Counsel requested that the Company provide detailed justification for the project, citing Washington State Department of Health compliance requirements where applicable. The Company's response to that request is attached.²³ Additionally, Public Counsel requested that the Company provide a list of infrastructure improvements which were required by a direct Department of Health order or were required due to overdue compliance with Department of Health standards. The Company's response to that request is also attached.²⁴

²¹ *Id.*

²² Attachment 4 (Northwest Natural Response to Public Counsel Informal Data Request No. 6).

²³ Attachment 5 (Northwest Natural Response to Public Counsel Informal Data Request No. 3).

²⁴ Attachment 6 (Northwest Natural Response to Public Counsel Informal Data Request No. 1).

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In its responses, the Company justified the Del Bay mainline improvement project by referencing “existing poor water quality on the Del Bay system as well as aging infrastructure, leaks and inaccessible main line locations.”²⁵ In neither of its responses did the Company cite a specific Department of Health compliance requirement that necessitated the mainline improvement, nor did it identify an immediate need for the improvement project.

Though Public Counsel is sympathetic to the need to replace aging infrastructure, a utility should weigh its prioritization of infrastructure improvements against the effect of those improvements on customers’ rates. If, as the Company indicates, it has an additional \$15–20 million in needed improvements, the Company needs to prioritize those projects which are strictly necessary for compliance over those that may be generally beneficial. The failure to do so is imprudent. Given the overall rate increase requested by the Company in this Docket, major improvements that were not immediately necessary should have been postponed to mitigate rate shock for customer in this general rate case. On the Island system in particular, where the Company’s proposed revenue requirement results in a rate increase of greater than 100 percent, infrastructure improvements should have been strictly prioritized.²⁶

In order to establish that Del Bay mainline improvements were immediately necessary, Public Counsel requested on June 11, 2024, that the Company provide evidence for its justification of the mainline improvements, but has not yet received a response.²⁷ Unless the Company provides evidence that supports prioritization of the Del Bay mainline improvements, Public Counsel recommends that the Commission disallow the associated \$793,082 added to the Island rate base, or require the Company to only begin recouping that investment in a future general rate case.

Return on Equity Policy Docket

Public Counsel notes that the Commission has previously expressed interested in opening a policy docket to revisit the UTC’s formula approach to water rate cases. Public Counsel has brought attention to, with acknowledgment from the Commission, the precedent that the return on equity for water companies was set at 12.0 percent in a rate case 20 years ago. This docket presents yet another example for why the UTC should take concurrent market conditions specific to each water company into account in calculating fair, just, reasonable, and sufficient rates.

²⁵ Attachment 5, ¶ 4. (Northwest Natural Response to Public Counsel Informal Data Request No. 3).

²⁶ Attachment 2 (Average Monthly Bills).

²⁷ Attachment 7 (Northwest Natural Response to Public Counsel Informal Data Request No. 14).

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Public Counsel made similar comments in the LakeLand Village Water Company rate case (Docket UW-210744),²⁸ Washington Water Service Company rate cases (Dockets UW-210560²⁹ and UW-230236³⁰), Suncadia Water Company rate case (Docket UW-220052),³¹ Gold Beach Water Company, Inc. rate case (Docket UW-220206),³² and Olympic Water and Sewer, Inc. rate case (Docket UW-230132).³³

It is critical that the Commission examine evidence of market conditions to develop a fair, just, and reasonable ROE for all water utilities serving Washington customers. Public Counsel does not recommend a specific methodology at this time, but requests that the Commission open a policy docket, stakeholder collaborative, or rulemaking to evaluate current policy and develop means to set ROEs that actually reflect evidence and market conditions while acknowledging the dynamics of large and small water companies.

Public Counsel appreciates the opportunity to submit these comments. If you have any questions about this filing, please contact Tad Robinson O'Neill via email at Tad.ONeill@ATG.WA.GOV or Stefan de Villiers via email at Stefan.deVilliers@ATG.WA.GOV.

Sincerely,



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²⁸ Comments of Public Counsel Unit, at 3–4, *LakeLand Village Water Co. General Rate Case*, Docket UW-210744, (filed Dec. 20, 2021).

²⁹ Comments of Public Counsel Unit, at 2–3, *Washington Water Service Co. General Rate Case*, Docket UW-210560 (filed Feb. 7, 2022).

³⁰ Comments of Public Counsel Unit, at 2–3, *Washington Water Service Co. General Rate Case*, Docket UW-230236 (filed Jul. 24, 2023).

³¹ Comments of Public Counsel Unit, at 2–3, *Suncadia Water Co. General Rate Case*, Docket UW-220052 (filed April 22, 2022).

³² Comments of Public Counsel Unit, at 3, *Gold Beach Co. General Rate Case*, Docket UW-220206 (filed June 24, 2022).

³³ Comments of Public Counsel unit, at 4–6, *Olympic Water and Sewer Inc. General Rate Case*, Docket UW-230132 (filed Dec. 1, 2023).