

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

IN RE: INTERSTATE NAVIGATION FILING TO :
RECOVER LOST EARNINGS BELOW THE 5.5% : DOCKET NO. 3762
FLOOR IN THE TRADITIONAL FERRY SERVICE :
RETURN ON EQUITY :

REPORT AND ORDER

In this docket, the Public Utilities Commission (“Commission”) approved a multi-year rate plan for Interstate Navigation Company (“Interstate” or “Company”), the result of an Amended Settlement that provided for a five year rate plan. The rate plan included a two year rate freeze through December 31, 2008. The rate plan then allowed for rate changes after December 31, 2008 to make inflationary adjustments and to allow Interstate to recover earnings if the return on common equity (“ROE”) fell below 5.5%.¹ The language relating to the ROE specifically states:

On or before November 15, 2008, 2009 and 2010, Interstate will file a report with the Commission detailing the earned return on common equity (“ROE”) for the twelve months ended as of the preceding May 31 (historic period). If the ROE, calculated using [an agreed methodology] is below 5.5% in the historic period, Interstate will be required to submit a report detailing the ROE calculated using [an agreed methodology]. If the ROE calculated using the [agreed methodology] is below 5.5%, Interstate shall be authorized to increase its traditional ferry service rates across the board, effective the following January 1, to collect over twelve months the revenue necessary to make up the difference between the ROE pursuant to [the agreed methodology] in the historic period and 5.5%, except that if the report detailing the earned ROE is not filed by September 1, the Commission will have the express authority to suspend any rate increase pursuant to R.I.G.L. § 39-3-11....²

At its hearing on December 12, 2006, the Commission reviewed the Amended Settlement and asked questions regarding the Settlement as a whole and the above-

¹ *Order No. 18957*, Appendix A (Amended Settlement Agreement), p. 7.

² *Id.* at 7-8.

referenced provision in particular.³ At its Open Meeting on December 27, 2006, the Commission approved the Amended Settlement.

On December 22, 2010, Interstate submitted the Pre-Filed Testimony of Walter Edge with supporting schedules, discussing the terms of the Amended Settlement as it related to the ROE calculation and requesting an increase in rates to recover a rate deficiency of \$159,906 (revenue deficiency plus gross receipts tax). Based on his calculations, Mr. Edge determined that Interstate had earned an ROE in FY 2010 of 1.8%, below the 5.5% floor that had been established in the Amended Settlement Agreement. The impact on rates would be an across-the-board increase of 1.92%.

On February 16, 2011, the Division submitted a Memorandum to the Commission recommending the Commission approve an increase to traditional ferry service rates of \$145,427, or 1.75% over a twelve (12) month period. The Division noted that in response to data request DIV-1-6, Interstate revised one of its calculations, resulting in the lower revenue deficiency.⁴ If approved, the impact on rates would be as follows: An adult round trip ticket would increase by \$0.30 from \$17.60 to \$17.90. A child round trip ticket would increase by \$0.15 from \$8.75 to \$8.90. Autos would increase by \$0.85 from \$47.90 to \$48.75. Pick-ups, trucks, vans and SUVs would increase by \$1.00 from \$57.80 to \$58.80. Freight rates would increase by varying amounts.⁵

On March 8, 2011, the Town of New Shoreham submitted a letter from Nancy O. Dodge, Town Manager, stating that: "The Town of New Shoreham acknowledges the Amended Settlement Agreement approved under Order No: 18957 and the provisions therein for an automatic ROE rate increase under certain circumstances." The Town

³ Order No. 18957, pp. 26-28.

⁴ Division Exhibit 2.

⁵ Interstate Exhibit 3.

further stated that it would “defer to the Division and Commission to determine in this matter whether the submitted financials support an increase and at what rate the increase should be.”⁶

On March 25, 2011, a public hearing was conducted at the Commission’s offices, 89 Jefferson Boulevard, Warwick, Rhode Island. The following appearances were entered:

FOR INTERSTATE NAVIGATION:	Michael R. McElroy, Esq.
FOR THE TOWN OF NEW SHOREHAM:	Christopher A. D’Ovidio, Esq.
FOR DIVISON:	Leo J. Wold, Esq. Assistant Attorney General
FOR COMMISSION:	Cynthia G. Wilson-Frias, Esq. Senior Legal Counsel

Interstate presented Mr. Edge in support of its filing. Mr. Edge stated that Interstate was seeking the effective dates of the increase to be April 1, 2011 through March 31, 2012. He suggested the Company would make a compliance filing in early 2012 to remove the increase effective April 1, 2012. Noting that the current rate plan ends December 31, 2011, Mr. Edge stated that he believed Interstate would be filing for a one-year extension through December 31, 2012. Therefore, if approved, there would be no general rate increase during the April 2011 through March 2012 period except for a potential inflationary increase, a potential exogenous event rate change, or another ROE related rate change. However, he did not believe these events would pose an obstacle to Interstate’s ability to reverse the requested rate increase that is the subject of this hearing.⁷

⁶ Town Exhibit 1. The Town did not sign on to the Amended Settlement.

⁷ Tr. 3/25/11, pp. 12, 15-21.

With regard to Interstate's adjustment to the deferred federal income tax, Mr. Edge explained that the Company had inadvertently used a rate that was lower than the one that should have been used. He explained that because the higher tax rate increases the deferred federal income tax which is a reduction to rate base, the return on rate base is reduced. Therefore, when one multiplies the weighted cost of equity by a smaller rate base, the result is a smaller profit and the smaller profit resulted in a smaller required rate increase.⁸

Finally, Mr. Edge agreed that if ridership were to be less than anticipated, Interstate would be at risk of not recovering the entire ROE shortfall through the currently requested increase. However, he believed that the risk of that happening lies with the Company and because the recovery period is limited to a twelve-month period, there would not be an opportunity to recover any additional funds from ratepayers.⁹

The Division made available John Bell, Rate Analyst V regarding the Division's review of Interstate's Petition. Mr. Bell stated that he had reviewed revised tariff filings designed to reflect Interstate's agreement to the Division's adjustment. Mr. Bell testified that the calculations appeared to be accurate.¹⁰

At the conclusion of the hearing, the Commission considered the evidence presented and approved a 1.75% increase to rates and further approved Interstate's revised tariffs (compliance filings) filed on March 25, 2011, finding them to be calculated in accordance with the terms of the Amended Settlement. The Commission further approved an amendment to the Amended Settlement in Section B.3, third sentence. The sentence originally stated, "If the ROE calculated using the same methodology set forth

⁸ *Id.* at 14.

⁹ *Id.* at 22.

¹⁰ *Id.* at 26.

in Section D.1.b, below, is below 5.5%, Interstate shall be authorized to increase its traditional ferry service rates across the board, effective the following January 1, to collect over twelve months the revenue necessary to make up the difference between the ROE pursuant to Section D.1.b in the historic period and 5.5%....” The sentence has been amended to state, “If the ROE calculated using the same methodology set forth in Section D.1.b, below, is below 5.5%, Interstate shall be authorized to increase its traditional ferry service rates across the board, effective the following January 1, to collect over twelve months *from the effective date approved by the Commission*, the revenue necessary to make up the difference between the ROE pursuant to Section D.1.b in the historic period and 5.5%....”

The Commission notes, as it did in Order No. 18957 approving the Amended Settlement, that the provision allowing Interstate to increase rates if its ROE falls below 5.5 percent is unusual. However, the Commission noted that Interstate is a small utility whose revenues are affected by the weather, but which, unlike the gas utility, does not have a weather normalization clause to protect its revenues from changes in the weather or other outside conditions. Because of this, the Commission found that an earnings floor provision was an acceptable part of Interstate’s overall rate plan. The Commission also noted that Interstate’s rate plan contained an earnings sharing mechanism to likewise protect ratepayers from excessive rates.¹¹

The Commission is cognizant of the fact that each of these mechanisms are designed to collect or refund through rates after the year in which the event occurred. However, the Commission finds that these provisions are exempt from the rule against retroactive ratemaking because the provisions were approved as part of a rate plan going

¹¹ *Order No. 18957* (issued 5/11/07), pp. 33, 35-36.

forward. These provisions created mechanisms which would protect both ratepayers and the utility from risks associated with a rate freeze. They were fully vetted during the course of the proceedings where the Commission reviewed the Amended Settlement. What Interstate is seeking in this filing and what the Commission is reviewing is whether Interstate properly calculated the new rates under the mechanism already approved in the Settlement. The Commission finds that, based on the Division's Memorandum, Interstate's data responses and Mr. Edge's testimony, the proposed 1.75% increase is a proper result.

Finally, because the 1.75% increase is meant to be temporary in nature, Interstate shall, on or before February 1, 2012, file compliance tariffs which will reduce the rates to remove the 1.75% increase approved in this Order for effect on April 1, 2012.

Accordingly, it is

(20383) ORDERED:

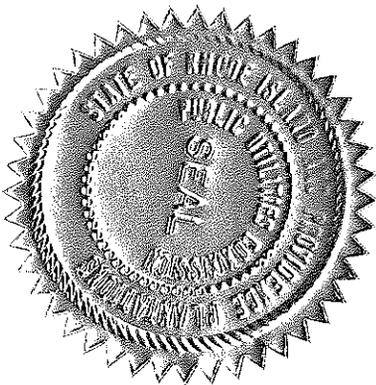
1. Interstate Navigation Company's Filing to Recover Lost Earnings Below the 5.5% Floor in the Traditional Ferry Service Return on Equity made on December 22, 2010 is hereby denied.
2. Interstate Navigation Company shall be allowed to increase its traditional ferry service rates by 1.75% for the twelve month period commencing April 1, 2011.
3. Section B.3, third sentence is hereby amended to state, "If the ROE calculated using the same methodology set forth in Section D.1.b, below, is below 5.5%, Interstate shall be authorized to increase its traditional ferry service rates across the board, effective the following

January 1, to collect over twelve months *from the effective date approved by the Commission*, the revenue necessary to make up the difference between the ROE pursuant to Section D.1.b in the historic period and 5.5%....”

4. Interstate Navigation Company’s compliance filings submitted on March 25, 2011, are hereby approved.
5. Interstate Navigation Company shall, on or before February 1, 2012, file compliance tariffs to reduce rates by the 1.75% increase approved in this Order.
6. Interstate Navigation Company shall comply with all findings and instructions contained in this Report and Order.

EFFECTIVE IN WARWICK, RHODE ISLAND ON APRIL 1, 2011,
PURSUANT TO A BENCH DECISION ON MARCH 25, 2011. WRITTEN ORDER
ISSUED JUNE 16, 2011.

PUBLIC UTILITIES COMMISSION

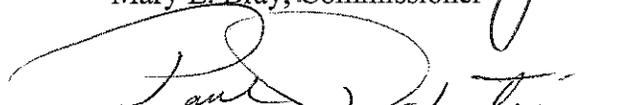




Elia Germani, Chairman



Mary E. Bray, Commissioner



Paul J. Roberti, Commissioner

NOTICE OF RIGHT OF APPEAL PURSUANT TO R.I.G.L. SECTION 39-5-1, ANY PERSON AGGRIEVED BY A DECISION OR ORDER OF THE COMMISSION MAY, WITHIN SEVEN DAYS (7) DAYS FROM THE DATE OF THE ORDER, PETITION THE SUPREME COURT FOR A WRIT OF CERTIORARI TO REVIEW THE LEGALITY AND REASONABLENESS OF THE DECISION OR ORDER.