

RRA Water Advisory

Major Rate Case Decisions — January – December 2019

During 2019, the average return on equity authorized in water utility rate cases trended upward, similar to the natural gas utility group, while the average delivery-only electric utility ROE remained largely flat year-over-year. In the past year, 13 water utility rate cases were completed, with traditional cost of capital parameters disclosed in just six cases, averaging 9.64%. This compares to 2018, when 22 cases were completed with 17 that included cost of capital parameters, averaging 9.43%. The natural gas ROE increased to 9.71% in 2019 from 9.59% in 2018.

For Detailed Data

Click [here](#) to see supporting data tables.

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Water utility rate case decisions —2019

State	Company	Order date	Decision type	Increase authorized				Common equity/total cap (%)	Test year end	Rate base (\$M)
				Rate increase (\$M)	Rate increase (%)	Return on rate base (%)	Return on equity (%)			
Hawaii	Hawaii Water Service (Waikoloa Resorts Utilities Inc.)	01/07/19	Settled	-0.05 W 1.75 WW	21.3	7.48	9.2	53.4	12/31/18	8 W 21 WW
Pennsylvania	The York Water Co.	01/17/19	Settled	3.36 W 0.29 WW		NA	NA	NA	02/29/20	NA
Maryland	Maryland American Water	02/05/19	Settled	1.45	31.3	NA	NA *	48.66	05/31/18	NA
West Virginia	West Virginia American Water Co.	02/08/19	Settled	18.7	14	7.21	9.75	49.79	12/31/17	650
Kentucky	Water Service Kentucky	02/11/19	Litigated	0.5	22	NA	NA **	NA	12/31/17	277
North Carolina	Carolina Water Service of North Carolina	02/21/19	Litigated	1.42		7.75	9.75	50.91	12/31/17	115
Pennsylvania	Aqua Pennsylvania	05/09/19	Settled	42.3 W 4.7 WW	9.8 W 34.6 WW	NA	NA	NA	03/31/20	NA
New Jersey	Aqua New Jersey	05/28/19	Settled	5.0	13	7.28	9.6	53.00	04/30/19	185
California	Golden State Water Co.	05/30/19	Settled	13.7	4.6	NA	NA	NA	12/31/19	899
California	Suburban Water Systems	06/05/19	Settled	4.9 '18 2.2 '19 2.2 '20	6.4 '18 2.7 '19 2.6 '20	NA	NA	NA	12/31/18	159
Kentucky	Kentucky American Water Co.	06/27/19	Litigated	13.4	15.7	7.69	9.7	48.76	06/30/20	444
Indiana	Indiana American Water Co.	07/01/19	Settled	3.8 13.7	1.73 6.07	6.17	9.8	53.41	04/30/19	1061
Texas	SWWC Utilities	10/16/19	Settled	4.6	NA	NA	NA	NA	12/31/16	12

As of Jan. 31, 2020.

In some rate proceedings, utilities tender a combined filing for water and wastewater tariffs.

W = water; WW = wastewater; NA = not available

* Case was resolved by a black box settlement with no traditional rate case parameters specified in the order. However, staff had recommended a return on equity of 9.9%.

** Return on rate base methodology was not used. Company was authorized an operating ratio of 88%.

Source: S&P Global Market Intelligence

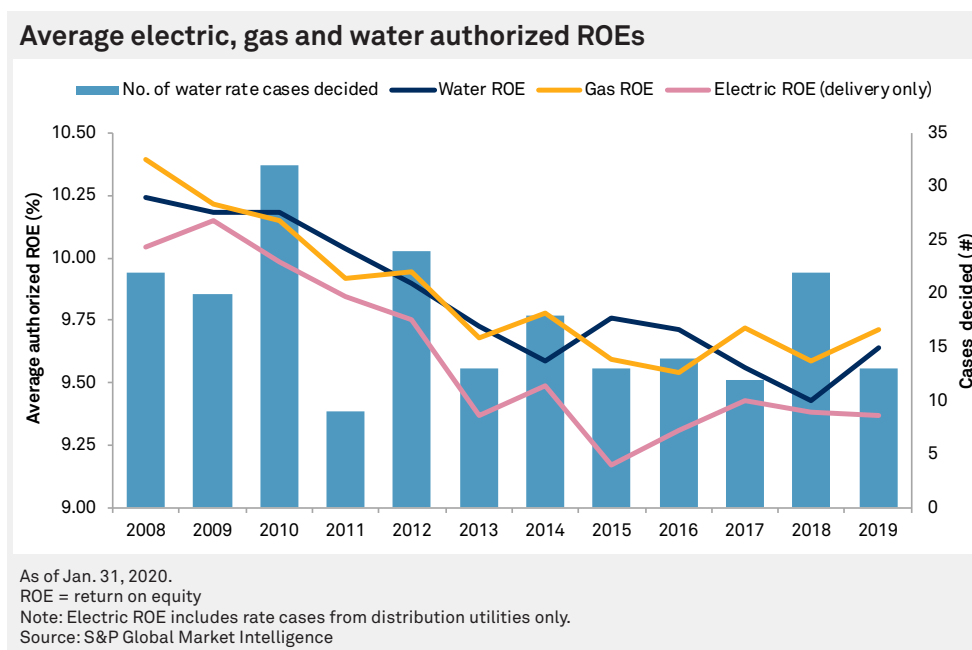
As investors familiar with the water utility sector are aware, there can be challenges discussing industry averages for such a small peer group. In 2019, water utility ROEs ranged from 9.2% to 9.8%. This range is considerably narrower than 2018, when ROEs ranged from 8.9% to 10.5%. During 2019, 10 of 13 rate cases were settled and cost of capital parameters were not disclosed in seven of those cases. In a small litigated Kentucky rate case, the return on ratebase methodology was not utilized and the company was authorized an operating ratio of 88%. The remaining litigated cases, in Kentucky and North Carolina, resulted in ROEs at the high end of the group's range, at 9.7% and 9.75%, respectively. The lowest ROE was authorized in a small Hawaii rate proceeding in a water, sewer and irrigation proceeding with a total rate base of less than \$30 million.

Utility sector comparison

The average ROE authorized natural gas utilities was 9.71% in cases decided during 2019, a rise from the 9.59% in 2018. There were only 32 gas cases that included an ROE determination in 2019, compared to 40 during 2018.

For electric distribution-only utilities, the average ROE authorized in 2019 was largely unchanged at 9.37% versus 9.38% in 2018. There were just eight distribution-only rate cases completed in 2019, compared to 16 in 2018.

As shown in the graph below, the annual average ROE for all three utility subsectors has been below 10% since 2012, as the persistently low interest rate environment has put a downward pressure on authorized returns.



What appears to be a recovery in the water utility authorized ROE from 2014 to 2015, as seen in the chart above, exposes the challenges that can come with a limited dataset. The 2014 average includes three New York rate decisions of 9.2%, a state that tends to authorize ROEs below the national average. In contrast, the 2015 water ROE average includes two relatively high ROEs, 10.0% and 10.1% in states with a small water footprint, Maryland and Hawaii, respectively. The combined rate base of these two decisions totaled less than \$25 million. Excluding these outliers, the ROE trend line for water utilities would appear a bit smoother. Similarly, the 2018 average is dragged down by the inclusion of five cost of capital proceedings in California for the largest water utilities, which authorized equity returns of 8.9% to 9.25%, well below the national average.

Across all utility subsectors, RRA has found no discernible pattern in the average authorized ROEs in cases that were settled versus those that were fully litigated. In some years, the average authorized ROE was higher for fully litigated cases, in others, it was higher for settled cases, and in a handful of years, the authorized ROE was similar for both fully litigated and settled cases.

For additional details on rate case trends for electric and gas utilities, refer to the Jan. 31, 2020 report titled [Major Rate Case Decisions – January – December 2019](#).

Declining rate case activity

Since 2012, the number of water rate cases has moderated somewhat. Many water utilities have consolidated their smaller operating companies, decreasing the frequency of rate filings. California Water Service Group had previously requested rate changes for its 24 systems on a cycle of eight systems per year, but starting with its 2009 general rate case, now files for all its jurisdictions in a single filing every three years. The two other large, multisystem water utilities in California similarly transitioned to consolidated rate proceedings.

By consolidating its small subsidiaries in each of the sixteen states in which Utilities Inc. operates, the company has also decreased the frequency of base rate case filings. SUEZ NA has similarly consolidated its New Jersey operations and is in the process of consolidating its New York subsidiaries in a pending rate proceeding. These actions streamline the rate case process and result in lower rate case expenses that are passed on to customers.

During the 2010-2012 time frame, American Water Works Company Inc. and Aqua America Inc. swapped assets in four states, leaving each company's customer count largely unchanged, while allowing for a more targeted approach to managing regulated operations and optimizing cost structures. Aqua America gained customers in Texas and Ohio in exchange for its New York and Missouri customers. As these systems were consolidated, rate case frequency declined in these jurisdictions.

Lastly, the expansion of infrastructure surcharge mechanisms has slowed the frequency of base rate cases in some jurisdictions. Commonly referred to as a distribution system improvement charge, or DSIC, the mechanism allows water utilities to earn a return on incremental qualifying, non-revenue producing infrastructure replacement in between general rate cases. DSIC mechanisms for water utilities are utilized in 20 states, with varying parameters regarding qualifying investments, surcharge caps and frequencies, and program oversight. Most recently, the mechanism was approved in rate cases in Kentucky and Rhode Island.

Historical rate case details

RRA currently evaluates water utility regulation in 25 state jurisdictions and monitors rate proceedings involving rate change requests of \$0.5 million or greater for the 13 largest investor-owned and privately held water utilities. As RRA broadens its water utility coverage to encompass all 44 states that currently regulate water utilities, this dataset will continue to expand, which will likely result in some adjustments to the historical water industry averages, as historical data is backfilled.

The individual water utility rate cases for 2010 through 2019 are available [here](#).

The decision date is shown first, followed by the company name, the abbreviation for the state issuing the decision, the authorized rate of return, or ROR, the ROE and percentage of common equity in the adopted capital structure. The following columns show the month and year in which the adopted test year ended and the rate base.

The simple mean is utilized for the return averages. In addition, the average equity returns indicated in this report reflect the cases decided in the specified time periods and are not necessarily representative of the returns actually earned by utilities industry wide.

Average ROEs authorized 2007 - 2019							
Year	Period	Water utilities		Electric utilities**		Gas utilities	
		ROE (%)	No. of observations*	ROE (%)	No. of observations*	ROE (%)	No. of observations*
2007	Full year	10.07	(15)	9.86	(10)	10.22	(35)
2008	Full year	10.24	(15)	10.04	(9)	10.39	(32)
2009	Full year	10.18	(17)	10.15	(10)	10.22	(30)
2010	Full year	10.18	(25)	9.98	(17)	10.15	(39)
2011	Full year	10.04	(8)	9.85	(12)	9.92	(16)
2012	Full year	9.90	(21)	9.75	(12)	9.94	(35)
2013	Full year	9.73	(11)	9.37	(9)	9.68	(21)
2014	Full year	9.59	(13)	9.49	(13)	9.78	(26)
2015	Full year	9.76	(11)	9.17	(6)	9.60	(16)
2016	Full year	9.71	(9)	9.31	(12)	9.54	(26)
	1st quarter	9.56	(4)	9.40	(3)	9.60	(3)
	2nd quarter	9.18	(2)	9.53	(3)	9.47	(7)
	3rd quarter	10.40	(1)	9.63	(3)	10.14	(6)
	4th quarter	9.55	(2)	9.26	(5)	9.68	(8)
2017	Full year	9.56	(9)	9.43	(14)	9.72	(24)
	1st quarter	9.23	(6)	9.00	(1)	9.68	(6)
	2nd quarter	10.50	(1)	9.23	(4)	9.43	(7)
	3rd quarter	9.07	(2)	9.63	(4)	9.69	(13)
	4th quarter	9.54	(8)	9.39	(7)	9.53	(14)
2018	Full year	9.43	(17)	9.38	(16)	9.59	(40)
	1st quarter	9.57	(3)	9.42	(3)	9.55	(4)
	2nd quarter	9.70	(2)	NA	0	9.73	(3)
	3rd quarter	9.80	(1)	9.60	(2)	9.80	(3)
	4th quarter	NA	0	9.17	(3)	9.73	(22)
2019	Year to date	9.63	(6)	9.37	(8)	9.71	(32)

As of Jan. 31, 2020.
* No. of observations identifies the amount of ROE data points available, not the number of rate cases completed during the period.
** Electric ROE includes distribution-only rate proceedings.
Source: S&P Global Market Intelligence

Expectations on future regulatory filings

The water utility sector faces growing capital investment needs, driven by increasing environmental standards and aging infrastructure, namely distribution pipes. Widely cited estimates of the spending needed to upgrade, replace and expand water and wastewater infrastructure over the next 20 years range from \$600 billion to \$1.3 trillion. It stands to reason that this accelerated spending would warrant the continuation of an active rate case agenda over the next few years.

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