

**STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH**

DOCKET NO. W-1318, SUB 1

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of
Application of HH Water, LLC, for)
Authority to Adjust and Increase Rates)
for Water Utility Service in High Hampton)
Service Areas in Jackson County, North)
Carolina)

**AFFIDAVIT OF
PATRICK A. FAHEY
PUBLIC STAFF –
NORTH CAROLINA
UTILITIES COMMISSION**

STATE OF NORTH CAROLINA

COUNTY OF WAKE

I, Patrick A. Fahey, being first duly sworn do depose and say:

I am a Public Utilities Regulatory Analyst with the Economic Research Division of the Public Staff of the North Carolina Utilities Commission (Public Staff), which represents the using and consuming public.

I received a Bachelor of Science degree in Economics from the University of North Carolina at Charlotte in 2018, and a Master of Economics degree from North Carolina State University in 2023. Since joining the Public Staff, I have conducted rate of return studies in water and wastewater utility rate cases and have been involved in the investigation and analysis of electric utilities proposed avoided cost rates and integrated resource plans.

The purpose of my affidavit is to make a recommendation to the North Carolina Utilities Commission (Commission) regarding the fair rate of return to be

employed as a basis for determining the appropriate revenue requirement for HH Water, LLC, to provide water and sewer utility service in all its service areas in Jackson County, North Carolina.

I recommend the use of a hypothetical capital structure comprised of 50% common equity and 50% debt. HH Water, LLC has financed its utility operations with 100% common equity, given it has no long-term debt for the purposes of ratemaking.

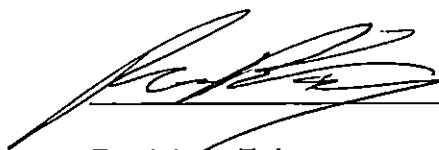
The actual capital structures of smaller utilities often are asymmetrical in that they are composed of either 100% equity balances of common equity or large balances of debt, neither of which are appropriate for ratemaking purposes. For example, if a utility owner financed the utility's rate base with little or zero amount of debt, the utility's capital structure would be comprised of 100% common equity. If one was to apply an average approved ROE, the higher cost rate for equity would lead to a higher level of revenue requirement than necessary to maintain financial sustainability. Furthermore, it is virtually impossible to estimate the appropriate equity cost rate given the absence of publicly traded securities that are comprised of unbalanced capital structures with 100% equity financing. In my opinion, the use of 50% debt and 50% equity capitalization ratio continues to be a reasonable assumption, as evidenced by recent ratemaking proceedings for other water and sewer utilities.

I recommend that HH Water, LLC be granted a 7.00% return on rate base for the water utility service. This recommended overall rate of return

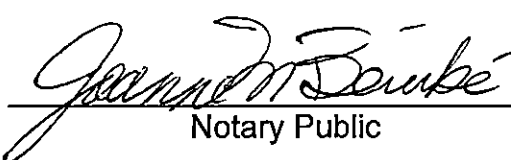
recommendation is based on a cost rate of long-term debt of 4.20%, and a cost rate for common equity of 9.80%. The reasonableness of this recommended margin is supported by the allowed overall rates of return approved by the Commission in recent cases involving large water and sewer utility companies. As allowed under N.C. Gen. Stat § 62-133, I have used the base rate method to evaluate HH Water, LLC's proposed rate increase. After investigation, the Public Staff has determined that the Company's rate base for this service area is greater than the reasonable level of operating expenses.

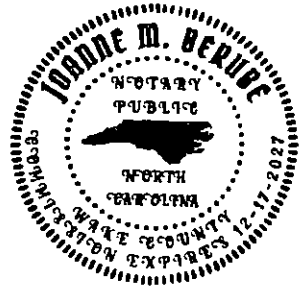
As outlined in Docket No. W-173, Sub 14, Montclair Water Company, several factors should be considered when judging the adequacy of a return. These are interest coverage, adequacy of the income level after interest expense, the level of inflation, and the quality of service. In considering these factors in conjunction with this proceeding, I have not incorporated any consideration with respect to quality of service. Interest coverage has been provided at an adequate level. The level of inflation has been factored into the interest rate on bonds that reflect investor expectations of the future levels of inflation. In my opinion, the recommended margin on rate base provides an adequate level of income after interest expense. The 7.00% overall return on rate base is also consistent with other approved overall rates of return for other water and sewer utilities in North Carolina.

For these reasons, I recommend to the Commission that HH Water, LLC be granted a 7.00% return on rate base. This concludes my affidavit.


Patrick A. Fahey

Sworn to and subscribed before me,
This the 6th day of June, 2024.


Notary Public



JOANNE M BERUBE
Printed Name

My Commission expires: 12/17/27