

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

DOCKET NO. W-1300, SUB 60

March 8, 2022

In the Matter of:

Application by Old North State Water	)	SETTLEMENT
Company, LLC, 3212 6th Avenue	)	TESTIMONY OF
South, Suite 200, Birmingham, Alabama	)	JOHN R. HINTON
35222, for Authority to Adjust and	)	PUBLIC STAFF – NORTH
Increase Rates for Water Utility Service	)	CAROLINA UTILITIES
in All Its Service Areas in North Carolina	)	COMMISSION

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION  
DOCKET NO. W-1300, SUB 60

SETTLEMENT TESTIMONY OF JOHN R. HINTON  
ON BEHALF OF THE PUBLIC STAFF –  
NORTH CAROLINA UTILITIES COMMISSION

March 8, 2022

1 Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND  
2 PRESENT POSITION.

3 A. My name is John R. Hinton. My business address is 430 N. Salisbury  
4 Street, Dobbs Building, Raleigh, North Carolina. I am Director of the  
5 Economic Research Division of the Public Staff – North Carolina  
6 Utilities Commission (Public Staff).

7 Q. ARE YOU THE SAME JOHN R. HINTON THAT FILED DIRECT  
8 TESTIMONY AND EXHIBITS ON RATE OF RETURN AND  
9 CAPITAL STRUCTURE ON FEBRUARY 8, 2022?

10 A. Yes, I am.

11 Q. WHAT IS THE PURPOSE OF YOUR SETTLEMENT TESTIMONY

12 A. The purpose of my settlement testimony is to support the Joint  
13 Settlement Agreement and Stipulation between Old North State  
14 Water Company, LLC (ONSWC or the Company) and the Public Staff  
15 (the Stipulation), as it relates to the cost of capital and capital  
16 structure to be used in setting rates in this proceeding.

1 **Q. WHAT IS THE COST OF CAPITAL IN THE STIPULATION?**

2 A. The Public Staff and the Company have agreed to a 7.00% overall  
3 weighted cost of capital in this proceeding. The cost rate is based on  
4 an average approved weighted cost of capital for recently approved  
5 general rate cases with water and wastewater utilities, as outlined in  
6 my direct testimony filed on February 8, 2022. Furthermore, this cost  
7 rate reflects the use of a hypothetical capital structure comprised of  
8 50% long-term debt and 50% common equity, a 9.40% cost of  
9 common equity, and a 4.60% cost of long-term debt, as shown in  
10 Hinton Supplemental Exhibit I.

11 **Q. WHAT IS YOUR EXPERIENCE WITH AND UNDERSTANDING OF**  
12 **SETTLEMENTS IN SIMILAR GENERAL RATE CASE**  
13 **PROCEEDINGS?**

14 A. It has been my experience that settlements are generally the result  
15 of good faith “give and take” and compromise-related negotiations  
16 among the parties to utility rate proceedings. Settlements, as well as  
17 the individual components of the settlements, are often achieved by  
18 the respective parties’ agreements to accept otherwise unacceptable  
19 individual aspects of individual issues. Settlements sometimes result  
20 in a “global” resolution of all the issues that would otherwise be  
21 litigated in a rate proceeding, and are sometimes restricted to

1 resolution of one or more individual issues. The Stipulation is global  
2 with respect to the contested issues the Public has identified.

3 **Q. DID YOU PARTICIPATE IN THE NEGOTIATIONS LEADING UP**  
4 **TO THE STIPULATION?**

5 A. Yes, I participated in the negotiations leading up to the Stipulation.

6 **Q. DO YOU STILL HAVE CONCERNS ABOUT THE COMPANY'S**  
7 **APPLICATION THAT PROPOSED A CAPITAL STRUCTURE**  
8 **CONTAINING 83% LONG-TERM DEBT AND 17% COMMON**  
9 **EQUITY?**

10 A. No, following settlement discussions, the Company provided  
11 consolidated financial statements of Integra Water, LLC (Integra).  
12 Those statements indicate a reasonable level of long-term debt and  
13 common equity for Integra. Furthermore, my discovery that Integra  
14 Water, LLC does not technically own ONSWC has not changed my  
15 recommendation on the cost of capital. I understand that John  
16 McDonald is the Member, Organizer, and Manager of ONSWC and  
17 Michael Myers is a Member and Organizer of ONSWC. Therefore,  
18 John McDonald is a co-owner of ONSWC while being the sole  
19 member of Integra Water, LLC (Integra). However, Mr. McDonald's  
20 role as the Manager of ONSWC, Integra's financial vitality, and his  
21 commitment that Integra will finance ONSWC's future capital  
22 requirements and fund ONSWC's ongoing, day-to-day capital and

1 operational needs supports my recommendation that ONSWC use a  
2 7.00% overall cost of capital, with a hypothetical capital structure  
3 composed of 50% long term debt and 50% equity.

4 John McDonald's authority to provide ONSWC with Integra's capital  
5 resources further supports this assurance. This commitment is  
6 memorialized on page 8 of the Joint Settlement Agreement and  
7 Stipulation filed in this docket on March 8, 2022, and is the basis for  
8 my revised recommendation that it is not necessary for the Company  
9 to bring its actual capital structure to 50% common equity, maintain  
10 a 45% equity ratio, or file audited financial statements with its Annual  
11 Report to the Commission for the next three years as means of  
12 showing its compliance with the recommended capital ratios.

13 **Q. IS THE 7.00% OVERALL COST OF CAPITAL A REASONABLE**  
14 **RESULT?**

15 A. Yes. I believe that the 7.00% overall cost of capital is reasonable.  
16 The 7.00% is based on recently approved, overall cost of capital for  
17 water and wastewater utilities and is applicable to determine the rate  
18 of return for both rate base-oriented utilities and for utilities where the  
19 risk to the owner is oriented toward its operating expense. In my  
20 opinion, the settled 7.0% overall cost of capital is appropriate for  
21 ONSWC and is fair to both ratepayers and the utility.

- 1 Q. DOES THIS CONCLUDE YOUR SETTLEMENT TESTIMONY?
- 2 A. Yes, it does.

Public Staff Overall Cost of Capital  
Old North State Water Company  
as of August 31, 2021

Item	Ratios	Cost Rate	Weighted Cost Rate	Pre-Tax Cost of Capital <sup>1</sup>
Long-Term Debt	50.00%	4.60%	2.30%	2.30%
Common Equity	50.00%	9.40%	4.70%	6.11%
Total	100.00%		7.00%	8.41%
			Pre-Tax Interest Coverage <sup>2</sup>	3.7

Notes:

<sup>1</sup> The pre-tax cost of debt and equity is grossed up by tax retention factors.

<sup>2</sup> Pre-Tax Interest Coverage:  $3.7 = 8.41 / 2.30$ .