

**CAROLINA WATER SERVICE, INC. OF NORTH CAROLINA
DOCKET NO. W-354, SUB 360**

**SUPPLEMENTAL TESTIMONY OF JOHN R. HINTON
ON BEHALF OF THE PUBLIC STAFF
NORTH CAROLINA UTILITIES COMMISSION**

October 12, 2018

1 **Q. PLEASE STATE YOUR NAME, POSITION, AND BUSINESS**
2 **ADDRESS FOR THE RECORD.**

3 A. My name is John R. Hinton and my business address is 430 North
4 Salisbury Street, Raleigh, North Carolina. I am the Director of the
5 Economic Research Division of the Public Staff.

6 **Q. ARE YOU THE SAME JOHN R. HINTON WHOSE DIRECT**
7 **TESTIMONY WAS FILED IN THIS DOCKET ON OCTOBER 4,**
8 **2018?**

9 A. Yes.

10 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**
11 **PROCEEDING?**

12 A. The purpose of my testimony is to revise my recommended capital
13 structure and cost of debt. The Company has provided additional
14 information to the Public Staff on the test-year level and cost rate
15 for the Company's Revolving Credit Facility (Credit Facility) that

1 was noted in my previous testimony. The updated information
2 allowed me to refine my recommendation for the June 30, 2018
3 balance of long term debt and to revise the embedded cost rate of
4 long term debt. As such, I recommend a capital structure that
5 consists of 49.09% long-term debt and 50.91% common equity.
6 Furthermore, I recommend a 5.68% cost rate for long term debt, as
7 shown below and in Hinton Supplemental Exhibit 1:

	CWSNC as of June 30, 2018	
	<u>Ratio</u>	<u>Cost Rate</u>
8		
9		
10		
11		
12	Long-Term Debt	49.09% 5.68%
13	<u>Common Equity</u>	<u>50.91% 9.20%</u>
14	Total	100.00%

15 **Q. HOW DOES THIS UPDATE INFLUENCE YOUR RECOMMENDED**
16 **OVERALL COST OF CAPITAL?**

17 A. The use of the updated capital structure and embedded cost of
18 debt combined with my October 4, 2018 pre-filed testimony
19 recommended 9.20% cost rate for common equity supports an
20 overall cost of capital of 7.47%, which supports a higher overall cost
21 of capital, relative to the 7.37% return from my October 4, 2018
22 testimony. The revised pretax interest coverage equals 3.2 times
23 and a funds flow to debt ratio of 26%, which should qualify for a

1 single "A" bond rating.

2 **Q. HOW DOES THE UPDATED RECOMMENDATION COMPARE**
3 **WITH PREVIOUSLY APPROVED OVERALL COST OF CAPITAL**
4 **FOR CWSNC?**

5 A. The recommended approved overall cost of capital of 7.47% is
6 lower than the 7.84% approved in Sub 356, the 8.20% approved in
7 Sub 344, and the 8.18% approved in Sub 336. The updated
8 recommendation with respect to the approved capital structure
9 ratios for long term debt and common equity are all similar to the
10 ratios approved in the Company's three previous cases, Sub 356,
11 Sub 344, and Sub 336. The decrease in the overall cost of capital
12 is partially due to the reduction in the Company's embedded cost
13 rate of long term debt from 5.93% approved in Sub 356, and the
14 6.60% approved in Sub 344 and Sub 336. The other contributing
15 factor is the recommended 9.20% equity return relative to the
16 approved 9.60% equity return in the Sub 356 rate case and the
17 approved 9.75% equity return in the Sub 344 and Sub 366 cases.

18 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

19 A. Yes.

Carolina Water Service, Inc. of North Carolina
 Cost of Capital as of June 30, 2018

Item	Ratios	Cost Rate	Weighted Cost Rate	Pre-Tax Cost of Capital ¹
Long-Term Debt	49.09%	5.68%	2.79%	2.79%
Common Equity	50.91%	9.20%	4.68%	6.12%
 Total	 100.00%		 7.47%	 8.91%
			Pre-Tax Interest Coverage ²	3.2
			Funds Flow to Debt ³	26.0%

Note:

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

² Pre-Tax Interest Coverage: 3.2 = 8.91 / 2.79

³ Funds Flow to Debt = (Recommended rate base*weighted debt cost rate) / (Net Income for Return + Depreciation + Amortization-Deferred taxes), Public Staff Henry Supp. Exhibit 1, 26% = (\$104,513,271*2.79%) / (7,809,265+5,149,485-1,547,356-132,758-519-83,570).