Exhibit_(HW-1R)
Docket No. 4800
Witness: H. Walker, III

SUEZ WATER RHODE ISLAND, INC.

WAKEFIELD, RHODE ISLAND

RATE OF RETURN

EXHIBIT

TO ACCOMPANY THE

REBUTTAL TESTIMONY

JULY 2018

Prepared by:
GANNETT FLEMING
VALUATION AND RATE CONSULTANTS, LLC

Valley Forge, Pennsylvania

UNITED WATER RHODE ISLAND, INC.

List of the Water Utility Proxy Companies

	Company	Safety Rating	Financial Strength	Beta	2013 Common Equity Ratio*
1.	American States Water	2	A	0.70	57.0%
2.	Aqua American	2	B++	0.60	50.0
3.	American Water Works	3	B +	0.65	46.0
4.	California Water	3	B++	0.65	58.0
5.	Connecticut Water	3	B+	0.75	50.5
6.	Middlesex Water	2	B++	0.70	57.0
7.	SJW Corporation	3	B+	0.85	45.5
8.	York Water	2	B+	0.70	55.0
	Average	**2.5**	**--**	**0.70**	**52.4%**

* The common equity ratio excludes short-term debt (and current maturities of long-term debt). Actual 2013 equity ratio including short-term debt and current maturities averages 49.6 percent.

Source: *Value Line Investment Survey,* October 18, 2013.

MOODY'S INVESTORS SERVICE

SECTOR COMMENT
24 January 2018

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Contacts

Toby Shea *VP-Sr Credit Officer* toby.shea@moodys.com	+1.212.553.1779
Ryan Wobbrock *VP-Senior Analyst* ryan.wobbrock@moodys.com	+1.212.553.7104
Nana Hamilton *AVP-Analyst* nana.hamilton@moodys.com	+1.212.553.9440
Natividad Martel, CFA *VP-Senior Analyst* natividad.martel@moodys.com	+1.212.553.4561
Robert Petrosino CFA *VP-Senior Analyst* robert.petrosino@moodys.com	+1.212.553.1946
Laura Schumacher *VP-Sr Credit Officer* laura.schumacher@moodys.com	+1.212.553.3853
Graham W Taylor *VP-Sr Credit Officer* graham.taylor@moodys.com	+44.20.7772.5206
Michael G. Haggarty *Associate Managing Director* michael.haggarty@moodys.com	+1.212.553.7172
Jim Hempstead *MD-Utilities* james.hempstead@moodys.com	+1.212.553.4318

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Regulated Utilities - US

Tax reform is credit negative for sector, but impact varies by company

The wide-ranging tax legislation passed by the US Congress on December 20, 2017 cut the statutory corporate tax rate to 21% from 35%. The legislation was broadly credit positive for corporate cash flows but for regulated investor-owned utilities, which include electric, gas and water utilities, the effect was the opposite.

» **The legislation is credit negative for investor-owned utilities.** A lower tax rate will reduce the difference between the amount that utilities collect from rate payers to cover taxes and their payments to tax authorities, reducing cash flow.

» **Tax reform is neutral for earnings but negative for cash flow.** Utilities collect revenue based on book tax but cash tax is much lower. A lower tax rate lowers revenue, while loss of bonus depreciation increases cash tax.

» **Cash flow to debt ratio could decline by 150-250 basis points.** We estimate that regulated utilities could experience a decline in the ratio of cash flow from operations pre-working capital to debt (CFO pre-WC/debt) of 150 bps to 250 bps, assuming no corrective action is taken.

» **Utilities with weaker than expected financials are most affected.** The potential for lower cash flows hurts the credit profile of numerous regulated utilities that already have weakening financial projections. Major holding companies affected include American Electric Power Company (AEP, Baa1 stable), Consolidated Edison, Inc. (ConEd A3 negative), Dominion Energy (Dominion, Baa2 negative), Duke Energy Corporation (Duke, Baa1 negative), Entergy Corporation (Entergy, Baa2 negative) and The Southern Company (Southern, Baa2 negative).

» **Most utilities are still well positioned within their credit profiles.**The vast majority of utilities and their holding companies are well positioned within their credit profiles thanks to supportive regulatory relationships and a capital structure balanced between both debt and equity.

S&P Global

FINANCIAL FOCUS

Average utility equity ratio rises slightly, possibly from tax reform fallout

Tuesday, June 26, 2018 12:47 PM ET

By Dennis Sperduto

Some provisions of the tax reform legislation that was enacted in December 2017 have relatively obvious financial implications for utilities. For instance, rate regulated utilities will, with very few exceptions, be required to lower customer rates to account for the reduced tax expense due to the decline in the corporate tax rate to 21% from 35%. In addition, the corporate tax rate reduction will require utilities to recalculate their deferred income tax balances at the new lower rate, which will lead to the companies having reduced deferred income tax balances.

<<< Read the full report >>>

One of the not-so-apparent implications of the tax reform legislation is that utility credit metrics will likely experience some strain due to the lower customer rates, revenues and cash flows resulting from the corporate tax rate reduction. Utilities can offset the pressure to their credit metrics in several ways. One approach is to reduce capital expenditures, which, while not increasing earnings or cash flow or rates, would conserve funds and counteract the strain on credit metrics. However, data contained in a RRA Financial Focus report that was published on April 20, Utility Capital Expenditures Update, indicates that a pullback in utility CapEx plans has not occurred.

Another approach is that utilities can petition regulators for an increase in their authorized equity returns as a means of offsetting the negative credit ramifications of the new tax law. In addition, the companies can increase the equity components of their capital structures which, when approved by regulators, would serve to increase rates, earnings, and cash flow.

This article examines capital structure data contained in a June 20 Financial Focus Quality Measures report for 83 utility operating companies. The data indicates that the average equity component of capital increased slightly for this group of companies, from 50.1% at year-end 2017 to 50.3% at the conclusion of 2018's first quarter. We note that the three months covered by the Quality Measures report that have elapsed since the new tax law became effective on Jan. 1, represent a short time frame in which to evaluate whether any significant trend has emerged. However, as the data indicates, a trend, albeit a slight one, may have commenced in the first quarter of 2018. We expect this nascent trend toward increased equity ratios to garner at least modest momentum in the remainder of 2018, given the anticipated pressure on utility credit metrics.