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October 23, 2008

Luly Massaro  
Clerk  
Division of Public Utilities and Carriers  
89 Jefferson Boulevard  
Warwick, RI 02888

Re: Interstate Navigation Company  
Compliance Filing – Combined Dockets D-06-51 and D-06-53

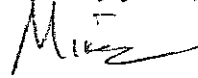
Dear Luly:

As you know, this office represents Interstate Navigation Company (Interstate).

Enclosed for filing in these combined dockets are an original and five copies of the compliance testimony of Walter E. Edge, Jr., concerning Interstate's fast ferry Certificate of Public Convenience and Necessity (CPCN).

If you have any questions or you need any further information, please feel free to call.

Very truly yours,



Michael R. McElroy

MRMc:tmg

cc: Susan Linda  
Joshua Linda  
Walter E. Edge, Jr.  
Paul Roberti, Esq.  
Katherine Merolla, Esq.  
Block Island Town Clerk, certified mail RRR  
Narragansett Town Clerk  
Newport City Clerk

**COMPLIANCE TESTIMONY  
OF  
WALTER E. EDGE JR. MBA CPA  
RELATING TO THE COMBINED DOCKETS D-06-51 and D-06-53  
WHICH ADDRESSED THE FOLLOWING ISSUES**

**DOCKET D-06-51**

**INTERSTATE'S PETITION TO BORROW \$5.6 MILLION DOLLARS**

**DOCKET D-06-53**

- 1. INTERSTATE NAVIGATION'S FILING REQUESTING APPROVAL OF INTERSTATE'S PURCHASE OF THE RHODE ISLAND ASSETS OF IHSF, INCLUDING THE *M/V ATHENA*, CPCN, ETC., AND LEASE OF THE *M/V ATHENA* TO IHSF, AND**
- 2. INTERSTATE'S REQUEST FOR THE ELIMINATION OF ALL RESTRICTIONS ON INTERSTATE'S FAST FERRY CPCN, AND**
- 3. INTERSTATE'S REQUEST FOR ELIMINATION OF RESTRICTIONS ON THE IHSF FAST FERRY CPCN, AND**
- 4. INTERSTATE'S REQUEST TO TRANSFER IHSF'S CPCN TO INTERSTATE AND TO CONTINUE TO HOLD THE IHSF CPCN IN ABEYANCE, AND**
- 5. INTERSTATE'S REQUEST TO CONTINUE TO HOLD THE NEWPORT LEG OF ITS FAST FERRY CPCN IN ABEYANCE**

**Before  
RHODE ISLAND DIVISION OF  
PUBLIC UTILITIES AND CARRIERS**

**October 2008**

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## GENERAL OVERVIEW

**Q. Will you please provide your full name and your employer for the record?**

A. Yes, my name is Walter Edward Edge Jr., MBA CPA. I am the president of B&E Consulting LLC.

**Q. Are you the same Walter E. Edge Jr. who has previously filed expert accounting and rate testimony for Interstate Navigation Company (Interstate) in previous Commission and Division dockets including Dockets D-06-51 and D-06-53 for which you are filing this compliance testimony?**

A. Yes, I am.

**Q. Mr. Edge, what is the purpose of your testimony in this docket?**

A. This testimony has a number of purposes as follows:

1. Provide an update on the successful purchase of all of the Rhode Island assets of Island Hi-Speed Ferry LLC (IHSF) including the fast ferry *M/V Athena*, IHSF's CPCN, customer list, a covenant not to compete, etc., with a \$5.6 million loan from the Washington Trust Company.
2. Provide an update on the lease of the *M/V Athena* to IHSF for the period November 15, 2006 until May 1, 2007.
3. Provide an update on Interstate's fast ferry operations relating to the merged fast ferry CPCNs (Interstate's original CPCN and the CPCN purchased by Interstate from IHSF) authorized by the RI Division of Public Utilities and Carriers (Division) to provide non-lifeline fast ferry service between Block Island and the ports of Point Judith and Newport.
4. Provide an update on Interstate's financial results of running the fast ferry *M/V Athena* between Point Judith and Block Island (Old Harbor and New Harbor) up to six times a day in the summer under Interstate's merged Fast Ferry CPCN in FYE May 31, 2007 (*M/V Athena* leased from IHSF) and FYE May 31, 2008 (*M/V Athena* purchased from IHSF).
5. Provide the current status of Interstate's plans regarding a second larger fast ferry vessel.

- 1 6. Provide the status of Interstate's plans to run a fast ferry service to/from Newport.  
2 (Please note that the Newport leg of Interstate's merged fast ferry CPCN was put into  
3 dormancy by the Division (Docket D-06-53) until October 31, 2008, at which time  
4 Interstate is required to file with the Division its intentions regarding this service.)  
5 7. Provide the Division with Interstate's current requests relating to all of the open issues  
6 identified above.

7  
8 **Status of Interstate's Purchase of the RI Assets of IHSF**  
9

10 **Q. What is the status of Interstate's purchase of all of the Rhode Island assets of IHSF?**

11 A. I believe that the Division is already aware that Interstate successfully purchased all of the  
12 Rhode Island assets of IHSF (including the fast ferry M/V *Athena*) on November 17, 2006. The  
13 Division approved Interstate's request to borrow \$5.6 million dollars to finance the purchase of  
14 all of IHSF's Rhode Island assets in Docket D-06-51. With this authority from the Division,  
15 Interstate was able to obtain favorable financing from Washington Trust in order to complete the  
16 purchase.

17  
18 **Q. How will Interstate pay back the \$5.6 million dollar loan it made to purchase the  
19 Rhode Island assets of IHSF?**

20 A. The Public Utilities Commission (PUC) allowed Interstate to collect, through its fast ferry  
21 rates, the entire debt service (principal and interest) on the \$5.6 million loan from Washington  
22 Trust. Interstate proposed (and the PUC agreed) that profits from Interstate's fast ferry  
23 operations (after paying all expenses and the debt service) would be retained in the company to  
24 help support the lifeline traditional service. The decisions of the Division to allow the  
25 borrowing and the PUC to allow full payment of the debt service payments have allowed  
26 Interstate to complete the purchase of the IHSF assets and have resulted in holding down  
27 traditional service rates.

28  
29 As I testified previously in this docket, the greater the fast ferry profits, the better for the  
30 traditional customers and the company:

1 "With the purchase of the IHSF assets, Interstate will gain control over the profits from  
2 the fast ferry operation from Point Judith and will be able to funnel those profits back into  
3 the company, as it has always done, for the good of the ratepayers. This approach,  
4 although good for the ratepayers, is also good for the company. The company gains  
5 through an increase in equity and a stronger financial position. Also the company gains  
6 from the reduction in competition." See page 6 of my original prefiled testimony, lines  
7 23-27.

8  
9 **Status of the 2006-2007 Winter Lease to IHSF**

10  
11 **Q. Mr. Edge, the next item you listed above for consideration is the Division approval of**  
12 **the lease of the *M/V Athena* to IHSF for the period November 15, 2006 until May 1, 2007.**  
13 **How did that lease work out?**

14 A. IHSF's plans to operate the *M/V Athena* in Puerto Rico under lease from Interstate fell  
15 through. However, through the efforts of management, Interstate was able to charter the *M/V*  
16 *Athena* to New York Waterways for substantial portions of the winter seasons of 2006-07 and  
17 2007-08.

18  
19 **Status of Interstate's Fast Ferry Operation**

20  
21 **Q. How is Interstate's fast ferry operation working since the purchase of the IHSF fast**  
22 **ferry?**

23 A. It is working quite well, and the company is very pleased. Interstate actually started its fast  
24 ferry operation in the summer of 2006 by leasing the *M/V Athena* from IHSF. That summer the  
25 fast ferry operation was profitable, but Interstate's management was somewhat disappointed with  
26 the ridership. Interstate found that it was getting most of IHSF's customers but that there was  
27 little new ridership. It appeared that Interstate's traditional service customers were slow to  
28 change from traditional service to fast ferry service.

29  
30 The summer of 2007 was much better for the fast ferry service. Interstate had the necessary lead  
31 time for the summer of 2007 to properly advertise and market its fast ferry service to Old Harbor.

1 The result was a significant increase in ridership resulting in a more profitable summer for the  
2 fast ferry operation. However, some of the increased ridership on the fast ferry service came at  
3 the expense of Interstate's traditional service where ridership was somewhat off in the summer of  
4 2007.

5  
6 The fast ferry experienced another increase in ridership year over year in the summer of 2008,  
7 even as traditional ridership declined, primarily due to a slowing economy and a dramatic  
8 increase in fuel prices which adversely affected summer tourism in general.

9  
10 Gaining fast ferry customers at the expense of the traditional service is generally a win for  
11 Interstate and its traditional service customers. Each customer that moves from the traditional  
12 service to the fast ferry service contributes more to Interstate's overall revenue and therefore they  
13 help maintain lower traditional life-line service rates for those who remain with the life-line  
14 service.

15  
16 It should also be noted that although Interstate runs its fast ferry primarily from Point Judith to  
17 Old Harbor, it also runs it to New Harbor during Race Week (the races are staged from New  
18 Harbor).

19  
20 **Interstate's Financial Results from the Fast Ferry Operation**

21  
22 **Q. Mr. Edge, have you calculated Interstate's fast ferry financial results for the summer**  
23 **of 2006 and 2007 that are included in the overall company results for the fiscal year May**  
24 **31<sup>st</sup> 2007 and 2008?**

25 A. Yes I have. Please see Schedule WEE-1 attached to this testimony. It is important to point  
26 out that the actual fast ferry profit for FYE May 31, 2007 (summer of 2006) was \$364,666 as  
27 compared to the estimated May 31, 2007 fast ferry profit of \$365,730 used by the Commission in  
28 establishing Interstate's current rates. The difference is immaterial to the rate calculation. The  
29 Commission amortized the projected 2007 fast ferry gain to the ratepayers of the traditional  
30 service over three years (CYE December 31, 2007, 2008 and 2009) at a rate of \$121,910 per  
31 year.

1 The actual fast ferry profit for FYE May 31, 2008 (summer 2007) was \$503,363, reflecting the  
2 increased ridership.

3  
4 **Status of Interstate's Plans Regarding**  
5 **a Second Larger Passenger/Vehicle /Freight Fast Ferry Vessel**  
6

7 **Q. Does Interstate still intend to acquire a second larger fast ferry vessel?**

8 A. Interstate would still like to eventually acquire a larger passenger/vehicle/freight fast ferry as  
9 was described in Interstate's original request for its fast ferry CPCN. However, although fast  
10 ferry ridership is increasing annually, to date Interstate has not observed that there is an adequate  
11 demand that would support two fast ferry vessels. If the passenger demand for fast ferry service  
12 sufficiently increases so that it makes financial sense, Interstate still intends to acquire (by lease  
13 or purchase) a new, larger fast ferry.

14  
15 **Q. What has Interstate determined regarding demand for fast ferry service after running**  
16 **its own fast ferry service for the last three summers (2006, 2007, and 2008)?**

17 A. Interstate has observed that only on rare occasions has the *M/V Athena* operated at full  
18 capacity. The fact is that if one fast ferry providing six runs a day to and from Block Island has  
19 not been fully utilized, there is no need, at this time, for a second fast ferry to address passenger  
20 demand. Therefore if Interstate were to acquire a new larger fast ferry at this time and run it  
21 three times a day from Point Judith to Block Island and Newport and return as originally  
22 suggested, while at the same time running the *M/V Athena* six times a day to Block Island,  
23 Interstate would be running both vessels well below their passenger capacity and would most  
24 likely incur significant losses which would adversely impact the traditional service.

25  
26 **Q. Mr. Edge wouldn't the added revenue from vehicles and freight to/from Block Island**  
27 **and the passengers to and from Newport help support a second fast ferry vessel?**

28 A. Yes, it would. However, when Interstate filed its original CPCN request, it estimated that  
29 the vehicle revenue would be \$63,000 from Interstate's current customers and \$57,540 from new  
30 customers; that freight revenue would be \$25,368; and that Newport passenger revenue would be  
31 about \$140,000, for a total additional passenger, vehicle and freight revenue of \$285,908.

1 Debt service alone was projected for the new boat of about \$720,000 per year. Therefore at this  
2 time it appears that the new boat could only generate new revenue of about \$285,908 which is  
3 only about 40% of the projected debt service costs.

4  
5 **Q. What would have to happen to make it possible for Interstate to go forward and**  
6 **acquire a second larger passenger/vehicle/freight fast ferry?**

7 A. In each of the last two years, Interstate has been able to increase the year over year ridership  
8 on its fast ferry service. If this trend continues and the passenger demand for fast ferry service  
9 from Point Judith to Block Island grows to a point where it exceeds the current capacity of the  
10 *M/V Athena*, this would provide an opportunity to reconsider the need for acquiring a bigger fast  
11 ferry.

12  
13 A second consideration that would favor acquiring another fast ferry vessel would be if the  
14 economy improved. Interstate believes that the current price of fuel and the general poor  
15 condition of the economy has forced prospective Interstate customers to stay at home. An  
16 improvement in the overall economy should increase ridership across the board for the  
17 traditional and fast ferry services. Increased demand from this activity would also provide an  
18 opportunity to reconsider the need for the bigger fast ferry.

19  
20 A third consideration would be the need for a new fast ferry service vessel to replace or augment  
21 one of the traditional service vessels. Interstate runs both the traditional and fast ferry  
22 operations as one company. Decisions for Interstate are made taking both services into  
23 consideration. Should Interstate determine that one of the traditional vessels was no longer  
24 suitable for the current demand, Interstate might consider replacing or augmenting the traditional  
25 vessel with a new passenger/vehicle/freight fast ferry. Although this may seem a bit reaching,  
26 Interstate has seen a significant change in its business in the last five years and is not sure how  
27 much the business will change in the next five years. Interstate is keeping its options open.

28



1                    Status of Interstate's Plans Regarding a Fast Ferry Service to/from Newport.

2  
3    **Q. What are Interstate's current plans regarding the introduction of fast ferry service**  
4    **between Newport and Block Island?**

5    A. Ridership from Newport to/from Block Island remains very weak. Interstate still believes  
6    that the ridership would improve if there were more than one run a day from Newport to Block  
7    Island and return. Because of the length of the run (approximately twice the Point Judith --  
8    Block Island run) as a practical matter, in order to accomplish additional Newport runs, Interstate  
9    would need to provide fast ferry service.

10  
11   **Q. Mr. Edge didn't you just testify that the new fast ferry would not be profitable?**

12   A. Yes I did. The larger auto and freight carrying fast ferry would not be profitable at this  
13   time. Further, the auto and freight aspects of the proposed fast ferry are not applicable for  
14   Newport. Interstate is instead beginning to consider the possibility of leasing a fast ferry which  
15   would carry only passengers to and from Block Island to determine if there is an adequate  
16   demand for fast ferry services to and from Newport. If the demand is significant enough to  
17   cover the Newport portion of the run, then Interstate would be able to reconsider the acquisition  
18   of a new vehicle/freight/passenger fast ferry.

19  
20   **Q. When might Interstate lease a fast ferry and run from Newport?**

21   A. Interstate does not know. Interstate is currently adjusting to the \$5.6 million dollar debt it  
22   incurred to buy the IHSF business. At this time Interstate has a great deal of outstanding debt  
23   and is hesitant to expand its operations. Further Interstate is in the second year of a five year  
24   PUC rate plan that allows for inflation adjustments in the last 3 years, but does not allow for a  
25   full rate filing during the plan. Interstate is also worried about the economy. Therefore,  
26   Interstate believes that this is not a good time to start this new service.

1                    **Summary of Interstate's Current Requests Relating to all of the Open Issues**

2  
3    **Q. What does Interstate want the Division to approve?**

4    A. Interstate would like the Division to keep everything status quo for at least another three  
5    years until the PUC Rate Plan ends. Interstate would like the Newport leg of its fast ferry CPCN  
6    to remain in dormancy at least until the end to the Rate Plan. Therefore, Interstate requests that  
7    the Division simply extend its merged fast ferry CPCN until July 2012 when Interstate would be  
8    in a far better position to address these issues. In June 2012 Interstate is required to calculate the  
9    sharing of profits from the five year rate plan for the PUC and may in fact have to refund  
10   earnings to the ratepayers. Interstate will be in a far better position to address these issues after  
11   Interstate knows the impact of the profit sharing. Therefore, Interstate suggests that another  
12   filing similar to this one be made no earlier than July 1, 2012.

13  
14   **Q. Does that conclude your testimony?**

15   A. Yes.

Analysis of Revenue and Expenses  
Interstate Fast Ferry

Schedule WEE-1

	<u>Actual FYE 5/31/07</u>	<u>Actual FYE 5/31/08</u>
<b>Revenues:</b>		
Passenger Revenue	\$ 1,213,684	\$ 1,528,253
Other Revenues (Bar, bike, etc)	63,692	81,580
Charter Revenue	<u>122,850</u>	<u>227,125</u>
Total Revenue	1,400,226	1,836,957
<b>Expenses:</b>		
Salaries and wages	140,328	201,394
Payroll taxes	4,253	15,295
Fuel	257,652	327,746
Maintenance:		
Vessel Maintenance-Athena	105,756	54,906
Lube Oil	5,957	7,900
Other Vessel Expenses	6,873	20,186
Insurance	15,550	54,866
Advertising	14,636	21,596
Bar expense	15,318	23,084
General and Administrative Expense		
Legal and accounting	39,319	15,731
General office supplies	23,753	4,754
Gross Receipts Taxes	17,503	22,962
Boat Charter	172,885	4,000
Fees (coast guard, banking, etc)	13,901	24,188
<u>Debt service on \$5,600,000:</u>		
Principal	-	82,420
Interest	201,875	403,419
Total Expense	<u>1,035,560</u>	<u>1,284,447</u>
Federal Income Tax	-	49,148
Net Income	<u>\$ 364,666</u>	<u>\$ 503,363</u>