BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Liberty Utilities (Missouri Water) LLC's Application for a Rate Increase.	))	File No. WR-2018-0170 SR-2018-0171

REPLY BRIEF OF SILVERLEAF RESORTS, INC. AND ORANGE LAKE COUNTRY CLUB, INC.

I. The Non-unanimous Stipulation and Agreement

Silverleaf regrets not filing an "objection" to the non-unanimous stipulation and agreement by Friday, August 10, 2018. This was a minor technical, procedural oversight which was fixed the following Monday, August 13, 2018.[1] No prejudice resulted from this oversight to any party. Silverleaf thanks and appreciates the Commission's willingness to deny Staff's motion for expedited treatment and modification of the evidentiary hearing schedule, and allowing the hearing to proceed as scheduled. Silverleaf inadvertently missed a deadline because it was focused on the substantive surrebuttal testimony of witness Stannard responding to the Stipulation and Agreement, and generally preparing for hearing, including discussing the Issues List for the evidentiary hearing in this case.

The non-unanimous stipulation and agreement between Staff and LU-MW was filed on August 3, 2018. There was no attempt by Staff or LU-MW to make this non-unanimous agreement unanimous before August 10, 2018. Silverleaf never received a draft prior to its filing. Silverleaf was never asked to compromise any position in exchange for a settlement. Silverleaf wishes that more time and energy was dedicated *prior* to August 10 to making the non-unanimous stipulation and agreement unanimous.

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[1] See, *Silverleaf Resorts, Inc. and Orange Lake Country Club, Inc.'s Response to Non-Unanimous Stipulation and Agreement*, filed August 13, 2018, Item No. 93. Silverleaf needs to clarify that OPC does not "oppose the overall revenue requirement but has concerns that the information in the Stipulation is incomplete." *Office of Public Counsel's Clarification of Its Response to Non-Unanimous Stipulation*, ¶ 4.

That Staff has seized enthusiastically upon a technical, procedural oversight (which was quickly remedied) is telling. Staff offers a remarkably candid rational for suggesting that the Commission consider a non-unanimous stipulation and agreement as unanimous: "By treating the Stipulation as unanimous, the Commission can approve the Stipulation *without need for making findings of fact or conclusions of law on those issues resolved.*"[2] (Emphasis added.) Staff encourages the Commission to use a procedural oversight – *which prejudiced absolutely no one* -- to avoid making findings of facts and conclusions of law, and to approve issues lacking evidentiary support.

Several points are worth mentioning regarding this suggestion. First, Staff's suggestion to use a minor procedural oversight to forego adjudication of this case does not project confidence in the evidentiary support of Staff's positions or the non-unanimous stipulation and agreement in this case. Staff even points out that there are parts of the non-unanimous stipulation and agreement which have no evidentiary support in the legal record. So it suggests that this minor procedural oversight offers a convenient opportunity to deal with that unrelated problem.[3] Silverleaf asks the Commission to not use a minor procedural oversight to remedy a lack of evidentiary support for the non-unanimous stipulation and agreement.

Second, the Commission should not base its decisions merely on the opportunity to avoid finding of facts and reaching conclusions of law. The recommendation to use a minor procedural oversight to cavalierly avoid adjudication of this case for no other reason than expedience and a lack of evidentiary support is unseemly. Silverleaf asks the Commission to look at the evidence presented in this case and apply Missouri law in its determination of safe and adequate service at just and reasonable rates for LU-MW and LU-MW customers. The Commission's decision should be based on competent and substantial evidence and not a fiction created by a minor procedural oversight.

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[2] *Staff's Initial Brief*, P. 9.
[3] *Ibid.*

Third, the Commission should not impute a position on a party which is clearly not the position of that party, even in light of a minor procedural oversight. As explained in Silverleaf's Initial Brief[4], witness Stannard's sur-rebuttal testimony clearly expressed the position of Silverleaf as it directly relates to the non-unanimous stipulation and agreement. Silverleaf has not been passive in this case and its positions were clearly understood. Specifically, all parties knew exactly where Silverleaf stood on the issues at least through August 9 because the parties were negotiating the *List of Issues* for the evidentiary hearing that week.

Finally, no party to this case has suggested any prejudice resulting from this minor procedural oversight. The Commission wisely proceeded with the evidentiary hearing. To declare now the non-unanimous stipulation and agreement "unanimous" after having taken substantial evidence at an evidentiary hearing, which clearly shows that the stipulation and agreement was not unanimous, is a waste of time and money. Silverleaf requests that the Commission deny Staff's motion to treat the non-unanimous stipulation and agreement as unanimous.

II. Disputed Issues

a. Staff's ROE Recommendation is based on a Self-Referential and Circular Methodology which does not support the significant difference with the ROE supported by the "Authoritative Source"

Staff points out in its Initial Brief that witness David Murray testifies that the Duff & Phelps based risk-premium assessment for a return on equity is the "S&P 500 Market required return on equity. Not a utility required return on equity."[5] Silverleaf absolutely agrees – the required return for utilities is lower than that of the S&P 500. As witness Murray explains in his surrebuttal

[4] *Initial Brief of Silverleaf Resorts, Inc. and Orange Lake Country Club, Inc.*, P. 17-18.
[5] *Ibid.* at 11.

testimony, because utility stocks are less volatile, the risk-premium is *less* than that of the S&P 500 Market.[6]

> Yes. Utility stocks are less volatile than the broader market. This lower volatility is typically measured by calculating the beta of utility stocks. Typically, betas of utilities are in the range of 0.6 to 0.8. Applying a typical utility beta of 0.7 to the market risk premium of 5%, results in an industry adjusted risk premium of 3 .5%. Adding this 3 .5% adjusted risk premium to Duff & Phelp's normalized risk-free rate of results in a cost of 6 equity of 7%.[7]

Witness Murray could not have been more clear that applying the utility risk premium to the "authoritative source" resulted in an ROE fully 1% less that the recommended range offered by Silverleaf of 8% - 9%.[8] Silverleaf's recommended ROE of 8% - 9% is clearly reasonable.

Murray's ultimate recommendation though veers drastically from his analysis of the "authoritative source"[9] solely based on the bootstrapping of a recent Spire Missouri natural gas case.[10] The platitude used to justify this grafting-approach to ROE is that "there's a lot of similarities" between utility companies.[11] Silverleaf agrees that there are similarities between utility companies; there are similarities between all companies, particularly all public utility companies. But little effort was made to identify the similarities which justified or explained such a substantial divergence for return on equity from the authoritative source.

It is apropos that Mr. Murry mentioned the "concern about circularity"[12] of regulatory cost of capital decisions during the evidentiary hearing. A decision by the Commission to simply

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[6] Ex. No. 110, Murray, Surrebuttal Testimony, 3:1-6.
[7] *Ibid.*
[8] *Ibid.*
[9] *Staff's Initial Brief*, P. 11.
[10] *Ibid.*
[11] *Ibid.*
[12] Evidentiary Hearing Tr., 113:20-22.

rely upon its own ROE decision for Spire Missouri in the LU-MW would be the definition of circular decision-making. If the recent decision on which Staff bases its recommendation was merely one factor, then it would be appropriate to take that decision into limited consideration. But it is the entire basis for Staff's ROE recommendation. No evidence was offered in this case justifying the significant delta between the ROE based upon an "authoritative source" and the circular, self-referential method proposed by Staff.

With regards to LU-MW's witness Keith Magee, as provided in Silverleaf's Initial Brief[13] and Motion to Strike[14], any reliance on Magee's testimony (either written or oral testimony) would be *reversible error* in its prejudicial effect on Silverleaf. LU-MW could have disclosed Magee as an expert witness in time for Silverleaf to conduct meaningful discovery. It chose not to. Magee's participation in this case was disclosed to Silverleaf on the last day of discovery.

Finally, if the Commission wants LU-MW to come in for another rate case within the next 24 months as recommended by Staff, it is entirely unnecessary for the Commission to unlawfully take over a management function and order LU-MW to come in for a rate case. Rather the Commission should use the tools that it lawfully has available (such as establishing a constitutionally permissible, just and reasonable ROE) to incentivize LU-MW to return to the Commission for a rate case.

b. Phase-In and Customer Charge: Staff's Analysis Opposing Silverleaf's Phase-In Proposal Recognizes Silverleaf's Time-share Owners as LU-MW Customers

Staff provides the following analysis of the Silverleaf system in opposition to Silverleaf's phase-in proposal:

[13] *Initial Brief of Silverleaf Resorts, Inc. and Orange Lake Country Club, Inc.*, P. 5-6.
[14] *Motion to Strike Surrebuttal Testimony of Keith Magee and Motion for Expedited Treatment* filed August 8, 2018.

> Thus, some 36,686 timeshare owners ultimately pay the cost of water service at 371 meters. Mathematically, this means that *approximately 99 customers pay toward one meter* and any increase would then be "passed through" under the maintenance fee provision of the Declaration to that volume of timeshare owners. Thus, the potential rate shock of a rate increase is significantly mitigated. (Emphasis included in the original.)[15]

Silverleaf appreciates Staff referring to Silverleaf's timeshare owners as "customers" because they do bare the ultimate financial responsibility for the utility service. Staff also treated Silverleaf's timeshare owners as "customers" for the purpose of justifying its rate-design (although studiously using the euphemism of "water users.")[16] Here again, it is fundamentally inconsistent to treat Silverleaf's timeshare owners as LU-MW customers for one policy analysis and decision, but not for another. If Silverleaf's time-share owners are LU-MW customers for the purpose of rate-design (both the phase-in proposal and customer charge issues) then it is inappropriate and contradictory that they should be considered non-customers for the purposes of SURP eligibility.

Silverleaf agrees with Staff that the Commission has legal authority to order a phase-in of rates.[17] If Silverleaf's time-share owners' water usage should be considered for rate design -- the legal justification under *Laudry* for a phase-in of rates limited to the Silverleaf system becomes apparent. Silverleaf timeshare owners represent the majority of LU-MW customers and revenues and those customers are "unique" according to Staff.[18] Silverleaf also believes that it would be appropriate to phase-in *all* LU-MW customer rates, not just Silverleaf. However, a phase-in of

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[15] *Staff's Initial Brief*, P. 22.
[16] *Initial Brief of Silverleaf Resorts, Inc. and Orange Lake Country Club, Inc.*, P. 14-15(citing Exhibit No. 102, Surrebuttal Testimony, Barnes, 2:5-12.)
[17] *Staff's Initial Brief*, P. 19, FN 90 ("As a matter of ratemaking policy, phase-ins for water utilities may be appropriate in certain circumstances.")
[18] *Initial Brief of Silverleaf Resorts, Inc. and Orange Lake Country Club, Inc.*, P. 14-15(citing Exhibit No. 102, Surrebuttal Testimony, Barnes, 2:5-12.)

Silverleaf's rates alone would be justified given Silverleaf's percentage of usage, customers of and revenues to LU-MW.

If the Commission authorizes a phase-in of LU-MW rates, Staff expresses concern regarding an "undue burden" placed on the utility if the "carrying costs" for such a phase-in are not included the revenue requirement.[19] Silverleaf asks the Commission to weigh the "undue burden" placed on Algonquin Power & Utilities, Corp. by absorbing its short-term borrowing rate for a phase-in with the "rate shock" on LU-MW customers if a phase-in is not ordered. It was not LU-MW customers which inexplicably waited almost a decade to ask this Commission for a rate increase. To be clear, any phase-in of rates would be preferable to the rate-shock for LU-MW's customers, even if it includes the additional revenues of Algonquin's short-term borrowing rate.

c. *Appropriate Customer Charge and Commodity Charge*

Similarly, Staff in proposing a 174% and 112% increase in the customer charge for water and sewer service based on its analysis on the water usage of customers. But Staff refuses to recognize these customers in the context of SURP eligibility.

Silverleaf disagrees with Staff that the only purpose of rate-design is to ensure that the utility company collects its entire revenue requirement.[20] In fact, rate-design is about much more that lowering the financial risk of the utility company. Rate-design has the power to impact customer behavior and greatly impacts customers (or "water users" depending on what policy

[19] *Staff's Initial Brief*, P. 23.
[20] *Ibid.* ("The purpose of rate design is to develop rates for a given utilities' tariffed operations in a manner to provide the Company an opportunity to collect its Commission-approved revenue requirement.")

Staff is advocating for) financially. If the Commission rewards LU-MW with a 174% and 112% increase in its customer charge for water and sewer service, it will send a clear signal to LU-MW customers that water conservation and energy efficiency are not a policy priority. Also, such a rate-design shows little concern for the smallest customers of LU-MW. Should the Commission adopt Staff customer-charge recommendation, it will be sending a clear signal that its sole policy interest in rate-design is to lower the financial risk of the utility.

If the Commission does chose to adopt Staff's utility-risk-free rate design proposal, it should recognize the enormous shift of risk to LU-MW customers and order an ROE commensurate with that rate design. The combined ROE and rate-design proposal offered by Staff and LU-MW asks for an ROE which compensates for an investor risk which does not exist under the proposed utility-risk-free rate design they offer in this case. A 9.75% ROE with a 174% and 112% increase in the customer charge is truly a fantastic deal for Algonquin Power & Utilities, Corp., but not so much for its Missouri customers.

d. Staff's Recommended Rate Case

Staff recommends the Commission order LU-MW to come in for a rate case in the next 24 months. This may be an intelligent and rational management decision to make for LU-MW, but it is also telling that Staff believes it is necessary for the Commission to *order* LU-MW to make an intelligent and rational management decision.

Silverleaf has asked to be exempted from this near-future rate case. Silverleaf -- as a non-regulated, market-based company doing business in Missouri -- does not have the Staff of the Public Service Commission to "assist" it through the regulatory process. In the Staff Assisted Rate Case Procedure, 4 CSR 240-10.075, it is the certificated monopoly utility getting the

"assist" from Staff, not the *market-based* businesses within the utility's service territory. And it is abundantly clear from this case that the market-based businesses within LU-MW's service territory must fend for themselves to protect their interests through the regulatory process. Silverleaf does not get to *automatically* build into its revenue requirement the cost of this regulatory process, because Silverleaf has market competition. Staff understands the effect of market competition when it comes to investor expectations and competition for capital among utilities; but the impact of regulatory costs on market-based companies seems to fall on deaf ears in this case.

Regardless, the Commission does not need to order LU-MW to come in for a rate case, because it already has the tools to appropriately incentivize the utility to come back for any rate adjustment which prudent management of the utility would require.

Respectfully Submitted,

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CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing have been e-mailed to all counsel of record this 11th day of September 2018.

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