**BEFORE THE PUBLIC SERVICE COMMISSION**
**OF THE STATE OF MISSOURI**

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| In the Matter of the tariff filing of | ) | |
| Algonquin Water Resources of Missouri, | ) | |
| LLC to implement a general rate increase | ) | Cases Nos. WR-2006-0425 |
| for water and sewer service provided | ) | SR-2006-0426 |
| to customers in its Missouri service areas. | ) | |

# BRIEF OF ALGONQUIN WATER RESOURCES OF MISSOURI, LLC


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**ALGONQUIN WATER RESOURCES OF MISSOURI, LLC**
**CASE NO. WR-2006-0425**

**BRIEF**
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Comes now Algonquin Water Resources of Missouri, LLC (Algonquin or Company), and states the following to the Missouri Public Service Commission (Commission) as its Brief:

## I. INTRODUCTION

Algonquin initiated this case with the filing of proposed tariffs and direct testimony on May 5, 2006.

The rates to be established in this case concern the following utility systems, which are owned and operated by Algonquin:

- A water system at Holiday Hills Resort near Branson, Missouri;
- Water and sewer systems at Ozark Mountain Resort near Kimberling City, Missouri; and
- Water and sewer systems at Timber Creek Resort near Desoto, Missouri.

Algonquin received approval from this Commission to purchase these systems from Silverleaf Resorts, Inc. by the Commission's order in Case No. WO-2005-0206 (issued on August 4, 2005). Silverleaf initially received certificates from the Commission to operate the facilities in 1994 as to Holiday Hills (WA-94-60) and Ozark Mountain (WA-94-246), and in 1998 as to Timber Creek (WA-98-129).

Silverleaf was, and is, primarily in the business of operating resorts. In fact, they remain the resort owner at each of the three resorts served by Algonquin. Silverleaf represents by far the largest customer for the water and sewer services. Exh. 1, Loos Dir., p. 6. At Timber Creek, Silverleaf is the only customer. At Ozark Mountain and Holiday Hills, Silverleaf represents about one-half of the total number of accounts, and exclusive of untreated water (used for golf course irrigation at Holiday Hills), about 75 percent of water use. *Id*. Overall at the three resorts, Silverleaf represents about 50 percent of the water accounts, 60 percent of the sewer accounts and 90 percent of water and sewer sales. *Id*.

None of the subject water or sewer operations have ever been through a formal rate case. Initial rates were established in 1994 and have been changed just once since then - in September 1998, as the result of a small company rate case proceeding initiated on April 4, 1997.

Algonquin's Brief will address on the following pages the issues identified by the parties in the Proposed List of Issues, Order of Witnesses, and Order of Cross-Examination that was filed by the Staff of the Commission (Staff) on January 5, 2007.

## II. ISSUES

### A. Plant.

This issue has been broken into two parts – 1) what amount, if any, should be reflected as plant-in-service for plant existing before 1993; and, 2) what amount should be reflected as plant-in-service for plant put in service after 1992.

This distinction relates to the fact that the water facilities at the Holiday Hills Resort and the water and sewer facilities at the Ozark Mountain Resort operated for at least as long as ten years prior to the Commission's grant of certificates for those facilities in 1994.

One of the reasons for continued uncertainty as to plant issues is the fact that these properties have never been through a formal rate proceeding. Initial rates were set with the issuance of the certificates and rates were changed just once, in 1998, as a result of a small company rate proceeding. Until this case, no formal case had been filed with, or litigated before, the Commission with regard to these properties. The Commission must keep in mind that if rate base is not sufficient for an on-going concern, there will not be funds to invest in the system when the facilities are ultimately retired or need to be expanded. Tr. 99-100. The Commission should also be mindful of the fact that the numbers being discussed are plant-in-service numbers, not rate base numbers. Once a plant-in-service number is identified, depreciation will be applied to derive a rate base number for purposes of determining the revenue requirement. Depreciation has a particularly significant impact on the pre-1993 property because of the length of time it has been in service.

**What amount, if any, should be reflected as plant-in-service for pre-1993 property?**

Algonquin witness Larry Loos has reviewed the property records on behalf of Algonquin inherited from Silverleaf. One of the things he noticed early in the process was that there was no plant on the Silverleaf books prior to 1993. Exh. 1, Loos Dir., p. 15. He found this strange because, as stated before, it is clear that there were water and sewer facilities operating at the Holiday Hills and Ozark Mountain resorts before 1993 and before the Commission certificated Silverleaf as a utility. Exh. 1, Loos Dir., p. 16.

An example of the unrealistic situation presented by the Silverleaf books is that that there is no source of supply related investment for the Ozark Mountain Resort facility prior to 1993. *Id*. at p. 21. This is in spite of the fact that the property went into service in about 1982. *Id*.

Because facilities were in place at Ozark Mountain and Holiday Hills prior to

1993, reasonable adjustments should be made to the plant balances to reflect an accurate assessment of the plant that is providing service to the customers. *Id*. at p. 17. To do this, Mr. Loos went about a detailed process where he determined what plant was in existence prior to 1993 and then determined an original cost estimate for the plant. Tr. 98-99; Exh. 1, Loos Dir., p. 19-24. This process enabled Mr. Loos to develop an estimate of original cost where no records were available to establish such. Exh. 4, Loos Sur., p. 11.

Accordingly, Mr. Loos has recommended that plant-in-service for pre-1993 property (prior to depreciation) should be equal to $1,914,032. This amount is split between distribution and collection facilities in the amount of $729,427; and water supply and treatment and sewage treatment facilities in the amount of $1,184,606. Exh. 1, Loos Dir., p. 22-23; Exh. 2, Loos Upd. Dir., Sch. LWL-3, Sht. 1 of 2. The rate base number, which would be net of depreciation, would be much less than these gross plant dollars because of the many years that have passed since the plant was put in service. Algonquin has proposed a depreciation reserve of $265,649 related to pre-1993 sewer plant and a depreciation reserve of $636,914 related to pre-1993 water plant. Exh. 1, Loos Dir., Sch. LWL-S, Sht. 2 of 8 and LWL-W, Sht. 2 of 8.

Silverleaf's lack of documentation has been a problem for many years and was already present at the time the original 1994 certificate cases were being processed. Exh. 9, Vesely Reb., p. 14. This circumstance is not unanticipated, at least as to the pre-1993 plant. As Staff witness Featherstone indicated, Silverleaf would have had no incentive, prior to becoming a public utility in 1994, to account for infrastructure costs separate from its development costs. Tr. 199-200; *see also* Tr. 136.

While there was some discussion of plant issues in the initial certificate cases, it was clear that the Commission orders were not meant to establish plant amounts on a going forward basis. In fact, the Commission's order in Case No. WA-94-246 (Ozark Mountain Resort certificate case) specifically ordered that "nothing in this Order shall be considered as a finding by the Commission of the reasonableness of the expenditures herein involved, nor of the value for ratemaking purposes of the properties herein included, nor as an acquiescence in the value placed on said properties by Ascension Resort, Ltd." Order Granting Certificate, p. 3; Tr. 96-97.

When Algonquin bought the subject systems, it was buying assets - sufficient plant for fully functioning water and sewer systems. Tr. 97-98. Staff argues primarily that there cannot be plant-in-service unless there is proper evidence of such. The evidence desired by Staff is in the form of paper. It is not sufficient for the Staff that one can walk out the door and see the property in place and functioning. Tr. 131-132. It is unclear why the physical existence and operation of the property is not sufficient evidence to establish a need for plant entries. The existence or non-existence of documentation does not change whether or not the plant exists and is providing service to the customers. Tr. 95.

Staff witness Vesely stated that he focused on documentation because that was his "interpretation of the correct position to take with regard to the . . . Uniform System of Accounts." Tr. 131. He further stated that if his interpretation of the Uniform System of Accounts proved to be inaccurate, he might have a different position. *Id*.

In fact, the Uniform System of Accounts (USOA) does not use the rigorous documentation standard proposed by Staff. For example, the NARUC USOA for Class

A and B Water Utilities (1973, as revised in 1976)[1] provides as follows in the Utility Plant Instructions (emphasis added): Section 1 (Classification of Utility Plant at Effective Date of System of Accounts), Subsection C. "The detailed utility plant accounts (301 to 399, inclusive) shall be stated on the basis of cost to the utility of plant constructed by it and the original cost, estimated if not known, of plant acquired as an operating unit or system." The USOA clearly provides that that plant may be estimated where it is not known. Exh. 4, Loos Sur., p. 12; Tr. 73-74. Algonquin witness Loos provided two other examples from the USOA that contain this same language as to estimation. *Id*. Therefore, Algonquin witness Loos went through a process (estimation) that is authorized by, and consistent with, the USOA.

Staff also pursued an argument that the Commission should consider the cost of the plant-in-service to have already been recovered because it was built by the developer of the three resorts. This approach reflects a misunderstanding of the differences in context between an unregulated property developer's business and the way in which utility rate making is performed. The resort business is a highly competitive, unregulated business. Tr. 48. The prices that are set are based on market conditions with only secondary consideration to the development costs. *Id*. This is very different from how utility rates are developed based on actual costs and allowed returns. Unlike utilities, developers are free to charge whatever amount they desire. A piece of real estate with access to water and sewer services has a value that is completely unrelated to who may have built the utility systems. Tr. 94. Thus, it is impossible to attempt to apply some sort of "recovery" analysis to the sale of lots. It is certainly possible that the only time Silverleaf recovered the costs of

1 This is the version of the USOA Missouri water utilities must follow in accordance with Commission Rule

construction of the water or sewer system was when it sold these systems to Algonquin. *See* Tr. 94-95.

A finding that plant-in-service should reflect some amount for pre-1993 is further consistent with how Algonquin has declared its property taxes. Algonquin's property tax declaration includes property with a purchase date prior to 1993 as to both its Ozark Mountain systems and its Holiday Hills system. Exh. 4, Loos Sur., p. 9.

The plant-in-service amounts identified by Algonquin witness Loos for pre-1993 plant are a reasonable estimate of the appropriate amount of plant to be reflected on Algonquin's books. The Commission should order Algonquin to reflect those amounts on its books subject to appropriate depreciation on a going forward basis.

**What is the appropriate level of post-1992 plant that should be included as plant- in-service?**

Algonquin and Staff also differ as to the amount of plant that should be deemed to be in service for more recent periods. Algonquin believes that plant-in-service for the post 1992 time period should equal $4,740,455. Exh. 3, Loos Reb., p. 18. The Staff's recommended amount of $4,234,202 represents a minimum amount of plant that should be reflected for this time period. *Id*. This is because Staff started from the ground up and utilized only those amounts for which it could find specific invoices and other paperwork. Exh. 3, Loos Reb., p. 15-16, 18. This approach is biased toward finding a minimum amount of plant-in-service, not necessarily the actual amount of plant-in-service. *Id*. at p. 16.

When this Staff approach is compared to how Staff treated contributions in aid of construction (CIAC), there appears to be what Algonquin witness Loos called a "double

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4 CSR 240-50.030.

standard." On one hand, for an asset to be included in plant, Staff believes the investment must be supported by detailed records (the mere existence of the plant will not do). However, Staff requires no records for plant to be considered contributed. Exh. 4, Loos Sur., p. 19.

Mr. Loos' analysis instead started with the Silverleaf books and a concept of what plant is actually in the ground. His plant-in-service total is a reasonable one based upon the plant that is in place and used to provide service to the customers.

If the Commission finds both the Company and Staff approaches to contain strengths and weaknesses, Algonquin believes that under the circumstances it would be reasonable to set an amount of $4,531,453 for the post-1992 property -- the midpoint between the Staff and Company recommendations. Exh. 3, Loos Reb., p. 16-18.

**B. Excess Capacity.**

**Do Algonquin's facilities include plant held for future use, which should not be included in plant in service, because they include excess capacity? If so, what is the value of the facilities that should not be included as plant-in-service?**

Staff originally alleged that there was excess well and storage capacity associated with the three Algonquin water operations. There was no alleged excess capacity alleged in regard to the sewer systems. The alleged excess capacity as to the wells concerned the Holiday Hills Resort ($3,371), Ozark Mountain Resort ($12,296) and Timber Creek Resort ($89,550). Tr. 160-161. The alleged excess capacity as to the storage capacity concerned the Holiday Hills Resort ($198,518) and Timber Creek Resort ($170,972). *Id*. The total amount of this proposed adjustment was $474,707, which the Staff recommended be treated as plant held for future use. This means that this amount of plant would be separated from rate base such that the Company is not allowed to earn a return on the investment until some point in the future when it is found that there is no longer any excess capacity.

At the hearing, Staff amended its position on this issue and later filed its revised accounting schedules (Exh. 28) to incorporate these changes. Based upon his consideration of fire flow information supplied by Algonquin witness Hamrick, Staff witness Merciel amended his recommendation as to the two storage capacity adjustments. Mr. Merciel recommended that $24,400 of the investment in the storage capacity at Holiday Hills be treated as excess capacity (instead of the original $198,518) and that $58,400 of the investment in the storage capacity at Timber Creek Resort be treated as excess capacity (instead of $170,972). Tr. 161-162. This leaves a total of $187,972, as the Staff's proposed excess capacity adjustment. Tr. 162.

Algonquin takes the position that there is no excess well capacity or storage at the Ozark Mountain, Holiday Hills or Timber Creek resorts and that the investment in those facilities is prudent. Holiday Hills and Timber Creek have used storage capacities within 11% of the actual storage volume and should not be considered to have excess capacity. Exh. 5, Hamrick Reb., p. 5. Further, all the subject facilities are used and useful and operating to the benefit of Algonquin's customers.

This issue highlights a classic problem for a utility. If it builds too little capacity, it is subject to complaints related to its ability, or inability, to provide safe and adequate service either now or in the future when growth takes place. Following Staff's position, if a utility takes advantage of economies of scale and builds a sufficient amount for the future, it risks suffering from stranded investment.

Capacity cannot be added to water systems in infinite increments to make capacity always match the theoretical requirement of the systems. Exh. 5, Hamrick Reb., p. 7. Inefficiency and wasted money would result from installing incremental storage every time a single additional dwelling unit customer was added to a system, if it would even be possible.[2] *Id*. As a consequence, it is much cheaper to add capacity in blocks that optimize the relationship between up front cost and the time value of money to the period where the capacity actually becomes useful to the system. *Id*. Balancing this relationship effectively results in situations where there may be excess capacity for periods of time, but the investments can still be considered the most wise and prudent action. *Id*. The utility should not be penalized for taking actions that in the future will be proven to be in the best interest of the utility's customers in that the utility will have secured capacity at an appropriate cost. *Id*.

Even if the Commission should decide that some excess capacity exists, there is a need to determine how much of the investment should be treated as plant held for future use. Mr. Merciel has utilized a straight percentage to calculate his adjustments. Tr. 165-166. In other words, if he believes 20% of the facility is excess, he has suggested that 20% of the original cost be deemed plant to be held for future use.

Determining the value or cost of any excess capacity is not simply a matter of multiplying the percentage of excess capacity by the total cost of the installation and assuming that is a proper valuation of that percentage of excess capacity that might be

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2 If calculations show a utility needs 70k gallons of storage and sections of tank only come in 20k increments, you can either build 60k of storage (not enough) or 80k gallons (excess?). Similarly, if a utility needs a well that produces 1000 gallons per minute, and the utility builds a well that produces 1100 gallons per minute, is there excess?

determined to exist. Exh. 5, Hamrick Reb., p. 6. There is no linear correlation between cost and capacity. *Id*.

Mr. Hamrick provided a water storage project as an example. For such a project, the cost of installing storage facilities will include design, permit approvals, tendering, mobilization, site preparation, foundations and supports, installation or erection of the storage tank (lets assume it is a bolted steel tank), controls automation and instrumentation, installation of electrical and plumbing, commissioning and startup, etc. *Id*. The capacity of such a storage tank could be increased by 30% (say from 300,000 to 400,000 gallons) by including one additional ring of bolt on steel wall segments, but that would not require any material change to any of the other components or labor. *Id*. Adding this additional 30% additional incremental capacity might add 5% to the cost of the entire installation. *Id*.

Staff acknowledges this principle to some extent. Staff witness Merciel stated that there is no simple way to determine an over-capacity adjustment. Exh. 17, Merciel Dir., p. 6; Tr. 165. He further stated that "small utilities generally cannot construct plant capacity on an incremental, ongoing basis to match the customer connections that are being made to a system because there are not many plant components involved." Exh. 17, Merciel Dir., p. 6.

Algonquin witness Hamrick has testified that the actual cost of the approximately 25% incremental capacity that Staff claims is excessive, would likely only reduce the installation cost by approximately 5%. Exh. 5, Hamrick Reb., p. 7. Although Algonquin does not believe any excess capacity exists and at any of the systems, if any amount is deemed to be plant held for future use should be more in line with this 5% figure than the figure suggested by the Staff.

### C. Construction Cost Overrun.

**Were some of the costs of constructing the facilities imprudently incurred? If so, how much should the plant-in-service accounts be reduced?**

This issue concerns the Well No. 2 construction project at the Holiday Hills Resort that was completed by Algonquin's predecessor, Silverleaf Resorts, Inc., in 2002. Exh. 8, Vesely Dir., p. 35. The project consisted of the construction of water plant infrastructure around an existing borehole that had not previously been used to supply potable water. Exh. 6, Hernandez Reb., p. 3. It included wellhead refurbishment, piping, storage, a pump station and associated facilities one would expect to find at a potable water supply location. *Id*. Staff has recommended a disallowance of $160,749 of the cost associated with this project. Exh. 28. This includes $42,292 alleged to be associated with loss of value of work done by the low bidder (Exh. 8, Vesely Dir., p. 35; Exh. 28); $41,686 alleged to be excess capitalized interest during the construction period (*Id*.); and, $76,771 associated with the switch from the lowest to second lowest bidder[3] (*Id*.).

The Commission has generally used a reasonable care standard in evaluating the prudence of utility actions. "The 'reasonable care standard' was described by the Commission in [*Union Electric Company*, 27 Mo. P.S.C. (N.S.) 183, 194 (1985)] as follows: 'The Commission will assess management decisions at the time they are made and ask the question, 'Given all the surrounding circumstances existing at the time, did

3 Staff originally indicated this latter amount was $102,395. Exh. 8, Vesely Dir., p. 35. However, during the hearing, Staff modified this position to reduce its disallowance by $25,624. Tr. 315-316, 323-324. Staff's revised accounting schedules incorporated this change and included $76,771 for this aspect of the

management use due diligence to address all relevant factors and information known or available to it when it assessed the situation?'" *State ex rel. Capital City Water Co. v. Missouri Pub. Servs. Co.*, 850 S.W.2d 903, 911-12 (Mo.App.W.D. 1993).

In the *Union Electric* case, the Commission further stated that it "will not rely on hindsight" and did "not adopt a standard of perfection" because "perfection relies on hindsight." *Union Electric* at p. 194. "Under a reasonableness standard relevant factors to consider are the manner and timeliness in which problems were recognized and addressed. Perfection would require a trouble-free project." *Id*.

Utilizing this standard, the costs associated with the Well No. 2 project at Holiday Hills were prudently incurred. While the project was not perfect, Silverleaf's decisions were reasonable based upon the facts known at the time decisions were made. Exh. 6, Hernandez Reb., p. 2-7.

Silverleaf bid this project before beginning construction. The two lowest bids received were from Larry Snyder and Company (Snyder) ($329,000) and Construction Management Services ($421,000). Tr. 268, 293. Staff witness Vesely indicated that Snyder successfully performed projects in the past for Silverleaf. Tr. 277. Silverleaf itself described Snyder as a long time supplier of construction services to Silverleaf. Exh. 6, Hernandez Reb., Sch. CAH-1, p. 5. Thus, based on the information available at the time, the initial decision to hire this contractor would appear to have been prudent.

However, during the course of various projects, including non-utility projects, Silverleaf perceived that Snyder was requesting a disproportionate amount of high value change orders such that its initial bid bore little resemblance to the ultimate cost of the

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proposed disallowance. Exh. 28.

project. *Id*. at p. 6. In Mr. Hernandez' opinion, this was conduct was consistent with either a failing contractor or a contractor that has bid a job too low. Exh. 6, Hernandez Reb., p. 4; Tr. 265-266.

True to form, Snyder later ceased doing business with Silverleaf. Tr. 278. Staff witness Vesely believed that the relationship ceased as a result of the Well No. 2 project. *Id*.

It was Silverleaf's opinion from its experience with other projects that Snyder would most likely not have delivered at the originally bid price and that Snyder was not prepared to complete this project on terms that were reasonable. Exh. 6, Hernandez Reb., Sch. CAH-1, p. 7. Faced with these surrounding circumstances, Silverleaf could either litigate – a process full of costs and uncertain outcome – or move on to the second lowest bidder. Silverleaf chose to move on to the second lowest bidder – a reasonable decision under the circumstances known at the time.

Silverleaf then turned to the second lowest bidder who provided a credit of $111,000 for the work performed and supplies purchased by the original contractor and then proceeded to complete the project for the bid amount. Tr. 322-323.

Mr. Vesely's proposed disallowance is not based on an opinion that the finished cost of the project was unreasonable, but rather that he thinks it could have been done cheaper. Tr. 292. Both the $42,292 portion of Staff's proposed disallowance described as the loss of value of work down by the low bidder and the $76,771 portion described as the difference between the low and second low bids are based directly on the fact that Silverleaf changed from the low bidder. Tr. 298, 308-309.

Returning to the Commission's standard for such questions, expenditure of these additional funds are only imprudent if it was unreasonable based upon the "surrounding circumstances existing at the time." It is not appropriate to look at the decisions with the benefit of hindsight.

Silverleaf made the most cost-effective decision based on the choices presented to them by the situation that developed. Exh. 6, Hernandez Reb., p. 5. Staff's proposed disallowance is based on a perfect project. That is, that the lowest bidder completed the project without difficulty at the original price. Silverleaf was not presented with a perfect situation and the Commission's standard of review does not require a perfect project. *Union Electric* at p. 194. Silverleaf's actions were prudent as to the Well No. 2 project and there should be no disallowance associated with this project.

**D. Contributions in Aid of Construction (CIAC).**

**What is the amount of contributions in aid of construction that should be used to reduce Algonquin's plant-in-service accounts?**

Staff recognizes that too much contributed plant will hamper a utility's viability. Staff witness Merciel states that the water and sewer department believes that the "regulated water and sewer utilities have the best chance of being viable entities if the utility owners invest in the central facilities such as well, storage tanks, sewage treatment facilities, and for larger systems, perhaps major feeder pipelines or trunk sewers. . . ." Exh. 18, Merciel Reb., p. 2.

In this case, the resort developer and the utility were one and the same – a single corporation -- until Algonquin purchased the utility properties in August of 2005. Based on this relationship, Staff has imputed an amount of contributed plant to be utilized as an off set to plant-in-service in determining rate base at all five utility systems.

“Imputed” is the appropriate word to use in this situation, as nothing exists to support the Staff approach.  The Staff’s approach to imputing contributed plant limits the rate base that a company can recover a return of and on and leaves it with little margin for error as external factors impact its revenues.

The Company does have tariffs regarding contributions of plant in conjunction with line extensions. Exh. 29 and 30.  The tariffs describe a process that is very specific in its requirements.  The tariffs require a “written application” and a “contract.” *Id*; Tr. 205.  No such documents exist as to the Algonquin properties or plant.  Tr. 205, 209-210.  Additionally, Mr. Loos found no evidence of any estimates, or any tender of an estimated amount, as required by the tariff.  Exh. 3, Loos Reb., p. 20.

Unlike its approach to the plant-in-service issue, Staff is not bothered by this lack of documentation as to the contributed plant.  Staff states that this omission is  “easily explained by the affiliate relationship the utility had with the developer.” Exh. 10, Vesely Sur., p. 12.  This is a significantly more forgiving standard than the one Staff attempts to apply to plant-in-service.

Moreover, both the water and the sewer connection tariff contemplate that refunds will paid to the requesting developer as connection are made to line extensions. Exh. 29, Rule 14(e); Exh. 30, Rule 11F.  If there were contributions in accordance with these tariffs, as supposed by the Staff, there would also be refunds to the developer (Silverleaf) that would serve to ultimately increase rate base.  Staff has not imputed any refunds along with its imputed contributions.

Lastly, it is significant that these tariffs were initially effective in 1994.  Thus, they could not be effective as to plant placed in service prior to 1994.

Silverleaf certainly did not agree with Staff's approach to CIAC. As recently as July of 2005, SIlverleaf provided the following statement to the Commission in regard to plant balances:

> I do not believe that there has been a meaningful and reasonable process by which a determination has been made that could have been reflected in the accounts of Silverleaf respecting any amounts -- be it depreciation, used and useful assets, CIAC, efficiently installed assets (Well#2) or any related matter -- through the informal rate case process in 1998, the Staff initiated earnings investigation in 2002, or otherwise. Silverleaf has not accepted most of the positions and amounts Staff has proposed and hence it cannot reasonably be expected that these should somehow have been acceptable to Silverleaf and have been reflected in the books and of the utility. Silverleaf has consistently rejected Staff's position on these matters and has therefore not taken its recommendation.

Exh. 31, p. 3-4.

Mr. Vesely admitted that Staff's interpretation of this issue had met with some resistance in the past. Exh. 8, Vesely Dir., p. 17. And although Silverleaf had begun to include a CIAC amount on its Annual Reports (Tr. 212), it had not reflected such amounts on any of its own books and records. Tr. 346; Exh. 4, Loos Sur., p. 20.

Further, even under the Staff's approach the contributions would only apply to distribution facilities. It would not apply to the water supply and treatment facilities and the sewage treatment facilities in place prior to 1993. It is for this reason that Mr. Loos indicates that, at a minimum, the $1,184,606 of pre-1993 supply and treatment related plant (as will be further reduced by applicable depreciation) should be recognized and should not be treated as contributed plant. Exh. 4, Loos Sur., p. 22.

There is no evidence of any transaction that meets the requirements of Silverleaf's extension tariffs such that it should constitute contributed plant. Algonquin's property records should not reflect any amount of either pre-1993 or post-1992 plant as contributed.

## E. Depreciation Rates.

**What depreciation rates should be applied to the various elements of Algonquin's plant in service?**

Depreciation reserve ratios (depreciation reserve divided by the total plant in service) should generally fall below 50%. Exh. 1, Loos Dir., p. 26-27; Tr. 351. In this case, relying on the rates proposed by Staff results in excessively high reserve ratios. Exh. 3, Loos Reb., p. 22. Algonquin witness Loos examined the reserve rations that would result from use of the depreciation rates recommended by Staff witness Schad. This exercise revealed that several accounts would have a reserve ratio of over 100% (Well Pump- Electric Pump Equipment - water, Computer Equipment and Software – water and sewer, Sewer System Development – Engineering - sewer). Exh. 2, Loos Upd. Dir., Sch. LWL-3 UPD, Sheet 2 of 2. Several other accounts carry reserve rations of over 50% (Office Furniture and Equipment – water and sewer (61.3%), Receiving Wells – sewer (64.6%), Pumping Equipment – sewer (53.9%), Treatment and Disposal Equipment – sewer (80.2%), Sewer Plant – Organization (82.5%)). *Id*. In order to address this issue, Mr. Loos adjusted his recommended depreciation rates to obtain a more reasonable ratio. Tr. 353.

Staff witness Schad did not examine the reserve ratios on an account by account basis, like Algonquin. Tr. 370-371. Accordingly, Staff does not know what impact its rates will have on each property account.

The Commission should approve the depreciation rates recommended by Algonquin witness Loos, as found in Exh. 2, Loos Upd. Dir., Sch. LWL-3 UPD, and calculate the existing reserve balance as of September 30, 2006, using those rates. Exh. 3, Loos Reb., p. 22.

**F. Capital Structure.**

**What capital structure should the Commission apply to Algonquin's investment in determining the proper rate of return on Algonquin's rate base?**

The capital structure of Algonquin Water Resources of Missouri, LLC consists of 100% equity. Exh. 1, Loos Dir., p. 30. As a result, Algonquin proposes the use of the capital structure of the operating company's ultimate parent, Algonquin Power Income Fund. *Id*. As of the end of the update period - September 30, 2006 – the actual capital structure of the parent was 58.21% equity and 41.79% long term debt (and convertible debentures). Exh. 3, Loos Reb., p. 6.

Instead of using this actual parent capital structure, Staff witness Barnes proposes a purely hypothetical capital structure of 47.88% equity and 52.12% debt. Exh. 11, Barnes Dir., p. 12. He creates this capital structure by utilizing an average of the capital structures of the companies contained in his comparable group. Tr. 409.

There is no reason to go from an actual capital structure of the parent to an average of what Mr. Barnes viewed to be comparable companies. Mr. Barnes points to the fact that Algonquin's parent is traded on the Toronto Stock Exchange, Staff's unfamiliarity with Canadian markets and the Company's structure as reasons for his use of a hypothetical structure. Exh. 11, Barnes Dir., p. 11-12. However, in spite of this, the actual Algonquin capital structure is not markedly different from capital structures the Commission has seen recently for other United States companies.

In fact, the actual Algonquin capital structure is very similar to that utilized in Kansas City Power & Light Company's recent Commission rate case. *In the Matter of the Application of Kansas City Power & Light Company*, Report and Order, Case No. ER-2006-

0314 (December 21, 2006). In that case, it was determined that KCPL had the following capital structure - Common Equity – 53.69%; Debt – 44.79%; Preferred Stock – 1.53%. *Id*. at p. 20. The capital structure used for The Empire District Electric Company's recently rate case is also not markedly different -- 49.74% -- common equity; 6.32% trust preferred securities; and, 43.99% -- long-term debt. *In the Matter of the Tariff Filing of The Empire District Electric Company*, Report and Order, p. 26, Case No. ER-2006-0315 (December 21, 2006).

Moreover, Staff witness Barnes agreed that the actual capital structure utilized by Algonquin was a reasonable capital structure for rate-making purposes. Tr. 408.

The capital structure of Algonquin's parent as of September 30, 2006, should be used by this Commission in calculating the overall rate of return in this case. That capital structure has a basis in fact, as it is an actual capital structure; it is consistent with a capital structure recently utilized by the Commission for Missouri companies; and, Staff admits it is reasonable for rate making purposes. Imputing a lower than actual capital structure discourages investment as new investment would necessarily earn a lower than allowed return on equity because of the higher level of assumed debt in the overall rate of return.

**G. Return on Equity.**

**What return on equity should the Commission apply to Algonquin's investment in determining the proper rate of return on Algonquin's rate base?**

Algonquin recommends the Commission adopt a return on equity in the range of 11.25% to 12.00%. (Loos Dir., p. 31-33; Loos Reb., p. 8-12). This results in an overall rate of return of 9.64%, when applied to Algonquin's actual capital structure. Tr. 374.

Staff recommends an 8.06 to 9.06 cost of common equity.  Exh. 11, Barnes Dir., p. 21. Applying this to Staff's hypothetical capital structure results in an overall recommended rate of return in the range of 7.02% to 7.50%. *Id*.

The United States Supreme Court, in two frequently-cited decisions, has established the constitutional parameters that must guide the Commission in its task.  In the earlier of these cases, *Bluefield Water Works*, the Court stated that:

> Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the services are unjust, unreasonable and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment.

*Bluefield*, *supra,* 262 U.S. at 690, 43 S.Ct. at 678, 67 L.Ed. at 1181.

In the same case, the Court provided the following guidance as to the return due to equity owners:

> A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures.  The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties.

*Id.,* 262 U.S. at 692-93, 43 S.Ct. at 679, 67 L.Ed. at 1182-1183.

The Court restated these principles in *Hope Natural Gas Company*, the later of the two cases:

> '[R]egulation does not insure that the business shall produce net revenues.'  But such considerations aside, the investor interest has a legitimate concern with the financial integrity of the company whose rates are being regulated.  From the investor or company point of view it is

> important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends on the stock. By that standard the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.

*Hope Nat. Gas Co.*, *supra,* 320 U.S. at 603, 64 S.Ct. 288, 88 L.Ed. 345 (citations omitted).

Recently, the Commission had the opportunity to issue decisions in two rate cases where ROE was at issue – Case No. ER-2006-0314 (KCPL) and ER-2006-0315 (Empire). In the KCPL case, the Commission granted an 11.0% return on common equity, plus a 25 basis point adder for construction risk. The Commission awarded Empire a 10.9% ROE.

Staff witness Barnes stated that his ROE recommendation as to Algonquin would not have changed even had he known when he filed his direct testimony what the Commission would order in Empire and KCPL. Tr. 418. It is hard to see why this is not deserving of at least some consideration.

Algonquin has a significant amount of risk associated with its Missouri operations. Mr. Loos stated that he did not recall having seen a utility with 75% of its revenues associated with a single customer. Tr. 393. Further, that single customer is in a business (time share sales) that Mr. Loos would consider risky in itself. Tr. 393-394. Algonquin's operations are also extremely small, having less than 500 customers and less than 1,000 connections. Exh. 1, Loos Dir. Sch.LWL-0, Item 3.

These factors did not have much impact on Mr. Barnes. When asked what makes Algonquin 200 to 300 basis points less risky than Empire or KCPL, Mr. Barnes could only state that "they are a small water and sewer company in Missouri" and that those are "usually operated by the developer of those properties." Tr. 419. Staff witness Barnes' ROE recommendation is also below the national averages of which he is aware. Mr. Barnes stated that he believed the "allowed ROE's for water companies in the AUS utility reports have been just above 10." Tr. 428.

Staff's recommended cost of common equity does not result in a reasonable return on Algonquin's investment in the Missouri properties and would discourage investment in small water and sewer properties.[4] The Commission should instead utilize the ROE range suggested by Algonquin witness Loos - 11.25% to 12.00%. This range recognizes the risk associated with Algonquin's operations in relation to other allowed rates of return in this area of the country.

**H. Payroll Expense.**

**What is the appropriate level of payroll expense that Algonquin should be allowed to recover in its rates?**

Algonquin has three employees that are assigned to its Missouri operations and on-site. Exh. 7, Hernandez Sur., p. 2; Tr. 435. These employees hold positions described as the Wastewater/Water Utilities Superintendent, Missouri Facility Accountant and Missouri Utilities Assistant. *Id*.

Staff has recommended that 100% of the cost of the Missouri Facility Accountant be recovered, 50% of the cost of the Wastewater/Water Utilities Superintendent be recovered and that none of the cost of the Missouri Utilities Assistant be recovered. Exh. 9, Vesely Reb., p. 3-5; Tr. 454. Staff witness Vesely believes that this one and a half person staffing is all that is reasonable and necessary for running the operations.

Tr. 454.

In coming to this conclusion, Staff attempts to compare Algonquin's labor expenses with those of Silverleaf. However, it must be remembered that Silverleaf had many employees on-site that would help with operational issues, whether or not they were allocated to the utilities. *See* Tr. 449. Those employees were not available to Algonquin once it had purchased the properties. Tr. 449-450.

Staff's witness admits he has no experience operating a water or sewer utility. Tr. 452. Thus, his opinion as to what personnel may be necessary to operate such systems safely and adequately is suspect.

The positions of Wastewater/Water Utilities Superintendent and Missouri Utilities Assistant were added by Algonquin in response to complaints and a specific request from Silverleaf Resorts. Exh. 7, Hernandez Sur., p. 3; Tr. 437. Silverleaf has represented approximately 75% of Algonquin's water and sewer sales. Tr. 452. Algonquin must give due consideration to a request from a customer of this size, if it is going to be responsive to its customer's needs. Moreover, this request must be placed in the context of coming from a formerly regulated owner of these systems (Silverleaf) that would understand that additional payroll costs are likely to eventually find their way into the rates to be paid by Silverleaf. Tr. 453.

The Superintendent was added in order to address communications issues related to water outages, to assess the condition of equipment and the necessity of repairs, to follow-up concerning required safety repairs and to maintain proper oversight in regard to customer service. Exh. 7, Hernandez Sur., p. 3. Algonquin's Regional

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4 This impact si more dramatic when combined with the hypothetical capital structure suggested by the Staff.

Operations Manager, Charles Hernandez, has received no complaints since he added the Superintendent to Algonquin's Missouri operations. Tr. 449.

Payroll expense should be sufficient to provide for the costs associated with a Wastewater/Water Utilities Superintendent (95%), a Missouri Facility Accountant and a Missouri Utilities Assistant. These positions are filled by persons that are on site at the three resorts and are performing work for the utilities. The Staff's payroll expense should be increased by $84,336, to provide for these positions. Exh. 28.

**I. Rate Case Expense.**

**Should the Commission allow Algonquin to recover in its rates any allowance for the rate case expenses that it incurred in presenting this case to the Commission? If so, how much rate case expense did Algonquin prudently incur, and over how many years should the rate case expense be amortized?**

The Commission has previously stated as follows concerning attacks on the recovery of rate case expense:

> The Commission does not want to put itself in the position of discouraging necessary rate cases by discouraging rate case expense. This is a particularly treacherous area for the Commission to be addressing in that the Commission cannot be viewed as having a dampening effect upon a regulated company's statutory procedural rights to seek out a rate increase when it believes that facts so justify it. Disallowing prudently incurred rate case expense can be viewed as violating the company's procedural rights.

*In re St. Joseph Light & Power Company*, 2 Mo.P.S.C.3d 248, 260 (1993); *See also In re St. Joseph Light & Power Company*, 3 Mo.P.S.C.3d 207, 214 (1994).

The Commission further stated that "if it is determined by clear and convincing evidence that a rate case was frivolously filed, then the Commission would be under a duty to protect ratepayers from imprudently incurred costs. The Commission finds that in order to uphold SJLPC's statutory rights to seek what it believes to be a necessary rate increase, expenses for this proceeding should be allowed." *Id*.

The Commission has followed a similar approach in other cases to include: *In re Missouri Gas Energy*, 12 Mo. PSC 3d 581, 623 (September 21, 2004) ("MGE is entitled to recover its reasonable and prudently incurred cost of presenting this rate case to the Commission. Such costs are routinely accepted as a cost of doing business for which the company will be allowed to recover its costs in rates . . . ."); *In re Missouri-American Water Company*, 4 Mo.PSC 3d 205, 221-222 (November 21, 1995) ("The Commission finds that it is in the public interest to allow such expenses for the accurate and adequate presentation of Company's rate case."); *In re Missouri-American Water Company*, 2 Mo.PSC 3d 446, 449 (November 18, 1993) ("The general rule governing rate case expense provides that those expenses which are known and measurable, reasonable, necessary and prudently incurred in the preparation and presentation of the Company's case may be included in the expenses of the Company."); and, *In re Missouri Cities Water Company*, 2 Mo.PSC 3d 60, 68-70 (January 8, 1993) ("Public Counsel and Platte County Intervenors <u>want to categorize this case as 'a case that should not have been filed</u>.' The Commission does not want to put itself in the position of discouraging necessary rate cases by denying rate case expense.") (emphasis added).

This case can certainly not be said to have been frivolously filed. It is the only formal case that has ever been filed for these properties and, as pointed out by Staff itself (Exh. 15, Boateng Reb., p. 4), there will be a significant increase in the Company's revenue requirement, even if the Commission finds in Staff's favor on the tried issues. Further, neither Staff nor the OPC have identified any specific Company expense that they suggest was imprudently incurred.[5]

Staff instead argues that rate case expenses should be denied because it believes that a small company rate case proceeding should have been attempted before the formal case was filed. This position is unlawful and unreasonable for the following reasons:

1) **Statutory Rate Making Procedure was Followed**. Section 393.150, RSMo provides the sole statutory basis for rate case filings. Algonquin followed the process outlined by that statute. Section 393.150, RSMo does not contain any requirement that a public utility first pursue a small company rate case;

2) **No Regulation Requires Filing of Small Case**. Commission regulations contain no requirement that a public utility pursue a small company rate case before filing a formal rate case; and,

3) **Agreement Not a Likely Outcome**. The small company rate case procedure, as it appears in the Commission regulations, depends upon agreement between the Staff and the company in the first instance, and, ultimately, with the OPC. If the Company cannot reach agreement with these parties, its sole remedy is to file a formal rate case. 4 CSR 240-3.330(1)(G) and 4 CSR 240-3.635(1)(G). Many of the issues tried in this case were disputed in the acquisition case and no agreement was

5 Nor should they, considering that Staff spent over 1,800 hours of time on this case (excluding Staff counsel

reached. There is nothing about the formal filing process that prohibits agreement among the parties and yet no agreement was reached in this case. Tr. 498. There is no reason to believe that pursuit of the small company rate case process would have done anything but prolong the rate making process. Even Staff witness Boateng did not believe that all the issues could have been resolved in a small company rate case. Tr. 505.

Staff also argued that the case was prematurely filed because there was only one and a half months of Algonquin data included in the original test year filed by the Company. This argument is also not supported by the law and the facts.

First, there is no statute or rule that limits when a rate case can be filed. Second, by the time the case was updated, there was thirteen and half months (or more than a year) of Algonquin data that was reviewed by the parties. Exh. 3, Loos Reb., p. 3. Staff seemed to imply that the update would not have been necessary had Algonquin waited. However, updates and true-ups are common parts of the Missouri rate case process even where an entity has not changed ownership. Tr. 484-485.

Third, it should have come as no surprise that a formal case was filed in that surrebuttal testimony in the acquisition stated as much. Exh. 31, p. 4. Lastly, with the need for rate relief identified by the Staff case, the Company could not afford to suffer its losses while it waited to file a rate case. Algonquin was under earning as of the time it purchased the properties in August of 2005. Tr. 484. It is unclear how long parties believe the utility should wait before addressing this deficiency.

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time) prior to January of this year. Exh. 34; Tr. 513-514.

Faced with this need for timely rate relief, Algonquin also had a perception that its predecessor company had a lack of success with the small company rate case process. Exh. 3, Loos Reb., p. 4. This perception is understandable as these systems have had a spotty track record in regard to small company rate case filings.

The existing rates resulted from a small company rate increase initiated by a letter received at the Commission offices on April 4, 1997. *Id*. An agreement between the Commission Staff and Silverleaf was signed over a year later, on July 16, 1998. *Id*. The proposed tariff associated with this agreement was filed on July 17, 1998. *Id*. The new rates did not become effective until September 4, 1998. *Id*. Thus, the small company process took approximately seventeen months from initiation to the effective date of the new rates. *Id*.

Silverleaf later initiated another small company case on August 3, 2000. *Id*. On April 26, 2002 (approximately twenty months later), the Staff filed a request to open an earnings investigation into Silverleaf that was also designed to process the small company rate request. *Id*. This resulted in a finding on November 30, 2003 of a net underearning at Silverleaf. *Id*. However, it never resulted in new rates. *Id*.

Silverleaf is not the only company to experience a lengthy small rate case procedure. An Aqua Missouri small company proceeding recently took approximately seventeen months from its initial filing on May 17, 2005, through the effective date of new tariffs in October of 2006 (Cases No. WR-2007-0020, WR-2007-0021 and SR-2007-0023). Tr. 503, 507.

Staff witness Vesely stated that he did not believe that seventeen months was a typical turn around time for a small company rate case. Exh. 10, Vesely Sur., p. 5; Tr. 543-

544.  This is little comfort for a utility (such as Aqua Missouri or Algonquin) if its case is the one that lasts seventeen months.

Regardless, Mr. Vesely believes that seven months is a common duration for such a case.  Tr. 544-545.  Of course, if an agreement is not reached in this more "common" situation, an under earning company will go at least seven additional months without sufficient revenues, plus whatever time it takes to prepare its proposed tariffs and direct testimony related to the formal filing. Tr. 549.

Staff witness Boateng suggested that use of the small company rate case procedure "avoids expenditure for legal and consulting services."  Exh. 15, Boateng Reb., p. 5; Tr. 502-503.  However, experience would lead one to a different conclusion. Hickory Hills ultimately hired counsel to represent it in a hearing conducted subsequent to a recent small company filing (Cases No. WR-2006-0250 and SR-2006-0249).  Tr. 502-503, 577.  Aqua Missouri also had legal expense associated with its small company cases as it used in-house counsel to file its cases and hired local counsel in addition to represent it in local public hearings, stipulation negotiations and appearances before the Commission. Tr. 507-509.

Staff witness Boateng admitted that he did not look at the Aqua Missouri example before he suggested that a small company rate case would be handled for $5,000 in legal and consulting services. Tr. 525-526.  His recommendation also assumed that all issues were resolved in the small company rate case and that no follow-on formal case was required. *Id*.  Certainly, if there was a need for a follow-on formal rate case, there would be rate case expense incurred. Tr. 566.

Staff witness Vesely indicated that the $5,000 figure was a "nominal expense to provide some alternative.” Tr. 558. This “alternative” appears to have no basis in fact.

Finally, Staff witness Boateng spoke of a possible “hearing” that might be “available upon agreement.” Exh. 15, Boateng Reb., p. 6-7. No such hearing is provided for by regulation. Tr. 500. The only example of such a hearing Staff witness Boateng could provide was a recent Hickory Hills matter and maybe an Aqua Missouri matter. Tr. 500-501. However, Staff witness Johansen later indicated that neither of these cited cases represented an example of a hearing in a small company rate case proceeding. Tr. 572, 573-574.

Algonquin has prudently incurred $174,954 of rate case expense in prosecuting this case, through December 31, 2006. Exh. 16, Boateng Sur., p. 11; Exh. 32; Exh. 33. Algonquin seeks recovery of rate case expenses in the amount of $225,000, an amount that will be exceeded in this case. Tr. 480. This amount should be amortized over a five year period for purposes of reflecting this amount in the revenue requirement. Exh. 3, Loos Reb., p. 2-3. If the Commission has a concern with the impact of these rate case expense, this should be addressed through a lengthening of the amortization period, not by disallowing all rate case expenses, as suggested by the Staff.

### J. Rate Design.

**Should the Commission’s order establish separate rates for each of Algonquin’s three service territories, or should the Commission’s order establish a unified rate for water service to Algonquin’s service to the Ozark Mountain and Holiday Hill service territories?**

Algonquin currently has single rates for water and sewer services that are applicable to all three resorts and has had such single rates since Holiday Hills and

Ozark Mountain were certificated in 1994. Tr. 190. There has been no public call for a change to this rate design approach. *Id*.

In this case, Staff proposes separate rates for each of the resorts. Making the move to district-specific pricing in this case may result in a strange result for customers. Under Staff's current revenue requirement and rate design, moving to district-specific pricing would create a slight decrease in rates for Holiday Hills water customers (other than irrigation), while the system as a whole would be increasing rates. Tr. 186; 190-192.

If the single rate for all three resorts is abandoned, Algonquin does not object to a separate rate for water and sewer services at the Timber Creek resort and sewer services at the Ozark Mountain resort. Exh. 3, Loos Reb., p. 22. However, Algonquin believes that a single potable water rate should be adopted for the Ozark Mountain and Holiday Hills resorts because of the operational and geographic similarities between these two operations. *Id*. at p. 23. Some of these similarities include:

1) Silverleaf classifies Ozark Mountain and Holiday Hills as "drive to resorts." Timber Creek is considered a "weekend resort."
2) Silverleaf is the only customer at Timber Creek. While Silverleaf is by far the predominant customer at Ozark Mountain and Holiday Hills, Algonquin serves other customers.
3) Ozark Mountain and Holiday Hills are located in relatively close proximity. Ozark Mountain and Holiday Hills are located about 20 miles from one another while Timber Creek is over 200 miles from Holiday Hills and even further from Ozark Mountain.

*Id*.

Regardless of what approach is taken to the design of potable water rates, a separate irrigation rate for delivery of non-potable water should still be established. Untreated water is supplied at Holiday Hills and used to irrigate the golf course located on the resort. Exh. 1, Loos Dir, p. 36. No charge is currently found in Algonquin's tariff for this service. Both Algonquin and the Staff propose that such a charge be established in this case.

**K. Rate Mitigation.**

**Should any increase in rates be phased-in, or be otherwise mitigated? If so, how?**

The Commission does not have the authority to require phase-in of a water or sewer company's rate increase over its objection. Section 393.155, RSMo specifically permits the Commission to implement a phase-in of rates for an electrical corporation where the increase is "primarily due to an unusually large increase in the corporation's rate base . . . ." No such authority is provided for other utility industries.

The express authorization for a phase-in of rates for electrical corporations implies the exclusion of such authority for other utility industries. *See Harrison v. MFA Mutual Insurance Corporation*, 607 S.W.2d 137 (Mo banc 1980); *see also Bridges v. Van Enterprises*, 992 S.W.2d 322 (Mo.App. SD 1999).

This being said, Algonquin does not oppose a phase-in for any part of an individual rate (as opposed to the overall revenue requirement) increase beyond 100%. Tr. 182, 184; Exh. 1, Loos Dir., p. 37. This assumes, however, that a phase-in would provide Algonquin with carrying costs to address the loss of the use of dollars necessary for Algonquin to have an opportunity to earn a reasonable return on its investment. Algonquin witness Loos described a method whereby these carrying costs could be addressed in the second step of such a phase-in by deferring a return on the revenues associated with the second phase. Tr. 185. Absent such treatment of carrying costs, a phase-in will certainly deny Algonquin the opportunity to receive a reasonable return on its investment and may not be ordered.

WHEREFORE, Algonquin respectfully requests that the Commission consider this Brief and, thereafter, issue its order granting relief that is consistent with the foregoing.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I do hereby certify that a true and correct copy of the foregoing document has been sent by electronic mail this 20th day of February, 2007, to:

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