

Exhibit No.:
Issues: Rate Case Expense, Capital Structure,
Cost of Capital, Plant Capacity, Plant in
Service, Contribution in Aid of
Construction, Depreciation Expense
Rates, and Rate Design
Witness: Larry W. Loos
Exhibit Type: Rebuttal
Sponsoring Party: Algonquin Water Resources of
Missouri, LLC
Case No.: WR-2006-0425 & SR-2006-0425
(Consolidated)
Date: December 28, 2006

MISSOURI PUBLIC SERVICE COMMISSION

**CASE NO. WR-2006-0425
SR-2006-0426
(Consolidated)**

REBUTTAL TESTIMONY

OF

LARRY W. LOOS

ON BEHALF OF

ALGONQUIN WATER RESOURCES OF MISSOURI, LLC

JEFFERSON CITY, MISSOURI

FILED²


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**Missouri Public
Service Commission**

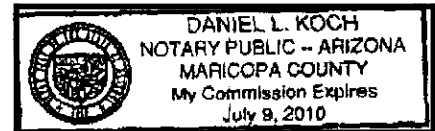
Algonquin Exhibit No. 3
Case No(s) WR-2006-0425
Date 1-22-07 Rptr KF

AFFADAVIT OF L. W. LOOS

L. W. Loos, being first duly sworn, deposes and says that he is the witness who sponsors the accompanying testimony entitled "Rebuttal Testimony of Larry W. Loos"; that said testimony and schedules were prepared by him and/or under his direction and supervision; that if inquiries were made as to the facts in said testimony and schedules, he would respond as therein set forth; and that the aforesaid testimony and schedules are true and correct to the best of his knowledge.


Larry W. Loos

State of Arizona
County of Maricopa
SUBSCRIBED and sworn to
Before me this 28th day of December 2006.





Notary Public

My commission expires: July 9th, 2010

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1 Before the Missouri Public Service Commission
2 CASE NO. WR-2006-0425
3 SR-2006-0426
 (Consolidated)

4 Rebuttal Testimony of Larry W. Loos

5 **INTRODUCTION**

6 **Q. Please state your name and business address.**

7 A. Larry W. Loos, 11401 Lamar, Overland Park, KS 66211.

8 **Q. Are you the same Larry W. Loos who previously filed direct testimony in**
9 **this matter?**

10 A. Yes, I am.

11 **Q. What is the purpose of your prepared rebuttal testimony?**

12 A. I will respond to the prepared direct testimony of various staff witness. The
13 issues I address include:

14 1) Rate Case Expense – Staff Witness Agyenim Boateng;

15 2) Rate of Return – Staff Witness Matthew J. Barnes;

16 3) Plant capacity – Staff Witness James A. Merciel;

17 4) Plant in Service – Staff Witness Graham A. Vesely;

18 5) Contributions in Aid of Construction – Staff Witness Graham A. Vesely;

19 6) Depreciation expense rates – Staff Witness Rosella L. Schad; and,

20 7) Rate Design – Staff Witness James M. Russo.

1 **RATE CASE EXPENSE**

2 **Q. What issues does Mr. Boateng raise?**

3 A. Mr. Boateng raises several issues in his direct testimony. While I do not
4 necessarily agree with his comments and recommendations, I address only
5 one of these issues in my rebuttal testimony. That issue is the level of rate
6 case expense Mr. Boateng recommends the Company be permitted to
7 recover through rates.

8 **Q. What is Mr. Boateng's recommendation with respect to rate case**
9 **expense?**

10 A. Mr. Boateng recommends that the Company not be allowed to recover any of
11 the cost the Company incurred (and is incurring) in preparing and prosecuting
12 this rate case. Mr. Boateng suggests that if the Commission determines that
13 the Company is entitled to some rate case expense, the amount be limited to
14 \$5,000. Mr. Boateng's recommendation is set forth at Page 10 of his
15 prepared direct testimony.

16 **Q. What rate case expense does the Company propose to recover?**

17 A. The Company originally estimated a total rate case cost of \$225,000
18 amortized over a period of 5 years. This results in an annual rate case
19 expense of \$9,000 per utility per resort (\$18,000 for the sewer utility and
20 \$27,000 for the water utility).

21 I recommend that the Company be permitted to collect through rates all
22 costs associated with the preparation and prosecution of this rate case, with

1 an annual allowance of \$9,000 per utility per resort until fully recovered, or
2 until a new amount is set in the Company's next rate case

3 **Q. What is Mr. Boateng's rational for disallowing recovery of any rate case**
4 **expense?**

5 A. Mr. Boateng cites two reasons:

6 1) The Company should have followed the informal rate process

7 2) The Company filed its application prematurely

8 **Q. Do you believe that the Company filed its application prematurely?**

9 A. No, I do not. The Company clearly needs rate relief as evidenced by the
10 Company's filing and by Staff recommendations in this case. With the need
11 for rate relief of the magnitude requested by the Company and recommended
12 by Staff, the Company reasonably and prudently filed when it did.

13 **Q. Do you believe the lack of Company specific data poses a problem as**
14 **suggested by Mr. Boateng?**

15 A. No, I do not. The fact that the September 30, 2005 test year represented ten
16 and one-half months of Silverleaf operations and one and one-half months of
17 Algonquin operation does not represent a barrier to developing a reasonable
18 measure of test period operations for rate case purposes. Since the
19 Company updated its original filing in its entirety to reflect September 30,
20 2006 operations, the test year ultimately used by the Company reflects a full
21 year's operations by Algonquin.

1 I find it curious that Staff on the one hand criticizes the Company for its
2 selection of test year because it includes a period when Silverleaf owned and
3 operated the systems when the Staff then:

4 1) Seems to ignore the updated data in its Schedules by starting with data for
5 the twelve months ended September 30, 2005; and,

6 2) Seems to focus on Silverleaf operations in the Staff data requests.

7 **Q. What factors did the Company consider in regard to the informal**
8 **ratemaking process?**

9 A. The considerations that went into the Company's decision primarily center on
10 the lack of perceived success that Silverleaf had with the informal process.

11 **Q. What was the Silverleaf experience with the ratemaking process?**

12 A. The existing rates resulted from a small company rate increase initiated by a
13 letter received at the Commission offices on April 4, 1997. An agreement
14 between the Commission Staff and Silverleaf was signed over a year later, on
15 July 16, 1998. The proposed tariff associated with this agreement was filed
16 on July 17, 1998. The new rates did not become effective until September 4,
17 1998. Thus, the small company process took approximately seventeen
18 months from initiation to the effective date of the new rates. Silverleaf later
19 initiated another small company case on August 3, 2000. On April 26, 2002
20 (approximately twenty months later), the Staff filed a request to open an
21 earnings investigation into Silverleaf that was also designed to process the
22 small company rate request. This resulted in a finding on November 30, 2003
23 of a net underearning at Silverleaf. However, it did not result in new rates and

1 Silverleaf's attempts to file a small company case in December of 2003 and
2 April of 2004 were not found sufficient for the Commission to process the
3 requests.

4 **Q. What course did the Company decide to follow?**

5 A. With the apparent lack of success by Silverleaf, the need the Company has
6 for rate relief (as verified in the Staff Schedules), the open ended nature of
7 the informal process, and the nature of the issues the Company desired to
8 have resolved, filing a general rate case was clearly the only option.

9 **Q. What is the nature of the issues that the Company desires be addressed**
10 **and resolved?**

11 A. The Company's concern primarily centers on the inadequate level of rate
12 base that Staff insists that Algonquin has devoted to public service. This
13 issue apparently goes back to 1994 when Silverleaf was first certificated.
14 More recently, Staff made its position clear in the acquisition case (Case No.
15 WO-2005-0206). I understand that the Commission has never specifically
16 determined the level of rate base which the Company is entitled to earn a
17 return. The Company believes that the Staff's position is unreasonable and
18 desires that the issue be resolved at a level that is more reasonable so that
19 going forward, conditions permitting, the Company can earn a return and
20 recover investment more in line with the value of the facilities its has devoted
21 to public service. Clearly, the Staff's position presented another obstacle to
22 the Staff and Company agreeing in the informal process to a level acceptable
23 to the Company.

1 **RATE OF RETURN**

2 **Q. What rate of return issues do you address?**

3 A. I will address two issues raised by Staff Witness Barnes. These issues are
4 capital structure and return on equity.

5 **Q. With regard to capital structure, what capital structure does Mr. Barnes**
6 **recommend?**

7 A. As shown in his Schedule 19, Mr. Barnes recommends the use of a
8 hypothetical capital structure consisting of 47.88% equity and 52.12% long
9 term debt. Mr. Barnes' hypothetical capital structure is based on the weighted
10 average of the capital structures of the four investor-owned water companies
11 he uses as a proxy.

12 As I show in my Schedule ___ (LWL-4 UPDATED), I recommend a capital
13 structure of 65.18% equity and 34.82% long term debt (and convertible
14 debentures). My recommended capital structure is based on the actual
15 capital structure as of December 31, 2005 of Algonquin's parent, Algonquin
16 Power Income Fund.

17 **Q. What is the actual capital structure as of September 30, 2006?**

18 A. As of September 30, 2006, the capital structure of Algonquin Power Income
19 Fund is 58.21% equity and 41.79% long term debt (and convertible
20 debentures).

21 **Q. Why does Mr. Barnes use a hypothetical capital structure?**

1 A. At Page 11, Line 21, Mr. Barnes answers that very question by stating
2 "because AlgonquinMO's operations are part of a division of Algonquin
3 Power. Consequently, AlgonquinMO does not have stock that is publicly
4 traded in the United States' capital markets"....."the company's stock is
5 traded on the Toronto Stock Exchange. The Staff is not familiar with
6 Canadian markets. Staff cannot provide informed judgment as to whether the
7 costs of capital in Canada are similar to those in the United States."

8 **Q. Do you consider Mr. Barnes' rational persuasive?**

9 A. No, I do not. The fact that the Staff is not familiar with Canadian markets is
10 no reason to abandon actual capital structure. If Staff is not comfortable with
11 Canadian markets, Staff should do the research necessary to become
12 reasonably informed. In this day of a global economy, the increasing
13 ownership of utilities by outside US companies, and by US companies whose
14 primary purpose is something other than operating utility property, familiarity
15 with other markets is imperative if utility operations and costs are to be
16 reasonably evaluated.

17 **Q. Are you familiar with Canadian markets?**

18 A. Yes, I am to some degree. As a developed country, Canadian markets are in
19 many respects similar to ours. While there is a difference in the value of the
20 Canadian dollar relative to the US dollar, I believe the relative costs of capital
21 are not materially different. With a global economy, so long as the economy
22 is stable and the threat of nationalization is not material; there is little
23 difference between financing so long as the entities primarily operate in

1 developed countries. This is especially true with Canada, which shares a
2 number of common cultural and economic roots with the US.

3 **Q. Mr. Barnes notes on Page 12, Line 6, that "Algonquin Power is**
4 **organized differently than water companies in the United States.**
5 **Algonquin Power is organized under operating divisions rather than**
6 **subsidiaries, which is unusual for a United States water company." Do**
7 **you have any observation?**

8 **A.** Yes, I do. I am unaware of whether water utilities are organized into
9 operating divisions. However, the concept of operating divisions is something
10 that I presume Mr. Barnes is familiar with since Aquila's electric and gas
11 operations are so organized. Additionally, I should note that there are
12 separate corporate entities in the Algonquin Power structure, one of which is
13 the operating company in this case – Algonquin Water Resources of Missouri,
14 LLC.

15 **Q. How does Mr. Barnes' recommended cost of long term debt compare**
16 **with your recommendation?**

17 **A.** Our recommendations are similar. Mr. Barnes recommends a cost of 6.09%
18 based on the average cost of his comparable companies. Based on
19 Algonquin Power Income Fund's actual cost, I recommend a cost of 6.05%
20 (6.26% including the cost implications of Algonquin's convertible debentures.)

21 **Q. How does Mr. Barnes' recommended cost of equity compare with your**
22 **recommendation?**

1 A. Our recommendations are significantly different. Mr. Barnes recommends a
2 cost of equity in the range of 8.06% to 9.06%. I recommend a cost of 12%.

3 **Q. How does Mr. Barnes' development of his recommendation differ from**
4 **yours?**

5 A. Mr. Barnes approaches the development of his recommendation in much the
6 same manner as I do. We use three of the same water companies in our
7 proxy group. He uses Middlesex Water Company as a fourth where as I use
8 Southwest Water. We both use a discounted cash flow approach. The
9 difference appears to center on what we view as important. Differences in
10 our individual measures are not as great as our differences in how the
11 individual elements should be weighted and combined.

12 **Q. Please explain.**

13 A. The DCF approach (formula) consists of two terms. These are the dividend
14 yield and growth.

15 With respect to dividend yield, Mr. Barnes includes allowance based on
16 expected (forecast) dividends in 2007 and the average of the high and low
17 prices during June through September 2006. I rely on the Value Line forecast
18 of dividends and market price for the 2007 to 2009 period to establish a lower
19 limit. I look at forecast dividends and the forecast book value to establish the
20 upper limit.

21 **Q. How do these dividend yield terms compare?**

1 A. Mr. Barnes includes an allowance of 2.88%. This allowance compares
2 reasonably well with my low end value of 2.50%. The high end of my range
3 amounts to 5.75%.

4 **Q. What are the implications of the difference between book value and**
5 **market price?**

6 A. The ratio of forecast dividends and forecast book value is critical since the
7 resultant value (rate of return on common equity) will be applied to a rate
8 base which is based on book value. By focusing only on the market yield, Mr.
9 Barnes does not provide allowance for sufficient funds to payout dividends at
10 the level he determines is required.

11 **Q. What are your differences with Mr. Barnes regarding growth?**

12 A. Here again, Mr. Barnes and I share some agreement. However, there is
13 again a difference in focus. Mr. Barnes develops his growth term as the
14 average of historical and forecast growth in per share dividends, earnings,
15 and book value. Whereas for his dividend term Mr. Barnes' focus is on
16 market price, for his growth term he looks more toward book value measures.
17 Mr. Barnes uses a growth term in the range of 5.18% to 6.18%.

18 I also, look at these "book" measures to establish the low end of 5.50%.
19 In addition to these "book" measures I also focus on growth in per share
20 market price and cash flow. These latter measures I believe are the more
21 relevant and tend to establish an upper limit of 9.50%.

1 From both my perspective as an investor and professionally, I know that
2 the long term value of the enterprise is driven by cash flow. I also understand
3 that while there is some value in growth of dividends, more important is the
4 growth (increase) in price per share. I also view historical performance as of
5 secondary importance since if I buy a security I am buying performance in the
6 future not in the past. The only relevance of past performance is to the
7 degree that I expect past performance to predict the future.

8 **Q. You indicate that your development of rate of return on equity shares**
9 **common features with Mr. Barnes. How do you differ?**

10 A. Mr. Barnes combines a dividend yield based on market price (2.88%) with a
11 growth term (5.18% to 6.18%) that is based on book measures. I develop
12 dividend yield and growth terms on the basis of both book and market
13 measures. As I show in my Schedule __ (LWL-4 UPDATED), when I
14 combine my book based dividend yield (5.75%) with my growth term based
15 on market measures (9.50%), I get a high end limit of 15.25%. When I
16 combine my dividend yield based on market price (2.50%) with my growth
17 term based on book measures (5.50%), I get a low end extreme of 8.00%. It
18 is this combination of yield based on market price of the stock and growth
19 based on book measures that Mr. Barnes relies on to determine his rate of
20 return on equity in the range of 8.06% to 9.06%.

21 As I demonstrate in the above, the combination that Mr. Barnes relies on
22 mixes book and market measures. In my Schedule __ (LWL-4 UPDATED), I
23 show values if the inconsistencies between book and market measures are

1 eliminated. As I show on Line 4 of Schedule __ (LWL-4 UPDATED), if I
2 combine dividend yield based on market price (2.5%) with growth based on
3 price and cash flow measures (9.50%), I get a value of 12.00%. If I combine
4 dividend yield based on book value (5.75%) with growth based on book
5 measures (5.5%), I get a value of 11.25%. Thus by eliminating the classical
6 mixing apples and oranges that Mr. Barnes relies upon in making his
7 recommendation, I get a value within the relatively narrow range of 11.25% to
8 12.00%.

9 **Q. What is your recommendation?**

10 A. I recommend the Commission adopt a return on equity in the range of 11.25%
11 to 12.00%. The values which are used to establish this range are combined
12 in a manner so that their measures are consistent.

13 **PLANT CAPACITY**

14 **Q. What is the issue regarding plant capacity?**

15 A. Staff Witness James A. Merciel, Jr. proposes to reduce plant investment by
16 what he terms excess capacity.

17 **Q. Do you believe that the Algonquin water and wastewater systems have**
18 **excess capacity?**

19 A. No, I do not. However, in my rebuttal testimony, I do not address the
20 question of whether excess capacity exists, but whether Mr. Merciel has
21 reasonably measured excess capacity if it does exist.

22 **Q. Do you believe Mr. Merciel's measure reasonable?**

1 A. No, I do not. Mr. Merciel's calculations fail to consider real world
2 considerations which if considered would tend to reduce Staff's proposed
3 adjustment considerably. Mr. Merciel's adjustment fails in two respects:

4 1) Mr. Merciel assumes that cost is a linier function of capacity and that no
5 economies of scale exist. Neither of the assumptions are correct. Unit
6 cost of capacity tends to decline as plant capacity increases. Further plant
7 sizes may not be available to exactly match the capacity needs suggested
8 by Mr. Merciel;

9 2) Mr. Merciel fails to consider the need to have some capacity in reserve for
10 growth and adverse conditions.

11 **Q. Do you have any recommendation?**

12 A. I recommend that the Commission reject Mr. Merciel's proposed adjustment
13 because he has failed to demonstrate that his adjustment properly reflects
14 these real world considerations.

15 In the event the Commission believes such an adjustment is appropriate,
16 Mr. Merciel's proposed adjustments should be modified to reflect not less
17 than a 20% reserve allowance. By including recognition of a 20% reserve
18 allowance, some consideration will be given to the real world need to size
19 equipment to meet abnormal demands and a limited amount of growth. In
20 addition, an additional 20% increment should be included to reflect the per
21 unit of capacity economies of scale associated with the larger sized
22 equipment, Mr. Merciel claims Silverleaf was imprudent in installing.

1 **PLANT IN SERVICE**

2 **Q. What are the issues regarding plant in service?**

3 A. In addition to the excess capacity and excess cost (associated with Holiday
4 Hills Well #2) issues, there are two other fundamental issues with regard to
5 plant:

6 1) What criteria should be used to determine plant in service and rate base
7 value?

8 2) Should the Company's books and rate base reflect plant installed prior to
9 1993 but not recorded on Silverleaf's books?

10 **Q. Please describe the first issue.**

11 A. As I addressed in my direct testimony, the books and records that were
12 maintained by Silverleaf leave a lot to be desired. While Silverleaf maintained
13 plant balances since 1994, Staff has not been able to verify, through normal
14 audit procedures, the plant levels reported on Silverleaf's, and now
15 Algonquin's, books. For example, in Schedule ___ (LWL-3 UPDATED), I show
16 plant in service as of September 30, 2005 in the amount of \$6.3 million.
17 Summarizing Mr. Vesely's schedules, I find his plant balance as of September
18 30, 2005 amounts to \$4.4 million. To this book amount, he deducts \$0.6
19 million to determine the Staff book balance as of September 30, 2005 of \$3.8
20 million. Thus the Staff balance amounts to \$2.5 million less than the book
21 amount I identified from the information set forth in Silverleaf/Algonquin's
22 books (as adjusted to reflect unrecorded plant installed prior to 1993). Of this

1 \$2.5 million difference, \$1.9 million relates to the unrecorded pre 1993 plant
2 and \$0.6 million relates to post 1993 plant additions.

3 **Q. How does Mr. Vesely develop the Staff book balance?**

4 A. Mr. Vesely describes his development of this balance in some detail
5 beginning at Page 10 of his prepared testimony. As he describes, Staff
6 develops plant balances by identifying the costs of individual projects for
7 those projects for which Staff has documentation in the form of purchase
8 orders, invoices, construction estimates and budgets, letters concerning
9 construction activities, and other related documents. In Schedules GAV-2A
10 through GAV-2E, Mr. Vesely demonstrates the detailed process he follows.

11 **Q. Do you take exception with the detailed process Mr. Vesely follows?**

12 A. No, I do not. However, though I have no problem with the integrity of Mr.
13 Vesely's process, I do have a problem with the completeness of the data on
14 which he relies.

15 The Staff approach, though thorough, is biased toward understating plant
16 in service. Staff assumes a perfect world. Staff assumes the utility has
17 maintained all records (in this case, at least as far back and possibly before
18 1982) and can locate all records. This assumption, while perhaps reasonable
19 for many utilities, is clearly unreasonable based on information regarding the
20 manner in which Silverleaf maintained its books, the nature of Silverleaf's
21 business as a resort operator and developer, deficiencies that have been

1 identified in the Silverleaf books and the fact that the systems did not become
2 subject to Commission regulation as a utility until 1994.

3 I trust that Mr. Vesely would agree that if Silverleaf cannot properly reflect
4 plant balances in its books, one cannot reasonable expect they would
5 maintain the underlying detail.

6 With the inherent bias toward understating the plant balances, the
7 balances developed by Mr. Vesely most likely understate the cost of the
8 property devoted to public service, not only for the pre 1993 plant but for the
9 post 1992 property as well. At page 26, Mr. Vesely acknowledges that
10 property was in service prior to 1994.

11 **Q. Do you place any reliance on the Staff balances?**

12 A. Yes, I do. The plant balances developed by Staff represent the absolute
13 minimum level of plant. I recognize that Staff balances understate plant in
14 service for property installed prior to 1993 and likely understate balances for
15 plant installed post 1992. None of this pre 1994 property is included in the
16 Staff balances or Silverleaf balances. This demonstrates that the records that
17 Staff relies on are incomplete and that Staff has understated plant. Likewise,
18 it demonstrates that Silverleaf's records are likewise deficient. While the
19 records prior to 1993 might be deficient based on utility standards, I am
20 unaware of any claim that they are deficient based on other non utility
21 standards.

1 **Q. Do you place greater reliance on the balances reported by**
2 **Silverleaf/Algonquin?**

3 A. Not really. Similar to balances developed by Staff, Silverleaf's books do not
4 reflect cost associated with any plant placed into service prior to 1993. Thus,
5 Silverleaf's books are equally questionable. With respect to plant installed
6 subsequent to 1993, the balances shown on the books exceed the amounts
7 calculated by Staff. These differences may be due to a combination of two
8 contributing factors -- either an understatement by Staff or an overstatement
9 by Silverleaf. As I indicated above, the Staff amount cannot be overstated.
10 The balances shown on the books of the Company may be either under or
11 over stated.

12 **Q. Do you have any observation regarding the reasonable level?**

13 A. Yes, I believe that the reasonable level, in so far as the post 1993 plant, lays
14 some place between the two extremes. As I discussed in my prepared direct
15 testimony, Silverleaf's books and records do not reflect plant investment
16 installed prior to 1993 that is used in providing service to customers. While
17 we do not know the precise cost of the plant when originally constructed, nor
18 the precise facilities, I make a reasonable estimate and include that estimate
19 in rate base. The Company has also reflected that investment on its books.

20 Staff does not include allowance for the cost of these facilities even
21 though Staff recognizes these facilities are used to provide service.

22 **Q. What is your recommendation?**

1 A. Absent a more definitive measure, and prior to consideration of Staff
 2 adjustments for excess capacity and excess cost, I recommend that the
 3 Commission establish \$6,445,484 as the total Company plant in service
 4 balance as of September 30, 2006. This amount is broken down by utility and
 5 resort in the following:

Algonquin Water Resources of Missouri, LLC Proposed Plant in Service Balances Prior to Adjustment for Excess Capacity and Excess Cost As of September 30, 2006								
Description	Water Utility				Sewer Utility			Algonquin
	OM	HH	TC	Total	OM	TC	Total	Total
Total Plant in Service	874,130	2,750,838	1,014,300	4,639,268	960,746	845,470	1,806,216	6,445,484

6

7 **Q. How do you arrive at the amounts you recommend?**

8 A. Very simply, the amounts I recommend include allowance for the pre 1993
 9 investment of \$1,914,032 as set forth in my Schedule __ (LWL-3 UPDATED)
 10 plus for the post 1992 property an amount of \$4,531,453. This latter amount
 11 is equal to the midpoint between the Staff recommended amount of
 12 \$4,234,202 (before reduction for excess cost and excess capacity) and the
 13 amount I recommend of \$4,740,455 in my prefiled testimony.

14 **Q. In your prior response, you suggest that there may be a more definitive
 15 method to determine the original cost balance. Please explain.**

16 A. The only method that I know to definitively determine the plant in service used
 17 to provide service to customers is to develop a complete inventory of all
 18 facilities owned by Algonquin that are used to provide service. Once this
 19 inventory is developed, its cost can be developed at current levels and then

1 restated to reflect cost levels at the time the property was originally installed.
2 This method has been used on many occasions when books and records of a
3 utility for one reason, or another, do not properly reflect the plant actually in
4 service.

5 **Q. Do you recommend that the Company undertake such an analysis?**

6 A. No, I do not. I do not believe the benefits of such a study are sufficient to
7 justify its cost.

8 **CONTRIBUTIONS IN AID OF CONSTRUCTION**

9 **Q. What is the issue with regard to contributions in aid of construction**
10 **(CIAC)?**

11 A. Staff imputes approximately \$0.6 million of phantom CIAC, which reduces
12 rate base by a like amount.

13 **Q. Why do you refer to this \$0.6 million as phantom CIAC?**

14 A. Staff's imputation is based on no definitive data. Staff's rationale is very
15 simply that because Silverleaf's tariff has a provision that requires CIAC, rate
16 base should be reduced by an amount that assumes that contributions were
17 collected as the tariff provides. These contributions imputed by Staff in no
18 way meet the requirements specified by the tariff that Staff cites to support its
19 recommendation.

20 **Q. What are the tariff requirements?**

21 A. The tariff requires:

22 1) A written application for a main extension

- 1 2) A Company estimate of the cost of such an extension
- 2 3) A contract between the applicant and Company for such extension
- 3 4) The applicant tender to Company the estimated cost (in the alternative the
- 4 applicant may construct at its own cost the required facilities)

5 **Q. Did Silverleaf follow these requirements?**

6 A. Based on my investigation, I found no evidence that Silverleaf ever required a
7 contribution from any customer or "developer," much less accepted an
8 amount that was tendered. Further, since Silverleaf was as far as I know, the
9 only developer and by far the largest customer in terms of both number of
10 accounts and sales volumes, I find that the concept of contributions makes no
11 sense.

12 **Q. Mr. Vesely states at Page 15, Line 1 that Silverleaf's tariffs require CIAC**
13 **to "help alleviate the burden of the utility of having to finance" the cost**
14 **of extending mains. Do you agree?**

15 A. No, I do not. I consider CIAC to represent a mechanism to help preserve
16 intergenerational equity between customers. The CIAC represents a
17 requirement to charge new customers (either directly or through a developer)
18 an amount sufficient to offset the difference between the investment
19 supported through rates charged the new customer and the costs incurred by
20 that customer. For example, rate levels might support 100 feet of main
21 extension and a service investment. An equitable extension policy might then
22 provide that the first 100 feet of an extension is provided by the utility at no
23 charge to the customer. The customer would then pay the cost associated

1 with the portion that exceeds the 100 foot limit. Thus, a new customer that
2 requires an extension of 150 feet would pay the utility directly for 50 feet of
3 the extension through a contribution and the balance (100 feet) through the
4 rates charged.

5 **Q. Does Mr. Vesely's interpretation provide intergenerational equity?**

6 A. No, Mr. Vesely's proposal to deduct from rate base phantom contributions
7 exacerbates inequities. The existing customers did not pay for extending
8 lines, yet Mr. Vesely suggests that the rates charged existing customers be
9 reduced as if they had. The rates to existing customers will be artificially
10 reduced. While the rates to new customers will likewise be reduced, these
11 new customers will be charged an entry fee equal to the cost of the entire line
12 extension and the service connection. This treatment is hardly fair and
13 introduces undue discrimination.

14 Any discriminatory treatment will be reduced if the Company's rate base is
15 not artificially reduced. If discrimination is to be eliminated, the Company's
16 extension policy needs to be modified to reflect the investment recovered in
17 existing rates and to charge new customers only the costs associated with
18 extensions that exceed the threshold level.

19 **Q. Do you have any further observations concerning Mr. Vesely's**
20 **proposal?**

21 A. Yes, I do. Not only does Mr. Vesely's treatment result in intergenerational
22 inequities, it serves to reward Algonquin's predominate customer, Silverleaf.

1 Silverleaf did in fact not charge new customers, including its own
2 developments for costs as required by the tariff. Even so, Mr. Vesely, would
3 reduce Silverleaf's rate as if it did.

4 **DEPRECIATION EXPENSE RATES**

5 **Q. Do you have any observations with regard to the depreciation expense**
6 **rates recommended by Ms Schad?**

7 A. Yes, I do. While I do not have a major problem with the depreciation rates
8 proposed by Ms Schad, I note that relying on those rates results in some
9 excessively high reserve ratios. I suggest given these high ratios the
10 Commission approve the depreciation rates I recommend in Schedule ____
11 (LWL-3 UPDATED). I further recommend that the existing reserve balance
12 as of September 30, 2006, be calculated using those rates.

13 **RATE DESIGN**

14 **Q. Did you review the rate design proposed by Staff witness Russo?**

15 A. Yes, I did. With one exception, I have no problem with Mr. Russo's overall
16 recommended design of rates. The single exception relates to separate rates
17 for the three resorts. I have no problem with the separate rate for Timber
18 Creek. I recommend however that a single water rate be adopted for Ozark
19 Mountain and Holiday Hills.

20 **Q. Why do you recommend Ozark Mountain and Holiday Hills be**
21 **combined?**

1 A. Ozark Mountain and Holiday Hills share a number of similarities. At the same
2 time, there are a number of differences between these two resorts and
3 Timber Creek. Some of these similarities include:

4 1) Silverleaf classifies Ozark Mountain and Holiday Hills as "drive to resorts."
5 Timber Creek is considered a "weekend resort."

6 2) Silverleaf is the only customer at Timber Creek. While Silverleaf is by far
7 the predominant customer at Ozark Mountain and Holiday Hills, Algonquin
8 serves other customers.

9 3) Ozark Mountain and Holiday Hills are located in relatively close proximity.
10 Ozark Mountain and Holiday Hills are located about 20 miles from one
11 another while Timber Creek is over 200 miles from Holiday Hills and even
12 further from Ozark Mountain.

13 **Q. Does this complete your rebuttal testimony?**

14 A. Yes, it does.