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Transcript Exhibit(s)

Docket #(s): WS-02676A-12-0196

Exhibit # : A-6, A-7, A8, A-9, A-10, A-11, A-12, A-13
A-14, A-15, A-16 A-17 & A-18
Part 3 of 6

Corporation Commission
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16 2013

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BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF RIO RICO UTILITIES, INC., AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANTS AND PROPERTY AND FOR INCREASES IN ITS WATER AND WASTEWATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.	DOCKET NO: WS-02676A-12-0196

REJOINDER TESTIMONY OF

THOMAS J. BOURASSA

COST OF CAPITAL

March 8, 2013

EXHIBIT
tabbies
A-6
ADMITTED

Table of Contents

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I. INTRODUCTION AND QUALIFICATIONS

Q. PLEASE STATE YOUR NAME AND ADDRESS.

A. My name is Thomas J. Bourassa. My business address is 139 W. Wood Drive, Phoenix, Arizona 85029.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?

A. I am testifying in this proceeding on behalf of the applicant, Rio Rico Utilities, Inc. ("RRUI" or the "Company").

Q. DID YOU ALSO PREPARE REBUTTAL TESTIMONY ON THOSE ISSUES IN THIS DOCKET?

A. Yes, my rebuttal testimony on rate base, income statement, revenue requirement and rate design is being filed in a separate volume at the same time as this testimony. In this volume, I present my cost of capital rejoinder testimony. Also attached are two exhibits, which are discussed below.

II. SUMMARY OF REJOINDER TESTIMONY AND THE PROPOSED COST OF CAPITAL FOR THE COMPANY

A. Summary of Company's Rejoinder Recommendation

Q. WHAT IS THE SCOPE OF THIS VOLUME OF YOUR REJOINDER TESTIMONY?

A. I will provide updates of my cost of capital analysis and recommended rate of return using more recent financial data. I also will provide rejoinder testimony as appropriate to the surrebuttal testimony of Staff witness John Cassidy and RUCO witness William Rigsby.

Q. HAS THE COMPANY CHANGED ITS POSITION WITH RESPECT TO THE CAPITAL STRUCTURE?

A. Yes, the Company is now accepting Staff's and RUCO's 100 percent equity capital structure.

Q. WHY IS THE COMPANY ADOPTING THE OTHER PARTIES' POSITIONS ON THE CAPITAL STRUCTURE?

A. To eliminate issues between the parties. In direct, Staff rejected our recommended capital structure and recommended 100 percent equity capital structures.[1] Then, in his surrebuttal, Mr. Rigsby changed his position – from agreeing with our direct position to agreeing with Staff's direct position.[2]

Q. BUT DIDN'T RRUI COMMIT TO INFUSE 20 PERCENT DEBT AS PART OF RRUI'S LAST RATE CASE?

A. Yes. RRUI upheld its commitment to infuse 20 percent debt and did so in its application and rebuttal testimony, however to eliminate issues between the parties RRUI is adopting Staff's and RUCO's recommended capital structure.

Q. HAVE YOU UPDATED YOUR COST OF CAPITAL ANALYSIS?

A. Yes, for two reasons. First, both Staff and RUCO provided recent updates to their respective cost of capital analyses. It has been approximately two months since I prepared my rebuttal analysis and I felt it was necessary. Second, I updated my analysis to reflect the change in the capital structure, which has less financial risk. The table below summarizes the results of my updated analysis:

Method	Low	High	Midpoint
Range DCF Constant Growth Estimates	8.6%	9.7%	9.2%
Range of CAPM Estimates	8.6%	12.7%	10.6%
Average of DCF and CAPM midpoint estimates	8.6%	11.2%	9.9%

[1] Direct Testimony of John A. Cassidy at 34.

[2] *See* Surrebuttal Testimony of William A. Rigsby ("Rigsby Sb.") at 6.

Method	Low	High	Midpoint
Financial Risk Adjustment	-0.9%	-0.9%	-0.9%
Specific Company Risk Premium	0.8%	0.8%	0.8%
Indicated Cost of Equity	**8.5%**	**11.1%**	**9.8%**

The schedules containing my updated cost of capital analysis are attached to this rejoinder testimony.

My 9.5 percent return on equity ("ROE") recommendation is lower than the mid-point of the results of my analysis. My recommendation balances my judgment about the degree of financial and business risk associated with an investment in RRUI as well as consideration of the current economic environment.

Q. PLEASE SUMMARIZE YOUR RECOMMENDED REJOINDER RATE OF RETURN ON RATE BASE.

A. Using a 100 percent equity capital structure, the weighted average cost of capital ("WACC") is 9.5 percent. The WACC is reflected on Rejoinder Schedule D-1. The Company's recommend return on rate base is the 9.5 percent WACC.

Q. HAVE YOU UPDATED YOUR COST OF EQUITY ESTIMATE FOR RRUI USING *DUFF & PHELPS* RISK PREMIUM STUDY DATA?

A. Yes, as shown in **Exhibit TJB-COC-RJ1**. The results are as follows:[3]

Stock Symbol	Company	Cost of Equity
AWR	American States Water Co.	9.92%
WTR	Aqua America	8.21%
CWT	California Water Services Group	10.67%

[3] *See* **Exhibit TJB-COC-RJ1**, Table 6.

Stock Symbol	Company	Cost of Equity
CTWS	Connecticut Water Services	12.29%
MSEX	Middlesex Water Company	11.61%
SJW	SJW Corp.	11.73%
	Average	10.74%
	RRUI	13.89%

Q. HOW DO THE *DUFF & PHELPS* COST OF EQUITY ESTIMATES COMPARE TO YOUR UPDATED DCF AND CAPM RESULTS?

A. The results of my DCF and CAPM analyses for the publicly traded water companies compare favorably to the build-up method using the *Duff & Phelps* study data. The mid-point of my DCF and CAPM results is 10.0 percent, which is below at the midpoint of the ranges of estimates produced by the build-up method using the *Duff &Phelps* study data which range from 8.21 percent to 12.29 percent with a midpoint of 10.25 percent. Second, and more importantly, the results of my models of 9.8 is below the mid-point of the range of estimates for RRUI using both build-up methods (one using the *Morningstar* data[4] and the other using the *Duff & Phelps* study data) which range from 10.8 percent to 13.7 percent with a mid-point of 12.3 percent. Accordingly, I find my recommendation of a 9.5 percent return on equity appropriately conservative.

[4] *See* Direct Testimony of Thomas J. Bourassa – Cost of Capital at 44 – 45.

B. Summary of the Staff and RUCO recommendations

Q. PLEASE SUMMARIZE THE RESPECTIVE RECOMMENDATIONS OF STAFF AND RUCO FOR THE RATE OF RETURN ON FAIR VALUE RATE BASE AT THIS STAGE OF THE PROCEEDING.

A. As explained above, Staff continues to recommend a capital structure consisting of 0 percent debt and 100 percent equity.[5] Staff has lowered its cost of equity recommendation from 8.4 percent to 8.2 percent based on the average cost of equity produced by its updated DCF and CAPM models, a financial risk adjustment and an economic assessment adjustment.[6] Based on its capital structure recommendation, Staff determined the WACC for RRUI to be 8.2 percent.[7]

RUCO has revised its recommendation regarding RRUI's capital structure from a capital structure consisting of 20 percent debt and 80 percent equity to 0 percent debt and 100 percent equity.[8] RUCO has also lowered its recommended cost of equity from 9.0 percent to 8.25 percent based, in part, on the results of its updated DCF and CAPM methods and the change in the capital structure.[9]

Q. PLEASE COMPARE THE PARTIES' RESPECTIVE COST OF EQUITY ESTIMATES AND RECOMMENDATIONS.

A. The respective parties' cost of equity recommendations are summarized below:

Party	DCF	CAPM	Average	Recommended
RRUI	8.5%	11.1%	9.8%	9.5%
Staff	8.8%	8.2%	8.5%	8.2%
RUCO	8.36%	6.25%	7.31%	8.25%

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5 Surrebuttal Testimony of John A. Cassidy at 4.
6 *Id.* at 5.
7 *Id.*
8 Rigsby Sb. at 6.
9 *Id.*

C. Comments on the Cost of Equity Results and Recommendations of Staff and RUCO

Q. WHY HAS MR. RIGSBY CHANGED HIS RECOMMENDATION REGARDING THE CAPITAL STRUCTURE?

A. I do not know because Mr. Rigsby does not explain why he changed his recommendation only that he decided to recommend a 100 percent equity capital structure.[10]

Q. HAS MR. RIGSBY EXPLAINED WHY HIS COST OF EQUITY RECOMMENDATION CHANGED FROM 9.0 PERCENT TO 8.25 PERCENT?

A. Mr. Rigsby explains that his lower 8.25 percent takes into consideration the lower financial risk associated with a capital structure that contains no debt.[11]

Q. DID MR. RIGSBY QUANTIFY THE FINANCIAL RISK ADJUSTMENT THROUGH THE USE OF THE HAMADA METHOD OR SOME OTHER METHOD?

A. No. The 75 basis point reduction from 9.0 percent to 8.25 percent appears to be another one of Mr. Rigsby's subjective judgments that cannot be verified or replicated; like his estimates of growth for his DCF model.[12]

Q. IF MR. RIGSBY DID USE THE HAMADA METHOD TO COMPUTE A FINANCIAL RISK ADJUSTMENT, WHAT WOULD IT BE?

A. Using the Hamada method, Mr. Rigsby's financial risk adjustment would be no more than 40 basis points. His recommended cost of equity would be 8.6 percent, not 8.25 percent.

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[10] *Id.*

[11] *Id.* at 7.

[12] Rebuttal Testimony of Thomas J. Bourassa – Cost of Capital ("Bourassa COC Rb.") at 25.

Q. DOESN'T MR. RIGSBY, ON PAGES 10 AND 11 OF HIS TESTIMONY, EXPLAIN HOW HE DETERMINED THE GROWTH RATES FOR HIS DCF MODEL IN RESPONSE TO YOUR REBUTTAL COMMENT THAT HIS DCF GROWTH RATES CANNOT BE VERIFIED OR REPLICATED?

A. Despite Mr. Rigsby's additional explanation of how he estimates his growth rates, he avoids disclosing the key inputs necessary to estimate the internal or retention growth rate he employs. Consequently, his method of estimating his growth rates remains subjective and cannot be verified or replicated. The key point of my rebuttal testimony remains the same; his approach allows him to simply select a growth rate that falls somewhere within a broad range that cannot be verified.[13]

Q. HAVE YOU IGNORED THE FACT THAT RRUI IS OWNED BY A LARGE PUBLICLY TRADED COMPANY?

A. No, contrary to Mr. Rigsby's assertion.[14] I have taken into consideration RRUI's access to capital through its parent company.[15] My recommended size risk premium reflects a consideration of RRUI's access to capital.[16] That said, I also stand by my statement that it is the investment (RRUI), and not the investor (RRUI's parent), that is analyzed for purposes of establishing the cost of equity.[17]

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[13] *Id.* at 24 – 25.

[14] Rigsby Sb. at 10.

[15] Bourassa COC Rb. at 18.

[16] *Id.*

[17] *Id.*

Q. PLEASE COMMENT ON THE 2012-2017 PROJECTED RETURNS FOR BOTH THE WATER UTILITY PROXY GROUP AND THE GAS PROXY GROUP THAT MR. RIGSBY COMPLAINS YOU DID NOT CONSIDER IN YOUR REBUTTAL TESTIMONY?

A. I would agree with Mr. Rigsby that the projected book returns for 2012 to 2017 for my water proxy group average 9.69 percent.[18] Whether it is the 10.30 percent for the 2015 to 2017 I computed in my rebuttal testimony or 9.7 percent (9.69) for 2012 to 2017 as Rigsby states, they are both considerably higher than both the results of his models at 7.13 percent and his 8.25 percent recommended cost of equity.

Q. WHAT IS THE DIFFERENCE IN YOUR PROXY GROUP AND MR. RIGSBY'S PROXY GROUP?

A. Mr. Rigsby excludes Connecticut Water (CTWS), whereas I exclude American Water (AWK).

Q. WHY DO YOU EXCLUDE AMERICAN WATER FROM YOUR PROXY GROUP?

A. For two reasons. First, there is relative little market history for American Water to make reliable judgments about future financial performance. Mr. Rigsby admits there is only 4 years of data.[19] Second, and more importantly, American Water is very, very, very large. It is has nearly 4 times the revenues and 4 times the net plant as the next largest water utility (Aqua America) making it even less relevant to a cost of capital analysis concerning a small water utility like RRUI.

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[18] Rigsby Sb. at 9.

[19] *See* Direct Testimony of William A. Rigsby at 20.

Q. WHY DOES MR. RIGSBY EXCLUDE CONNECTICUT WATER?

A. Mr. Rigsby says it is because *Value Line* does not provide the same type of forward looking information that it provides on the six water utilities in his proxy group.[20]

Q. IS THIS TRUE?

A. No. Value Line currently provides the same forward looking information for Connecticut Water as the other water utilities in Mr. Rigsby's water proxy group.

Q. WHAT WOULD BE VALUE LINE'S PROJECTED RETURNS ASSUMING ALL SEVEN UTILITIES WERE CONSIDERED?

A. Mr. Rigsby points out that the 2012-2017 projected returns for his proxy group plus Connecticut Water is 9.55 percent.[21] Again, still considerably higher than either the results of his models at 7.13 percent or his 8.25 recommended cost of equity.

Q. WHAT ABOUT MR. RIGSBY'S GAS PROXY GROUP?

A. *Value Line* (December 7, 2012) projects the following returns on equity for the nine gas utilities in RUCO's proxy group:

AGL Resources, Inc. (GAS)	10.2%
Atmos Energy Corp. (ATO)	8.0%
Laclede Group (LG)	10.0%
New Jersey Resources (NJR)	14.7%
Northwest Gas Co. (NWN)	9.8%
Piedmont Natural Gas Co. (PNY)	12.0%
South Jersey Industries, Inc. (SJI)	14.3%
Southwest Gas (SWX)	9.8%
WGL Holdings, Inc. (SJW)	10.1%
Average	11.0%

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[20] *Id.* at 24.

[21] Rigsby Sb. at 9.

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I should point out while Mr. Rigsby mentions his water proxy group's 2012-2017 projected book returns are 9.55 percent, he does not mention that his gas proxy group's 2012-2017 projected book returns is 11.0 percent. The midpoint of his water proxy group and gas proxy group is 10.30 percent, which makes his 8.25 percent recommendation all the more unbelievable.

Q. WHAT IS THE SIGNFICANCE OF ALL OF THESE PROJECTED BOOK RETURNS?

A. For one, they are all much higher than either the Staff or RUCO returns produced by their respective models before any consideration of financial risk or other risks. The average of Staff's DCF and CAPM results is 8.5 percent. The average of RUCO's DCF and CAPM results is 7.13 percent.

For another, since we are applying a return to a book value rate base, book equity returns have relevance. Additionally, if we are to meet the comparable earnings standards set forth in *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944) and *Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia*, 262 U.S. 679, 692-93 (1923), then a comparison to book returns is an essential element.

Q. WHAT ABOUT DIFFERENCES IN FINANCIAL RISK BETWEEN THE PROXY GROUPS AND RRUI?

A. If the difference in financial risk is considered and assuming the appropriate financial risk adjustment is Staff's 90 basis point downward adjustment (which is based on book values), the indicated return would fall between 8.6 percent and 10.1 percent with a midpoint of 9.4 percent. Of course, the 9.4 percent does not consider other risk factors such as size. Putting that aside, the 9.4 percent is still much higher than the Staff recommended 8.2 percent ROE and RUCO's recommended 8.25 percent.

Q. PLEASE COMMENT ON MR. CASSIDY'S SUREBUTTAL TESTIMONY CONCERNING THE USE OF BOOK VALUES IN THE HAMADA METHOD.

A. Mr. Cassidy makes the very point I have been attempting to make throughout my rebuttal testimony and now here. That is, the inputs and assumptions Staff uses in their approach to the cost of capital depress the results. Assuming book values are appropriate in a market based method, like the Hamada method, is a bad assumption that ultimately results in an overstatement of the financial risk adjustment and an understatement of the cost of equity.

Q. WILL RRUI HAVE SUFFICIENT EARNINGS TO PAY DIVIDENDS AT A LEVEL COMPARABLE TO THE PUBLICLY TRADED WATER UTILITY COMPANIES IF STAFF'S RETURN ON EQUITY IS ADOPTED?

A. No. In fact, in order for the Company to pay dividends the payout ratio will exceed 100 percent of earnings; which is not sustainable. The same problem exists under RUCO's recommended equity return.

Q. HAVE YOU PREPARED AN EXHIBIT TO SHOW THE COMPUTATIONS OF THE PAYOUT RATIOS?

A. Yes. Attached hereto is **Exhibit TJB-COC-RJ2**. Table 1 of the exhibit shows the computations using the Staff recommendations. Table 2 of the exhibit shows the computations using the RUCO recommendations. Table 3 of the exhibit shows the computations using the Company's recommendations. The payout ratio for Staff is 94 percent; the payout ratio for RUCO is 93 percent; and, the payout ratio for the Company is 76 percent.

Q. WHAT IS THE PAYOUT RATIO FOR THE PUBLICLY TRADED WATER UTILITIES?

A. The 5 year average payout ratio is 71 percent.

Q. DOES A UTILITY HAVE TO SUPPORT ITS CAPITAL WITH ITS EARNINGS?

A. Yes. All invested capital must be supported as each dollar of capital has an earnings requirement. Whether each dollar is recognized in rate base, it nevertheless has capital costs and these costs must be absorbed by earnings from existing investments. As Dr. Morin states:

> The totality of a company's capital has to be serviced... Therefore, the allowed rate of return on common equity is applicable to the total common equity component of the total investments of the utility company. Anything less than that has the direct and immediate effect of reducing common equity return below the level needed to meet the capital attraction and the comparable earnings standards articulated in the Hope and Bluefield decisions. To apply an allowed rate of return to a rate base that does not maintain the integrity of that capital does not enable the company to attract capital.[22]

Q. WHAT WOULD HAPPEN TO THE VALUE OF AN INVESTMENT IN RRUI IF IT PAID DIVIDENDS IN THE SAME PROPORTION OF EARNINGS AS THE PUBLICLY TRADED UTILITIES?

A. The value of the equity investment in RRUI would necessarily decrease. Let me explain. Using the figures in Table 1, if RRUI paid out 71 percent of its net earnings, comparable to the publicly traded water utilities, it would pay dividends totaling about $668,189 (Staff's required operating income $941,124 times 71 percent). This would translate to a dividend yield of only 2.17 percent ($668,189 cash divided by $13,495,513 book equity divided by 2.28 market-book ratio). However, investors expect a dividend yield of 3.1 percent according to Staff, so the value of an investment in RRUI would need to decrease to

[22] Roger A. Morin, *The New Regulatory Finance*, chapter 4 (2006) at 497 – 498.

$21,554,483 million ($668,189 divided by 3.1 percent) from a market value of $30,765,210 ($13,493,513 book equity times 2.28 market-to-book ratio). In other words, RRUI's investors will lose approximately $9,210,726 of investment value ($21,554,483 minus $30,765,210). The market-to-book ratios would drop precipitously from the 2.28 of the publicly traded water utilities from to 1.60 ($21,554,483 divided by $13,495,513).

Q. WOULD THE REDUCTION IN THE VALUE OF EQUITY BE SIMILAR UNDER THE RUCO RECOMMENDATIONS?

A. Yes.

Q. WHAT WOULD THE RATE OF RETURN THAT IS APPLIED TO STAFF'S PROPOSED RATE BASE NEED TO BE IN ORDER FOR THE COMPANY TO BE COMPARABLE TO THE PUBLICLY TRADED WATER COMPANIES?

A. 10.8 percent. Let me explain. If RRUI has a payout ratio of 71 percent, then it must have earnings of about $1,343,849 ($13,495,513 book equity times 7.07 percent Staff book dividend yield divided by 71 percent payout ratio). Staff's proposed rate base (water and wastewater combined) is $12,395,518, so the return required is 10.8 percent ($1,343,849 divided by $12,395,518). RUCO's recommended rate base is somewhat lower at $12,270,684 which would mean a higher required return than 10.8 percent.

Q. BUT MR. BOURASSA, ISN'T IT THE RATE BASE WE RECOGNIZE AS THE COMPANY'S INVESTMENT IN RATE MAKING?

A. Yes. Putting aside Dr. Morin's comments above, and determining the required earnings on rate base, then RRUI must have earnings of $1,234,314 in order to be comparable to the publicly traded companies ($12,395,518 Staff combined rate base for water and wastewater times 7.07 percent Staff book dividend yield divided by 71 percent payout ratio). The return required is 9.96 percent ($1,234,314 divided by $12,395,518).

Similarly, under the RUCO recommendations, RRUI must have earnings of $1,209,785 ($12,270,684 RUCO combined rate base for water and wastewater times 7.00% RUCO book dividend yield divided by 71 percent payout ratio). The return required is 9.86 percent ($1,209,785 divided by $12,270,684).

Q. ANY FINAL THOUGHTS?

A. Yes. Either way you look at it, the Staff recommended return on equity of 8.2 percent and the RUCO recommended return on equity of 8.25 percent fail the comparable earnings test and the capital attraction standards set forth in *Hope* and *Bluefield.*

Q. DOES THAT CONCLUDE YOUR REJOINDER TESTIMONY ON COST OF CAPITAL?

A. Yes, although my silence on any of the issues, matters or findings addressed in the testimony of Staff and/or RUCO does not constitute my acceptance of their positions on such issues, matters or findings.

RIO RICO UTILITIES, INC. DBA LIBERTY UTILITIES

REJOINDER TESTIMONY OF THOMAS J. BOURASSA

COST OF CAPITAL

MARCH 8, 2013

EXHIBIT TJB-COC-RJ1

Rio Rico Utilities, Inc. dba Liberty Utilities
COST OF EQUITY (COE) USING RISK PREMIUM BUILD-UP METHOD
Based on *Duff and Phelps* Risk Premium Study Data

TABLE 1

	Company	Symbol	MV Equity[1]	Book Equity[1]	MVIC[1]	5 Yr Avg. Net Income	Total Assets[2]	5 Yr Avg. EBITDA[3]
			Measures of size (Millions)					
1.	American States	AWR	$ 1,039	$ 408	$ 1,380	$ 32	$ 1,192	$ 120
2.	Aqua America	WTR	$ 4,129	$ 1,251	$ 5,525	$ 113	$ 4,072	$ 407
3.	California Water	CWT	$ 862	$ 450	$ 1,344	$ 37	$ 1,692	$ 128
4.	Connecticut Water	CTWS	$ 260	$ 119	$ 395	$ 10	$ 425	$ 23
5.	Middlesex	MSEX	$ 310	$ 177	$ 442	$ 12	$ 489	$ 38
6.	SJW Corp.	SJW	$ 517	$ 264	$ 861	$ 20	$ 935	$ 87
	Rio Rico Utilities, Inc. dba Liberty Utilities		NA	$ 11.0	NA	$ 0.1	$ 29.7	$ 1.9

[1] From Zacks Investment Research data
[2] From Zacks Investment Research. From E-1 for subject utility.
[3] Net Income. From Zacks Investment Research and Company ACC reports

Net Income Data

Company	Symbol	2011	2010	2009	2008	2007	Average
American States	AWR	$ 45.9	$ 33.2	$ 29.5	$ 22.0	$ 28.0	$ 31.7
Aqua America	WTR	$ 143.1	$ 124.0	$ 104.4	$ 97.9	$ 95.0	$ 112.9
California Water	CWT	$ 37.7	$ 37.7	$ 40.6	$ 39.8	$ 31.2	$ 37.4
Connecticut Water	CTWS	$ 11.3	$ 9.8	$ 10.2	$ 9.4	$ 8.8	$ 9.9
Middlesex	MSEX	$ 13.4	$ 14.3	$ 10.0	$ 12.2	$ 11.8	$ 12.4
SJW Corp.	SJW	$ 20.9	$ 24.4	$ 15.2	$ 21.5	$ 19.3	$ 20.2
Rio Rico Utilities, Inc. dba Liberty Utilities		$ (2.8)	$ 0.8	$ 0.8	$ 0.6	$ 1.0	$ 0.1

Net Income data for publicly traded water utilities from Zacks Investment Research and/or Yahoo Finance

[4] Earnings before Interest, Taxes, Depreciation and Amortization (EBITDA). From Zacks Investment Research and Company ACC reports.

EBITDA Data

Company	Symbol	2011	2010	2009	2008	2007	Average
American States	AWR	$ 133.3	$ 134.4	$ 122.6	$ 105.9	$ 102.8	$ 119.8
Aqua America	WTR	$ 397.8	$ 473.2	$ 415.2	$ 384.7	$ 364.5	$ 407.1
California Water	CWT	$ 143.3	$ 155.7	$ 125.5	$ 122.1	$ 95.6	$ 128.4
Connecticut Water	CTWS	$ 24.2	$ 22.5	$ 20.3	$ 21.1	$ 27.9	$ 23.2
Middlesex	MSEX	$ 34.6	$ 43.3	$ 34.6	$ 38.6	$ 36.6	$ 37.6
SJW Corp.	SJW	$ 87.1	$ 75.4	$ 93.5	$ 99.7	$ 77.7	$ 86.7
Rio Rico Utilities, Inc. dba Liberty Utilities		$ 1.4	$ 4.0	$ 1.9	$ 0.8	$ 1.2	$ 1.9

EBITDA data for publicly traded water utilities from Zacks Investment Research and/or Yahoo Finance
EBITDA data for subject utility from E-1 and/or ACC reports

Rio Rico Utilities, Inc. dba Liberty Utilities
COST OF EQUITY (COE) USING RISK PREMIUM BUILD-UP METHOD
Based on *Duff and Phelps* **Risk Premium Study Data**

TABLE 2

MRP_{m+s} Estimates Using Duff & Phelps Study (Unlevered)
Assumes 100% Equity and 0% debt
Data Smoothing with Regression Analysis
Smoothed Premium (RP_{m+s}) = Constant + X Coefficients * Log(Relevent Metric)

$RPun_{relevered} = RP_{levered} - W_d/W_e*(\beta_u-\beta_d)*RP_{market}$
Where β_u = unlevered portfolio beta
β_d = debt beta, assumed to be 0.1
W_d = percentage of debt in capital structure
W_e = percentage of equity in capital structure
$RP_{levered}$ = levered realized risk premium

	MV Equity (Table C-1)	Book Equity (Table C-2)	MVIC (Table C-4)	5 Yr Avg. Net Income (Table C-3)	Total Assets (Table C-5)	5 Yr Avg. EBITDA (Table C-6)
Constant	18.475%	15.380%	18.661%	13.224%	17.273%	14.736%
X Coefficient(s)	-3.239%	-2.561%	-3.201%	-2.616%	-2.812%	-2.723%

MRP_{m+s} (unlevered)

	Company	Symbol	MV Equity	Book Equity	MVIC	5 Yr Avg. Net Income	Total Assets	5 Yr Avg. EBITDA	Average
1.	American States	AWR	8.70%	8.70%	8.61%	9.30%	8.62%	9.08%	8.83%
2.	Aqua America	WTR	6.76%	7.45%	6.68%	7.85%	7.12%	7.63%	7.25%
3.	California Water	CWT	8.97%	8.59%	8.65%	9.11%	8.19%	8.99%	8.75%
4.	Connecticut Water	CTWS	10.65%	10.07%	10.35%	10.62%	9.88%	11.02%	10.43%
5.	Middlesex	MSEX	10.41%	9.62%	10.19%	10.37%	9.71%	10.45%	10.12%
6.	SJW Corp.	SJW	9.69%	9.18%	9.27%	9.81%	8.92%	9.46%	9.39%
	Average (unlevered)		9.20%	8.93%	8.96%	9.51%	8.74%	9.44%	9.13%
	Rio Rico Utilities, Inc. dba Liberty Utilities		NA	12.71%	NA	16.23%	13.13%	14.01%	14.02%

Indicated size premium 4.89%

Rio Rico Utilities, Inc. dba Liberty Utilities
COST OF EQUITY (COE) USING RISK PREMIUM BUILD-UP METHOD
Based on *Duff and Phelps* Risk Premium Study Data

TABLE 3

Unlevered Portfilio Beta
(from 2012 Duff & Phelps RP Study - Table C)

			Unlevered Portfolio Beta (β_u)						
	Company	Symbol	(Table C-1)	(Table C-2)	(Table C-4)	(Table C-3)	(Table C-5)	(Table C-6)	Average
1.	American States	AWR	0.95	0.96	0.98	0.94	0.94	0.97	0.96
2.	Aqua America	WTR	0.87	0.86	0.81	0.88	0.83	0.84	0.85
3.	California Water	CWT	0.98	0.95	0.95	0.94	0.92	0.97	0.95
4.	Connecticut Water	CTWS	0.96	1.00	0.97	0.97	0.99	1.03	0.99
5.	Middlesex	MSEX	0.96	0.98	0.97	0.97	0.99	0.99	0.98
6.	SJW Corp.	SJW	0.95	0.97	0.97	0.96	0.97	0.95	0.96
	Average		0.95	0.95	0.94	0.94	0.94	0.96	0.95
	Rio Rico Utilities, Inc. dba Liberty Utilities		0.95	0.98	1.00	1.01	1.05	1.03	1.00

Rio Rico Utilities, Inc. dba Liberty Utilities
COST OF EQUITY (COE) USING RISK PREMIUM BUILD-UP METHOD
Based on *Duff and Phelps* Risk Premium Study Data

TABLE 4

MRP Estimates Using Duff & Phelps Study (Relevered)
Relevered Realized Risk Premium
$RP_{relevered} = RP_{unlevered} + W_d/W_e*(\beta_u-\beta_d)*RP_{market}$
Where β_u = unlevered portfolio beta
β_d = debt beta, assumed to be 0.1
W_d = percentage of debt in capital structure
W_e = percentage of equity in capital structure
$RP_{unlevered}$ = unlevered realized risk premium from Table 2
RP_{market} = general equity risk premium for the market since 1963 (4.4%)

			MRP$_{m+s}$ (Relevered)							
	Company	Symbol	W_d/W_e	MV Equity	Book Equity	MVIC	5 Yr Avg. Net Income	Total Assets	5 Yr Avg. EBITDA	Average
1.	American States	AWR	32.7%	9.90%	9.91%	9.85%	10.48%	9.81%	10.30%	10.04%
2.	Aqua America	WTR	33.8%	7.88%	8.55%	7.71%	8.99%	8.18%	8.71%	8.34%
3.	California Water	CWT	55.8%	11.08%	10.63%	10.69%	11.13%	10.16%	11.08%	10.79%
4.	Connecticut Water	CTWS	52.0%	12.58%	12.08%	12.30%	12.57%	11.87%	13.10%	12.42%
5.	Middlesex	MSEX	42.6%	11.98%	11.24%	11.79%	11.96%	11.34%	12.08%	11.73%
6.	SJW Corp.	SJW	66.5%	12.12%	11.67%	11.75%	12.27%	11.41%	11.89%	11.85%
	Average MRP (Relevered)		47.26%	10.92%	10.68%	10.68%	11.23%	10.46%	11.19%	10.86%
	Rio Rico Utilities, Inc. dba Liberty Utilities		0.00%	NA	12.71%	NA	16.23%	13.13%	14.01%	14.02%

Rio Rico Utilities, Inc. dba Liberty Utilities
COST OF EQUITY (COE) USING RISK PREMIUM BUILD-UP METHOD
Based on *Duff and Phelps* **Risk Premium Study Data**

TABLE 5

Equity Risk Premium Adjustment and Other meterics used in Build-up Method

[1] Estimate of Current Market Risk Premium ($\mathbf{RP_{market}}$)	**5.50%**	<<<< Current Duff and Phelps recommendation
[2] Risk Premium Assumed in Duff & Phelps Study (1963-2011) [1]	4.30%	
[3] Equity Risk Premium Adjustment ([1] - [2])	1.20%	
[4] Average MRP (relevered) for publicly traded water companies (from Table 4)	10.86%	
[5] MRP (relevered) for publicly traded water companies $\mathbf{(RP_{m+s})}$ ([3] + [4])	12.06%	
[6] Equity Risk Premium Adjustment ([3])	1.20%	
[7] Average MRP (relevered) for subject utility company (from Table 4)	14.02%	
[8] MRP (relevered) for subject utility company $\mathbf{(RP_{m+s})}$ ([6] + [7])	15.22%	
[9] Industry Risk Premium (From *Ibbotson* for SIC 494 Water Supply Industry Table 3-5)	-4.83%	
[10] Adjustment Factor to Industry Risk Premium ([2] / 6.6% [1])	0.8333	
[11] Adjusted Industry Risk Premium $\mathbf{(R_i)}$ ([9] x [10])	-4.03%	
[12] Risk Free Rate $\mathbf{(R_f)}$[2]	2.65%	

[1] From Duff and Phelps Risk Premium Report 2012.
[2] Yield on 20 Yr U.S. Treasury January 11, 2013 (Federal Reserve)

Rio Rico Utilities, Inc. dba Liberty Utilities
COST OF EQUITY (COE) USING RISK PREMIUM BUILD-UP METHOD
Based on *Duff and Phelps* Risk Premium Study Data

TABLE 6

Cost of Equity (COE) Estimate using Build-up Method

$E(R_i) = R_f + RP_{m+s} + RP_i + RP_u$
Where:
- **$E(R_i)$ = Expected (indicated) rate of return**
- **R_f = Risk-free rate of return. See Table 5.**
- **RP_{m+s} = Market risk premium including size premium. See Table 4.**
- **RP_i = Industry risk premium (adjusted) See Table 5.**
- **RP_u = Company-specific risk premium**

	Sample Publicly Traded Water Utilities	Rio Rico Utilities, Inc. dba Liberty Utilities
R_f =	2.65%	2.65%
RP_{m+s} =	See Table 4	See Table 4
RP_i =	-4.03%	-4.03%
RP_u =	0.00%	0.00%

	Company	Symbol	Indicated COE $E(R_i)$ MV Equity	Book Equity	MVIC	5 Yr Avg. Net Income	Total Assets	5 Yr Avg. EBITDA	Average
1.	American States	AWR	9.73%	9.73%	9.67%	10.30%	9.63%	10.13%	9.87%
2.	Aqua America	WTR	7.71%	8.38%	7.54%	8.81%	8.01%	8.53%	8.16%
3.	California Water	CWT	10.90%	10.45%	10.51%	10.95%	9.99%	10.91%	10.62%
4.	Connecticut Water	CTWS	12.40%	11.91%	12.12%	12.39%	11.70%	12.93%	12.24%
5.	Middlesex	MSEX	11.81%	11.06%	11.61%	11.79%	11.17%	11.90%	11.56%
6.	SJW Corp.	SJW	11.94%	11.49%	11.58%	12.09%	11.23%	11.72%	11.68%
	Average COE estimate		10.75%	10.50%	10.51%	11.06%	10.29%	11.02%	10.69%
	Rio Rico Utilities, Inc. dba Liberty Utilities		NA	12.54%	NA	16.05%	12.96%	13.83%	13.84%

RIO RICO UTILITIES, INC. DBA LIBERTY UTILITIES

REJOINDER TESTIMONY OF THOMAS J. BOURASSA

COST OF CAPITAL

MARCH 8, 2013

EXHIBIT TJB-COC-RJ2

Table 1 – Staff Recommendations and Actual Equity in Capital Structure

[1]	Total Equity per Direct Schedule D-1	$13,493,513
[2]	% Equity per Rejoinder D-1	100%
[3]	Book Value of Equity [1] x[2]	$13,493,513
[4]	Expected Dividend Yield per Staff	3.10%
[5]	Current market-to-book ratio publicly traded water utilities	2.28
[6]	Book Value Dividend Yield [4] x [5]	7.07%
[7]	Cash Dividend [3] x[6]	$953,721
[8]	Staff Recommended Operating Income (W and WW)	$1,013,480
[9]	Less: Annual Interest Expense	$0
[10]	Earnings Available for Dividends [8] - [9]	$1,013,480
[11]	Less: Dividends [7]	$953,721
[12]	Retained Earnings [10] - [11]	$59,759
[13]	Pay-out ratio [11]/[10]	94%

Table 2 – RUCO Recommendations and Actual Equity in Capital Structure

[1]	Total Equity per Direct Schedule D-1	$13,493,513
[2]	% Equity per Rejoinder D-1	100%
[3]	Book Value of Equity [1] x[2]	$13,493,513
[4]	Expected Dividend Yield per RUCO	3.07%
[5]	Current market-to-book ratio publicly traded water utilities	2.28
[6]	Book Value Dividend Yield [4] x [5]	7.00%
[7]	Cash Dividend [3] x[6]	$944,492
[8]	RUCO Recommended Operating Income (W and WW)	$1,010,331
[9]	Less: Annual Interest Expense	$0
[10]	Earnings Available for Dividends [8] - [9]	$1,010,331
[11]	Less: Dividends [7]	$944,492
[12]	Retained Earnings [10] - [11]	$65,839
[13]	Pay-out ratio [11]/[10]	93%

Table 3 – RRUI Recommendations and Actual Equity in Capital Structure

[1]	Total Equity per Direct Schedule D-1	$13,493,513
[2]	% Equity per Rejoinder D-1	100%
[3]	Book Value of Equity [1] x[2]	$13,493,513
[4]	Expected Dividend Yield per D-4.7	2.92%
[5]	Current market-to-book ratio publicly traded water utilities	2.28
[6]	Book Value Dividend Yield [4] x [5]	6.66%
[7]	Cash Dividend [3] x[6]	$898,344
[8]	RRUI Recommended Operating Income (W and WW)	$1,184,203
[9]	Less: Annual Interest Expense	$0
[10]	Earnings Available for Dividends [8] - [9]	$1,184,203
[11]	Less: Dividends [7]	$898,344
[12]	Retained Earnings [10] - [11]	$285,859
[13]	Pay-out ratio [11]/[10]	76%

RIO RICO UTILITIES, INC. DBA LIBERTY UTILITIES

REJOINDER TESTIMONY OF THOMAS J. BOURASSA

COST OF CAPITAL

MARCH 8, 2013

D SCHEDULES

Exhibit
Rejoinder Schedule D-1
Page 1
Witness: Bourassa

Rio Rico Utilities, Inc. dba Liberty Utilities
Test Year Ended February 29, 2012
Summary of Cost of Capital

Consolidated Capital Structure of Water and Wastewater Division

Porforma Capital Structure

Line No.	Item of Capital	Percent of Total	Cost Rate	Weighted Cost
1	Long-Term Debt	0.00%	0.00%	0.00%
2				
3	Stockholder's Equity	100.00%	9.50%	9.50%
4				
5	Totals	100.00%		9.50%
6				
7				
8				
9				
10				
11				
12				
13				
14				
15				
16				
17				
18				
19				
20				
21				
22	SUPPORTING SCHEDULES:			RECAP SCHEDULES:
23	D-1			A-1
24	D-3			
25	D-4			
26	Testimony			
27				
28				
29				
30				

Rio Rico Utilities, Inc. dba Liberty Utilities
Test Year Ended February 29, 2012
Cost of Long Term Debt

Exhibit
Schedule D-2
Page 1
Witness: Bourassa

		End of Test Year				End of Projected Year			
Line No.	Description of Debt	Amount Outstanding	Annual Interest	Interest Rate	Weighted Cost	Amount Outstanding	Annual Interest	Interest Rate	Weighted Cost
1									
2			-	0.000%	0.000%		-	0.000%	0.000%
3			-	0.000%	0.000%		-	0.000%	0.000%
4			-	0.000%	0.000%		-	0.000%	0.000%
5			-	0.000%	0.000%		-	0.000%	0.000%
6			-	0.000%	0.000%		-	0.000%	0.000%
7			-	0.000%	0.000%		-	0.000%	0.000%
8			-	0.000%	0.000%		-	0.000%	0.000%
9			-	0.000%	0.000%		-	0.000%	0.000%
10			-	0.000%	0.000%		-	0.000%	0.000%
11									
12									
13	Totals	$ -	-		0.000%	$ -	-		0.000%
14									
15									
16	Supporting Schdules:								
17									
18									
19									
20									
21									
22									
23									
24									
25									
26									
27									
28									
29									
30									

Rio Rico Utilities, Inc. dba Liberty Utilities
Test Year Ended February 29, 2012
Cost of Preferred Stock

Exhibit
Schedule D-3
Page 1
Witness: Bourassa

	End of Test Year			End of Projected Year		
Description of Issue	Shares Outstanding	Amount	Dividend Requirement	Shares Outstanding	Amount	Dividend Requirement

NOT APPLICABLE, NO PREFERRED STOCK ISSUED OR OUTSTANDING

SUPPORTING SCHEDULES:

RECAP SCHEDULES:
D-1

Rio Rico Utilities, Inc. dba Liberty Utilities
Test Year Ended February 29, 2012
Cost of Common Equity

Exhibit
Schedule D-4
Page 1
Witness: Bourassa

The Company is proposing a cost of common equity of 10.30% .

SUPPORTING SCHEDULES:	RECAP SCHEDULES:
D-4.1 to D-4.16	D-1

Rio Rico Utilities, Inc. dba Liberty Utilities
Summary of Results

Exhibit
Rejoinder Schedule D-4.1

Line No.	Method	Low	High	Midpoint
6	Range DCF Constant Growth Estimates[1]	8.6%	9.7%	9.2%
8	Range of CAPM Estimates[2]	8.6%	12.7%	10.6%
12	Average of midpoint estimates	8.6%	11.2%	9.9%
15	Financial Risk Adjustment[3]	-0.9%	-0.9%	-0.9%
17	Small Company Risk Premium[4]	0.8%	0.8%	0.8%
19	Indicated Cost of Equity	8.5%	11.1%	9.8%
23	Recommended Cost of Equity			9.5%

27 [1] See Schedule D-4-8
28 [2] See Schedule D-4.12
29 [3] See Schedule D-4.13, Testimony
30 [4] See Schedule D-4.16, Testimony

Rio Rico Utilities, Inc. dba Liberty Utilities
Selected Characteristics of Sample Group of Water Utilities

Exhibit
Rejoinder Schedule D-4.2

Company[1]	% Water Revenues	Operating Revenues (millions)	Net Plant (millions)	S&P Bond Rating	Moody's Bond Rating	Allowed ROE
1. American States	68%	$ 449.7	$ 912.0	A+	A2	9.99
2. Aqua America	96%	$ 755.7	$ 3,863.4	AA-	NR	10.33
3. California Water	100%	$ 541.5	$ 1,443.1	AA-	NR	9.99
4. Connecticut Water	100%	$ 79.8	$ 422.6	A	NR	9.75
5. Middlesex	89%	$ 106.6	$ 433.3	A	NR	10.15
6. SJW Corp.	96%	$ 261.4	$ 870.5	A	NR	9.99
Average	92%	$ 365.8	$ 1,324.2			10.03
Rio Rico Utilities, Inc. dba Liberty Utilities (Adjusted as of February 29, 2012)	68%	$ 4.2	$ 28.2	NR	NR	

[1] AUS Utility Reports (March 2013).

Rio Rico Utilities, Inc. dba Liberty Utilities
Capital Structures

Exhibit
Rejoinder Schedule D-4.3

	Book Value[1]		Market Value[1]	
Company	Long-Term Debt	Common Equity	Long-Term Debt	Common Equity
1. American States	45.5%	54.5%	24.7%	75.3%
2. Aqua America	52.7%	47.3%	25.3%	74.7%
3. California Water	51.7%	48.3%	35.8%	64.2%
4. Connecticut Water	53.2%	46.8%	34.2%	65.8%
5. Middlesex	42.8%	57.2%	29.9%	70.1%
6. SJW Corp.	56.6%	43.4%	39.9%	60.1%
Average	50.4%	49.6%	31.6%	68.4%
Rio Rico Utilities, Inc. dba Liberty Utilities (Proforma)	0.0%	100.0%	N/A	N/A

[1] Value Line Analyzer Data (March 6, 2013)
[2] Adjusted Per Schedule D-1

Exhibit
Rejoinder Schedule D-4.4

Rio Rico Utilities, Inc. dba Liberty Utilities
Comparisons of Past and Future Estimates of Growth

	[1]	[2]	[3]	[4]	[5]	[6]	[7]
							Average of Future and Historical Growth
	Five-year historical average annual changes				Average	Average Future	
Company	Price[1]	Book Value[2]	EPS[2]	DPS[2]	Col 1-4	Growth[3]	Col 5-6
1. American States	7.59%	5.50%	10.50%	3.00%	6.65%	5.83%	6.24%
2. Aqua America	3.63%	6.00%	6.00%	8.00%	5.91%	6.06%	5.98%
3. California Water	NMF	5.00%	5.00%	1.00%	3.67%	6.00%	4.83%
4. Connecticut Water	7.74%	3.00%	4.00%	1.50%	4.06%	6.80%	5.43%
5. Middlesex	4.44%	5.00%	2.00%	1.50%	3.24%	4.85%	4.04%
6. SJW Corp.	NMF	4.50%	NMF	5.00%	4.75%	11.00%	7.88%
GROUP AVERAGE	5.85%	4.83%	5.50%	3.33%	4.71%	6.76%	5.73%
GROUP MEDIAN	6.02%	5.00%	5.00%	2.25%	4.40%	6.03%	5.71%

[1] Average of changes in annual stock prices ending on December 31 through 2012. Data from Yahoo Finance website.
[2] Value Line Analyzer Data, March 6, 2013
[3] See Schedule D-4.6.

Exhibit
Rejoinder Schedule D-4.5

Rio Rico Utilities, Inc. dba Liberty Utilities
Comparisons of Past and Future Estimates of Growth

	[1]	[2]	[3]	[4]	[5]	[6]	[7]
	Ten-year historical average annual changes						Average of Future and Historical
		Book			Average	Average Future	Growth
Company	Price[1]	Value[2]	EPS[2]	DPS[2]	Col 1-4	Growth[3]	Col 5-6
1. American States	9.71%	5.00%	5.00%	2.00%	5.43%	5.83%	5.63%
2. Aqua America	6.42%	8.50%	7.00%	7.50%	7.36%	6.06%	6.71%
3. California Water	5.72%	5.00%	4.00%	1.00%	3.93%	6.00%	4.96%
4. Connecticut Water	3.13%	4.00%	0.50%	1.50%	2.28%	6.80%	4.54%
5. Middlesex	4.42%	4.50%	2.50%	1.50%	3.23%	4.85%	4.04%
6. SJW Corp.	5.50%	5.50%	2.00%	5.00%	4.50%	11.00%	7.75%
GROUP AVERAGE	5.82%	5.42%	3.50%	3.08%	4.45%	6.76%	5.61%
GROUP MEDIAN	5.61%	5.00%	3.25%	1.75%	4.21%	6.03%	5.30%

[1] Average of changes in annual stock prices ending December 31, 2011. Data from Yahoo Finance website.
[2] Value Line Analyzer Data, March 6, 2013.
[3] See Schedule D-4.6.

Rio Rico Utilities, Inc. dba Liberty Utilities
Analysts Forecasts of Earnings Per Share Growth

Exhibit
Rejoinder Schedule D-4.6

	[1]	[2]	[3]	[4]
	ESTIMATES OF EARNINGS GROWTH			Average
			Value	Growth (G)
Company	Reuters[1]	Yahoo[1]	Line[1]	(Cols 1-3)[2]
1. American States	6.00%	6.00%	5.50%	5.83%
2. Aqua America	6.27%	4.90%	7.00%	6.06%
3. California Water	6.00%	6.00%	6.00%	6.00%
4. Connecticut Water		6.10%	7.50%	6.80%
5. Middlesex	neg	2.70%	7.00%	4.85%
6. SJW Corp.		14.00%	8.00%	11.00%
GROUP AVERAGE	6.09%	6.62%	6.83%	6.76%
GROUP MEDIAN				6.03%

[1] Data as of March 6, 2013

[2] Where no data available or single estimate, average of other utilities assumed to estimate for utility.

Rio Rico Utilities, Inc. dba Liberty Utilities
Current Dividend Yields for Water Utility Sample Group

Exhibit
Rejoinder Schedule D-4.7

Company	Curent Stock Price (P_0)[1]	Current Dividend (D_0)[1]	Current Dividend Yield (D_0/P_0)[1]	Average Annual Dividend Yield (D_0/P_0)[1,2]
1. American States	$ 55.29	$ 1.10	1.99%	3.20%
2. Aqua America	$ 29.73	$ 0.63	2.12%	2.85%
3. California Water	$ 20.63	$ 0.62	3.01%	3.36%
4. Connecticut Water	$ 29.54	$ 0.94	3.18%	3.62%
5. Middlesex	$ 19.75	$ 0.73	3.70%	4.02%
6. SJW Corp.	$ 27.79	$ 0.69	2.48%	2.94%
Average			2.75%	3.33%
Median			2.74%	3.28%

[1] Value Line Analyzer Data. Stock prices as of March 6, 2013.
[2] Average Annual Dividend is dividends declared per share for a year divided by the average annual price of the stock in the same year, expressed as a percentage. For comparison purposes only.

Rio Rico Utilities, Inc. dba Liberty Utilities
Discounted Cash Flow Analysis
DCF Constant Growth

Exhibit
Rejoinder Schedule D-4.8

	[1] Average Spot Dividend Yield (D_0/P_0)[1]	[2] Expected Dividend Yield (D_1/P_0)[2]	[3] Growth (g)	[4] Indicated Cost of Equity k=Div Yld + g (Cols 2+3)
DCF - Past and Future Growth	2.75%	2.90%	5.73% [3]	8.6%
DCF - Future Growth	2.75%	2.93%	6.76% [4]	9.7%
Average	2.75%	2.92%	6.25%	9.2%

[1] Spot Dividend Yield = D_0/P_0. See Schedule D-4.7.
[2] Expected Dividend Yield = $D_1/P_0 = D_0/P_0 * (1+g)$.
[3] Growth rate (g). Average of Past and Future Growth. See Schedule D-4.4, column 7
[4] Growth rate (g). Average of Analyst Estimates Future Growth. See Schedule D-4.6.

Rio Rico Utilities, Inc. dba Liberty Utilities
Market Betas

Exhibit
Rejoinder Schedule D-4.9

	Company	Beta (β)[1]
1.	American States	0.70
2.	Aqua America	0.60
3.	California Water	0.65
4.	Connecticut Water	0.75
5.	Middlesex	0.70
6.	SJW Corp.	0.85
	Average	**0.71**

[1] Value Line Investment Analyzer data (March 6, 2013)

Note: Beta is a relative measure of the historical sensitivity of a stock's price to overall fluctuations in the New York Stock Exchange Composite Index. A Beta of 1.50 indicates a stock tends to rise (or fall) 50% more than the New York Stock Exchange Composite Index. The "Beta coefficient" is derived from a regression analysis of the relationship between weekly percent-age changes in the price of a stock and weekly percentage changes in the NYSE Index over a period of five years. In the case of shorter price histories, a smaller time period is used, but two years is the minimum. The Betas are adjusted for their long-term tendency to converge toward 1.00.

Rio Rico Utilities, Inc. dba Liberty Utilities
Forecasts of Long-Term Interest Rates
2012-14

Exhibit
Rejoinder Schedule D-4.10

Description	Spot Feb. 2013	2014	2015	Average
Blue Chip Consensus Forecasts[1]	3.2%	3.6%	4.3%	3.7%
Value Line[2]	3.2%	4.6%	4.5%	4.1%
Average				3.9%

[1] December 2012 Blue Chip Financial Forecasts consensus forecast of 30 Year U.S.Treasury

[2] Value Line Quarterly forecast, dated February 22, 2013, Long-term Treasury

Rio Rico Utilities, Inc. dba Liberty Utilities
Computation of Current Market Risk Premium

Exhibit
Rejoinder Schedule D-4.11

Line No.	Month	Dividend Yield (D_0/P_0)[1]	Expected Dividend Yield (D_1/P_0)[2]	+	Growth (g)[3]	=	Expected Market Return (k)	-	Monthly Average 30 Year Treasury Rate[4]	=	Market Risk Premium (MRP)
1											
2											
3											
4	Jan 2011	2.34%	2.60%	+	11.10%	=	13.70%	-	4.52%	=	9.18%
5	Feb	2.41%	2.73%	+	13.16%	=	15.89%	-	4.65%	=	11.24%
6	Mar	2.35%	2.64%	+	12.33%	=	14.97%	-	4.51%	=	10.46%
7	April	1.83%	2.02%	+	10.30%	=	12.32%	-	4.50%	=	7.82%
8	May	1.95%	2.18%	+	11.76%	=	13.94%	-	4.29%	=	9.65%
9	June	1.97%	2.21%	+	12.11%	=	14.32%	-	4.23%	=	10.09%
10	July	2.23%	2.58%	+	15.51%	=	18.09%	-	4.27%	=	13.82%
11	Aug	2.73%	3.24%	+	18.51%	=	21.75%	-	3.65%	=	18.10%
12	Sept	2.88%	3.47%	+	20.40%	=	23.87%	-	3.18%	=	20.69%
13	Oct	2.60%	3.03%	+	16.35%	=	19.38%	-	3.13%	=	16.25%
14	Nov	2.75%	3.24%	+	17.89%	=	21.13%	-	3.02%	=	18.11%
15	Dec 2011	2.70%	3.17%	+	17.41%	=	20.58%	-	2.98%	=	17.60%
16	Jan 2012	2.61%	2.98%	+	14.18%	=	17.16%	-	3.03%	=	14.13%
17	Feb	2.60%	2.99%	+	15.01%	=	18.00%	-	3.11%	=	14.89%
18	Mar	2.36%	2.65%	+	12.33%	=	14.98%	-	3.28%	=	11.70%
19	April	2.62%	3.02%	+	15.22%	=	18.24%	-	3.18%	=	15.06%
20	May	2.86%	3.38%	+	18.12%	=	21.50%	-	2.93%	=	18.57%
21	June	2.73%	3.18%	+	16.59%	=	19.77%		2.70%	=	17.07%
22	July	2.79%	3.29%	+	18.10%	=	21.39%		2.59%	=	18.80%
23	Aug	2.73%	3.17%	+	16.23%	=	19.40%		2.77%	=	16.63%
24	Sept	2.67%	3.07%	+	14.95%	=	18.02%		2.88%	=	15.14%
25	Oct	2.71%	3.14%	+	15.81%	=	18.95%		2.90%	=	16.05%
26	Nov	2.74%	3.15%	+	14.88%	=	18.03%		2.80%	=	15.23%
27	Dec 2012	2.62%	2.95%	+	12.63%	=	15.58%		2.88%	=	12.70%
28	Jan 2013	2.56%	2.86%	+	11.74%	=	14.60%		3.08%	=	11.52%
29	Feb	2.60%	2.94%	+	13.13%	=	16.07%		3.17%	=	12.90%
30											
31	Recommended	2.59%	2.92%	+	12.50%	=	15.42%	-	3.04%	=	12.37%
32											
33	Short-term Trends										
34	Recent Twelve Months Avg	2.67%	3.07%	+	14.98%	=	18.04%	-	2.93%	=	15.11%
35	Recent Nine Months Avg	2.68%	3.08%	+	14.90%	=	17.98%	-	2.86%	=	15.12%
36	Recent Six Months Avg	2.65%	3.02%	+	13.86%	=	16.87%	-	2.95%	=	13.92%
37	Recent Three Months Avg	2.59%	2.92%	+	12.50%	=	15.42%	-	3.04%	=	12.37%
38											
39											

40 [1] Average Current Dividend Yield (D_0/P_0) of dividend paying stocks. Data from Value Line Investment Analyzer Software Data - Value Line 1700 Stocks

41 [2] Expected Dividend Yield (D_1/P_0) equals average current dividend yield (D0/P0) times one plus growth rate(g).

42 [3] Average 3-5 year price appreciation (annualized). Data from Value Line Investment Analyzer Software Data - Value Line 1700 Stocks

43 [4] Monthly average 30 year U.S. Treasury. Federal Reserve.

44

Rio Rico Utilities, Inc. dba Liberty Utilities
Capital Asset Pricing Model (CAPM)

Exhibit
Rejoinder Schedule D-4.12

	Rf[1]	+	beta[3]	x	Rp		=	k
Historical Market Risk Premium CAPM	3.9%	+	0.71	x	6.6%	4	=	8.6%
Current Market Risk Premium CAPM	3.9%	+	0.71	x	12.4%	5	=	12.7%
Average								10.6%

[1] Forecasts of long-term treasury yields. See Schedule D-4.10.
[2] Value Line Investment Analyzer data. See Schedule D-4.9.
[3] Historical Market Risk Premium from (Rp) MorningStar SBBI 2012 Valuation Yearbook Table A-1 Long-Horizon ERP 1926-2011.
[4] Computed using DCF constant growth method to determine current market return onValue Line 1700 stocks
and CAPM with beta of 1.0 to compute Current Market Risk Premium (Rp). See Schedule D-4.11.

Rio Rico Utilities, Inc. dba Liberty Utilities
Financial Risk Computation

Exhibit
Rejoinder Schedule D-4.13

	Rf		+	β		x	(Rp)		=	k
CAPM										
Historical Market Risk Premium	3.9%	1	+	0.71	2	x	6.6%	3	=	8.6%
Current Market Risk Premium	3.9%	1	+	0.71	2	x	12.4%	4	=	12.7%
Average										10.7%
CAPM Relevered Beta										
	Rf		+	β		x	(Rp)			k
Historical Market Risk Premium	3.9%	1	+	0.62	5	x	6.6%	3	=	8.0%
Current Market Risk Premium	3.9%	1	+	0.62	5	x	12.4%	4	=	11.6%
Average										9.8%
Financial Risk Adjustment										**-0.9%**

[1] Forecast of long-term treasury yields. See Schedule D-4.10
[2] Value Line Investment Analyzer data. See Schedule D-4.9
[3] Historical Market Risk Premium from (Rp) MorningStar SBBI 2012 Valuation Yearbook Table A-1 Long-Horizon ERP 1926-2011
[4] Computed using DCF constant growth method to determine current market return on Value Line 1700 stocks and CAPM with beta of 1.0 to compute Current Market Risk Premium (Rp). See Schedule D-4.11
[5] Relevered bata found on Schedule D-4.15

Rio Rico Utilities, Inc. dba Liberty Utilities
Financial Risk Computation
Unlevered Beta

Exhibit
Rejoinder Schedule D-4.14

Line No.		Company	VL Beta β_L[1]	Raw Beta Raw β_L[2]	Tax Rate t[3]	MV Debt D[4]	MV Equity E[4]	Unlevered Raw Beta β_U[5]
5	1.	American States	0.70	0.55	41.7%	24.7%	75.3%	0.46
6	2.	Aqua America	0.60	0.40	32.9%	25.3%	74.7%	0.33
7	3.	California Water	0.65	0.48	40.5%	35.8%	64.2%	0.36
8	4.	Connecticut Water	0.75	0.63	41.3%	34.2%	65.8%	0.48
9	5.	Middlesex	0.70	0.55	32.7%	29.9%	70.1%	0.43
10	6.	SJW Corp.	0.85	0.78	41.1%	39.9%	60.1%	0.56
13		Sample Water Utilitie	0.71	0.57	38.4%	31.6%	68.4%	0.44

[1] Value Line Investment Analyzer data. See Schedule D-4.13
Value Line uses the historical data of the stock, but assumes that a security's beta moves toward the market average over time. The formula is as follows:
Adjusted beta = .33 + (.67) * Raw beta

[2] Raw Beta = (VL beta - .33)/(.67)

[3] Effective tax rates per Value Line Analyzer Data (March 6, 2013).

[4] See Schedule D-4.3

[5] Raw B_u = Raw B_L/ (1+ (1-t)*D/E)

Exhibit
Rejoinder Schedule D-4.15

Rio Rico Utilities, Inc. dba Liberty Utilities
Financial Risk Computation
Relevered Beta

Line No.		Unlevered Raw Beta β_U[1]	MV Book Debt BD[2]	MV Equity Capital EC[2]	Tax Rate t[3]	Relevered Raw Beta $\beta_{RL}=\beta_U(1+(1-t)BD/EC))$ β_{RL}	VL Adjusted Relevered Beta .33 + .67(Raw Beta) β_{RL}
5	Rio Rico Utilities, Inc. dba Liberty Utilities	0.44	0.0%	100.0%	38.60%	0.44	0.62

13 [1] Unlevered Beta from Schedule D-4.14.
14 [2] Proforma Capital Structure of Company

Line No.		BV (in Thousands)			MV (in Thousands)	MV %
17	Long-term Debt	$ -	1.00		$ -	0.00%
18	Preferred Stock	$ -	1.00		-	0.0%
19	Common Stock	$ 100	2.28	(a)	228	100.0%
20	Total Capital	$ 100			$ 228	100.0%

22 (a) Current market-to-book ratio of sample water utilities. See work papers.

24 [3] Current Tax rate based on test year at proposed rates.

Rio Rico Utilities, Inc. dba Liberty Utilities
Size Premium[1]

Exhibit
Rejoinder Schedule D-4.16

	Beta(β)	Size Premium	Risk Premium for Small Water Utilities[7]
Mid-Cap Companies[2]	1.12	1.14%	
Low-Cap Companies[3]	1.23	1.88%	
Micro-Cap Companies[4]	1.36	3.89%	
Decile 10[5]	1.41	6.10%	3.67%

	Risk Premium for Small Water Utilities
Estimated Risk Premium for small water utilities[6]	0.99%

[1] Data from Table 7-8 of Morningstar, *Ibbotson SBBI 2012 Valuation Yearbook.*
[2] Mid-Cap companies includes companies with market capitalization between $1,621 million and $6,896 million.
[3] Low-Cap companies includes companies with market capitalization between $423 million and $1,620 million.
[4] Micro-Cap companies includes companies with market capitalization less than $422 million.
[5] Decile 10 includes companies with market capitalization between $1.0 million and $206 million.
[6] From Table 2, Thomas M. Zepp, "Utility Stocks and the Size Effect Revisited," *The Quarterly Review of Economics and Finance*, 43 (2003), 578-582.
[7] Computed as the weighted differences between the Decile 10 risk premium and the inidicated risk premiums for the sample water utlities as shown below. Excludes risk due to differences in beta.

		Market Cap. (Millions)	Class	Size Premium	Difference to Decile 10	Weight	Weighted Size Premium
1.	American States	$ 1,039	Low-Cap	1.88%	4.22%	0.166667	0.70%
2.	Aqua America	$ 4,129	Mid-Cap	1.14%	4.96%	0.166667	0.83%
3.	California Water	$ 862	Low-Cap	1.88%	4.22%	0.166667	0.70%
4.	Connecticut Water	$ 260	Micro-Cap	3.89%	2.21%	0.166667	0.37%
5.	Middlesex	$ 310	Micro-Cap	3.89%	2.21%	0.166667	0.37%
6.	SJW Corp.	$ 517	Low-Cap	1.88%	4.22%	0.166667	0.70%
	Weighted Size Premium for Small Companies						3.67%

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BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF RIO RICO UTILITIES, INC., AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANTS AND PROPERTY AND FOR INCREASES IN ITS WATER AND WASTEWATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.	DOCKET NO: WS-02676A-12-______

DIRECT TESTIMONY OF

GREG SORENSEN

May 31, 2012

EXHIBIT
A-7
ADMITTED

TABLE OF CONTENTS

I. INTRODUCTION AND PURPOSE OF TESTIMONY

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Greg Sorensen. My business address is 12725 W. Indian School Road, Suite D-101, Avondale, AZ 85392.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?

A. On behalf of the Applicant Rio Rico Utilities, Inc. ("RRUI" or "Company").

Q. BY WHOM ARE YOU EMPLOYED?

A. I am employed by Liberty Utilities as Vice President of Service Delivery. Liberty Utilities is the same entity formerly known as Liberty Water. In order to better align our operations to reflect our serving water, sewer, gas and electric customers we have updated our name.

Q. THANK YOU, PLEASE CONTINUE.

A. Liberty Utilities, like RRUI and all of the other subsidiary utility providers and service companies, is ultimately owned by Algonquin Power Utility Corporation, or APUC, a publicly traded member of the Toronto Stock Exchange. Through its distinct operating subsidiaries, APUC owns and operates a diversified portfolio of $1.2 billion of clean renewable electric generation and sustainable utility distribution businesses in North America. Liberty Utilities Co., APUC's regulated utility business, provides regulated water and electric utility services to more than 120,000 customers with a portfolio of 22 water and electric utility systems. Pursuant to previously announced agreements, Liberty Utilities is committed to acquiring Granite State Electric Company, a New Hampshire electric distribution company, EnergyNorth Natural Gas Inc., a regulated natural gas distribution utility, and certain regulated natural gas distribution assets in Missouri, Illinois and Iowa, which together serve approximately 213,000 customers. Algonquin Power Co. (APCo), APUC's electric generation subsidiary, includes 45 renewable energy facilities and 12 thermal energy facilities representing more than 460 MW of installed capacity. APUC's common shares and convertible debentures are traded on the Toronto Stock Exchange under the symbols AQN and AQN.DB.B. The APUC website is www.AlgonquinPowerandUtilities.com.

Q. PLEASE DESCRIBE LIBERTY UTILITIES AND YOUR ROLE AS VICE PRESIDENT.

A. Liberty Utilities is the indirect APUC subsidiary that owns and operates water, sewer and, more recently, gas and electric utilities in California, New Hampshire, Missouri, Illinois and Iowa (www.libertyutilities.com). I am currently responsible for Liberty Utilities' operations in Texas, Missouri, Illinois, and Arizona.

In Arizona, I am responsible for the daily operations and administration of all the utilities, including RRUI, for the financial and operating results for each utility, for capital and operating cost budgeting, for rate case planning and oversight, and rate setting policies and procedures as they relate to the operations under my responsibility. I also oversee customer and development services, human resources, engineering and conservation planning.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE COMMISSION?

A. Yes, I have testified in Commission proceedings for all of Liberty Utilities' affiliate entities, including several rate cases.

Q. WHAT IS THE PURPOSE OF THIS DIRECT TESTIMONY?

A. To support RRUI's application for rate relief. Specifically, I will provide background on the Company and its operations. I will also summarize significant capital improvements completed by the Company and other operating cost changes since the last rate case that are now contributing to the need for this rate case. Finally, I will address certain aspects of the relief being requested in this case, including approval of certain changes to our tariff of rates and charges for water and wastewater service.

II. OVERVIEW OF RIO RICO UTILITIES, INC.

Q. PLEASE PROVIDE AN OVERVIEW OF RRUI.

A. The Company provides both water and wastewater service to its customers. The Company's service area is located in Santa Cruz County, Arizona, north of the city of Nogales. The Company's water and wastewater CC&Ns are geographically the same. However, due to varied terrain, wastewater service is generally concentrated in the central portion of the service area and, as such, includes fewer customers. Those who are not provided sewer service by the Company utilize septic tanks.

Our water customers include a number of commercial, a few industrial and several irrigation customers. The 5/8 metered residential class, which is the largest customer class, uses an average of 7,794 gallons per month.[1] RRUI is an industry leading provider of water and wastewater services in Santa Cruz County and has received several awards in the past few years for operational excellence, including the Arizona Water Association (formerly AWPCA) Small Water Distribution System of the year for 2003, 2005, and 2010, and the 2005 Small Wastewater Collection System of the year, as well as an Award of Merit for outstanding safety record in 2010. These awards are given for significant efforts to provide safe drinking water and protect public health.

Q. PLEASE DESCRIBE THE COMPANY'S WATER RESOURCES.

A. The Company's water supply comes from groundwater. The groundwater is pumped from 6 wells directly into the distribution system or into one of five storage facilities for later distribution to customers. All water supplies are chlorinated prior to delivery to customers for disinfection purposes. The Company

[1] *See* Direct Testimony of Thomas J. Bourassa at Schedule H-2, page 1.

and our customers are fortunate that the groundwater in the area has not yet required significant treatment for any constituents such as arsenic or nitrates. However, due to the vast elevation differences within the distribution system, which includes 7 different 150 foot pressure zones, the Company utilizes 27 booster stations to maintain proper pressure for its customers. RRUI's service territory is within the Santa Cruz Active Management Area.

Q. DOES THE COMPANY PROVIDE WATER SERVICE FOR IRRIGATION?

A. Yes. The Company does supply water to three school complexes, one hotel, and two parks, including the one used for the local Little League. The Company also supplies water to Rio Rico Properties for use in irrigating medians, common areas and drip irrigation, and provides separate irrigation water to a few residential customers who requested a dedicated irrigation line. There is one golf course in our service area, but RRUI only supplies domestic water for potable use. RRUI does not provide water for landscape irrigation to any golf courses at this time. The one golf course in our CC&N has its own well, which it uses for its irrigation needs. Additionally, our wastewater is treated at the Nogales International Wastewater Treatment Plant ("NIWWTP"), and transporting effluent from that plant over ½ mile, uphill and under the Santa Cruz River, would be extremely cost prohibitive.

Q. PLEASE DESCRIBE THE COMPANY'S PRIMARY WASTEWATER TREATMENT FACILITIES.

A. The Company has purchased 550,000 gallons per day of treatment capacity from the City of Nogales ("City"). The Company also has two sets of three evaporative ponds. The first set of three ponds has a general permit to treat up to 20,000 gallons per day of sewage. The second set of three ponds is permitted to treat up to

150,000 gallons per day of sewage on an emergency basis only. The collection system includes five lift stations, four of which pump wastewater for treatment under our agreement with the City, and the remaining pump to the aforementioned evaporative ponds.

Q. WHAT WERE THE COMPANY'S AVERAGE DAILY AND PEAK FLOWS DURING THE TEST YEAR?

A. During the test year, RRUI delivered wastewater to the City of Nogales WWTP plant in the following amounts:

- Approximately 385,000 gallons per day on an annual average basis,
- A peak monthly flow of approximately 406,000 gpd in April and May 2011, and
- A peak day flow of 481,000 gpd during December 2011.

During the Test Year, the Company delivered approximately 13,500 gpd to the North Sewer Basin evaporative ponds on an average annual basis.

Q. WHEN DID THE CURRENT RATES GO INTO EFFECT?

A. The Company's current rates were approved in Decision No. 72059 (January 6, 2011) and became effective on February 1, 2011. These rates were based on a test year ending December 31, 2008. Because the Company is utilizing a test year ending February 29, 2012 in this filing, it will be just over three years between test years.

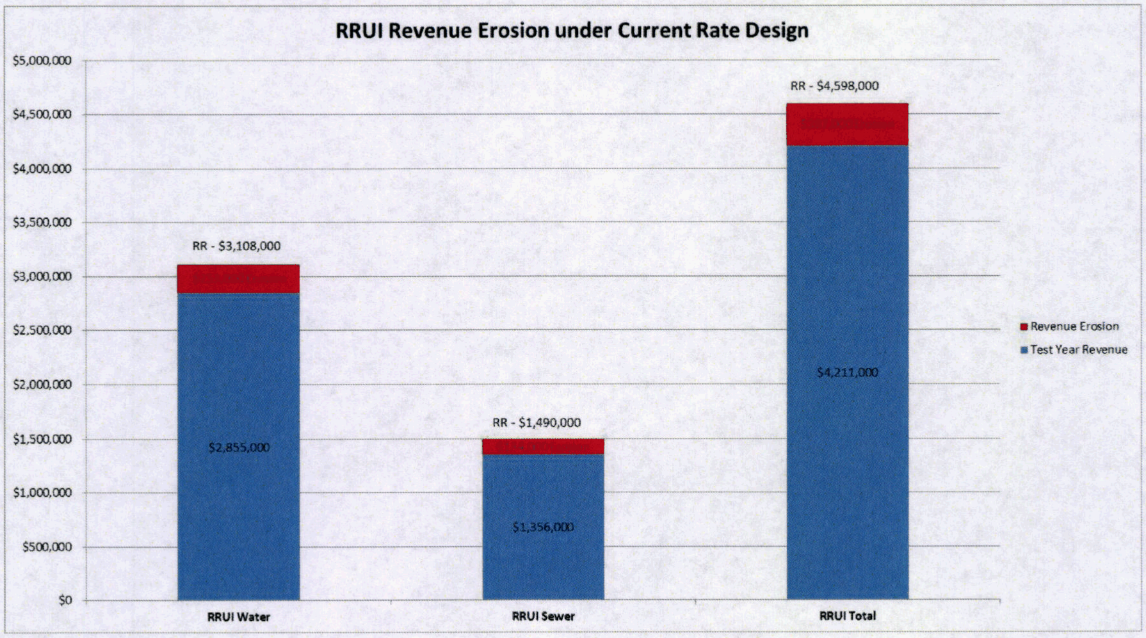
Q. HAS THE COMPANY EXPERIENCED GROWTH SINCE THE LAST RATE CASE?

A. No, there has been very minimal growth of less than 2% per year in the system since the last rate case. However, RRUI's aging system has required additional capital investment that has contributed to the need for the current filing.

Q. WHY IS RRUI FILING FOR NEW RATES AT THIS TIME?

A. There are several reasons. First, our shareholder has made additional and substantial investment in water and wastewater infrastructure to serve our customers in the RRUI service areas and this infrastructure investment needs to be included into rate base. Second, some of our operating expenses have increased. Third, the Commission has in the past expressed concern that some of Liberty's utilities waited too long to file rate cases, so we are trying to keep rates current and rate hikes manageable, by following a fairly regular rate case cycle.

Finally, in the prior rate case, the expected revenue for water was $3,108,000 and $1,490,000 for sewer. However, as noted in Mr. Bourassa's C schedules, during the test year our actual revenues were $2,855,000 and $1,356,000, for water and sewer, respectively. Collectively, we earned almost $400,000 less in the test year than the revenue authorized in the prior rate case.



Q. CAN YOU POINT TO A REASON OR REASONS FOR THIS REVENUE SHORTFALL?

A. As I'm sure will be pointed out, a revenue requirement is an estimated target, not a guarantee and revenues and expenses can move up or down after a test year. Admittedly, it is hard to express these events in precise numbers. Nevertheless, I believe we have experienced some degree of revenue erosion.

Q. WHAT DO YOU MEAN, MR. SORENSEN?

A. In our last decision, the Commission adopted Staff's rate design, a rate design that put approximately 70% of our revenue recovery in the commodity charge. By relying so heavily on volumetric charges, we were exposed to and suffered significant revenue erosion. This has left the Company in the position of significantly under-earning on its invested capital as Mr. Bourassa addresses more completely in his testimony.

III. SUMMARY OF SIGNIFICANT SYSTEM IMPROVEMENTS AND OTHER CHANGES SINCE THE LAST TEST YEAR

Q. CAN YOU DESCRIBE THE "SUBSTANTIAL INVESTMENT" YOU TESTIFIED HAS BEEN MADE SINCE THE LAST TEST YEAR?

A. Yes. Since the last rate case, RRUI has purchased a new building for its offices, rehabilitated a 28-year old water plant, and paid approximately $2 million for upgraded treatment capacity and a new agreement with the City. Additionally, the Company has made ongoing investment to improve the water distribution and wastewater collection system and service lines.

A. Nogales Upgrade

Q. THE SEWER DIVISION HAS SEEN A SIGNIFICANT INCREASE IN RATE BASE SINCE THE LAST RATE CASE. WHAT SUBSTANTIAL UPGRADE(S) LED TO THIS INCREASE?

A. The primary reason for the significant increase in rate base is the cost of our pro rata share of the cost to upgrade the Nogales wastewater treatment facility, or NIWWTP. A map of the plant's location is attached as Exhibit GS-DT1.

Q. CAN YOU PROVIDE A BRIEF SUMMARY OF THE SITUATION?

A. Since the last test year, we have paid the City an additional $1,822,000. With the $427,000 payment made to Nogales that is already in rate base, and the approximate $181,000 of additional costs, we have now invested $2,424,000 to upgrade the treatment plant where about 97% of our collected waste is treated. This second payment, and the associated legal and consulting costs, was incurred after the Company was sued by the City.

Q. THE CITY SUED RRUI?

A. Yes. We had a dispute with them regarding our obligation to share in the costs of upgrades to the NIWWTP needed to address operational compliance issues at the plant. We were originally told by the City that we had to pay $2.75 million. However, after all the negotiations and proceedings in Court, we paid about $2.43 million, saving our customers over a quarter million dollars that would have been included in rate base. So, at the end of the day, we were contractually obligated to pay about $4.42 per gallon for used and useful plant to help bring the NIWWTP closer to regulatory compliance, and saved our customers money compared with the original demand and obligation to the City under the contract. On top of that, we reached a new long-term treatment agreement that clarifies our rights and obligations and minimizes the likelihood of similar disputes in the future.

Q. DOES THE CITY OWN THE NIWWTP?

A. I believe the City is a part-owner in the facility, along with the United States Section of the International Boundary and Water Commission (USIBWC). However, the 14.2 MGD treatment plant was mostly paid for by a federal grant and the plant is actually operated by the USIBWC, an international cooperative agency of sorts. The NIWWTP treats wastewater flows from the City, RRUI, and the City of Nogales, Sonora, Mexico.

Q. WHY DID NOGALES UPGRADE THE NIWWTP?

A. The technical explanations could fill many pages of testimony and are outside my area of specialty. However, I think the City's reasons can be summed up as follows – in order to continue to treat wastewater, in a manner commensurate with applicable regulations, the plant had to be upgraded. In general, the plant was not meeting regulatory standards for TSS and Nitrogen. There were also improvements needed for disinfection and sludge treatment. **Q. DID RRUI INCREASE ITS CAPACITY ALLOTMENT AT THE NIWWTP?**

A. No, we had an allotment of 550,000 gpd before and after the upgrades. These were upgrades to the existing facility to bring it into compliance and process wastewater in an appropriate manner. The overall cost per gallon for these upgrades was about $4.42.

Q. DID RRUI PARTICIPATE IN THE DECISION-MAKING?

A. No, and that was a point of contention between the Company and the City. There were others. I will try to provide further background.

RRUI entered into a contract for treatment with the City in 1996. Under that agreement, the Company purchased an interest in the NIWWTP and paid a monthly fee for treatment. The Company also had the right to purchase additional capacity interests, a right we exercised on two separate occasions to bring us to our current total of 550,000 gpd. Then, in 2006, the City informed the Company that it owed the City for its pro rata share of the cost of upgrading the treatment capacity at the NIWWTP. This demand for payment caught us by surprise. As I said, we had not been involved in the decision-making and, at that time, we didn't know why the plant was being improved or why we had to pay for it.

Q. DID RRUI RAISE THESE CONCERNS WITH THE CITY?

A. Yes, we balked at first and raised a number of concerns. The City, though, was under tremendous pressure because the plant was being funded by a federal grant, which grant, the City claimed, could not benefit RRUI or its customers. Therefore, the City argued that we had to pay our own share. The saber rattling reached a peak when the City threatened to send us notice they would stop taking our flows. Soon after receiving the City's demand, we received their offer in the form of a Memorandum of Agreement, which was eventually finalized in December 2006. In this agreement, we agreed to pay the City \$2.75 million (\$5 per gallon) to upgrade our capacity. This is the \$2.75 million I mentioned above.

Q. DIDN'T THAT END THE MATTER?

A. No. When we made our deposit payment on December 29, 2006, in the amount of \$427,000, we paid it "Under Protest." Then, when the City attempted to collect the rest of the money for the upgraded capacity, we refused to pay and the City sued RRUI in Superior Court.

Q. SINCE YOU PAID THEM DOES THAT MEAN YOU LOST THE LITIGATION?

A. Not at all. During mediation, we reached terms for settlement and later entered into a settlement agreement. Thereafter, the City and the Company entered into a new and much improved wastewater treatment agreement. All in, including legal expenses, we spent approximately $181,000.

Q. **WHAT "LEGAL EXPENSES" MR. SORENSEN?**

A. The legal fees, expert witness and court costs were incurred in connection with negotiation of multiple agreements related to the plant upgrade and the litigation initiated by the City against RRUI.

Q. **WHY SHOULD THOSE COSTS BE INCLUDED IN THE COST OF THE PLANT UPGRADE?**

A. Because all of these costs were incurred in connection with the placement of used and useful plant in service. Legal expenses are commonly capitalized with plant costs. For example, if we had to build a plant and had to condemn a plant site, we would capitalize those legal costs and expect them to be included in rate base. There's no question whether legal expenses can be capitalized and included in rate base. They can, as long as they are prudent and reasonable.

Q. **THEN WHY ARE THESE LEGAL COSTS PRUDENT AND REASONABLE?**

A. By taking the legal action to pay under protest, we initiated a series of events that culminated in an all in price that was $320,000 less than the amount the City originally demanded we pay. We also replaced a less than adequate agreement we inherited from our predecessor-owner. In the end, we spent $4.42 per gallon for long-term treatment capacity. For the Company and its customers, it was a better result than the City's initial demand would have been and we made certain that any and all expenditures were necessary, reasonable and prudent.

Q. **BUT DIDN'T THE COMPANY TAKE A RISK MR. SORENSEN?**

A. Yes, we took a risk. But we had no intention of spending almost $3 million of our money to be recovered from our customers for something we thought we already had without first making sure we were being reasonable and prudent. I have heard the argument that regulated utilities will just spend money because they can recover it. We showed that certainly isn't the Liberty approach. We had no intention of coming to this Commission and asking to recover any of these costs until I could testify this was a necessary investment in used and useful plant, and we got the best deal we could. While it was a hard road, and not one I would choose, we feel that we did the right thing and in the end got a better deal and better contract, so the risk was well taken.

B. <u>Water Plant Rehab</u>

Q. PLEASE DESCRIBE THE IMPROVEMENTS THAT WERE MADE TO THE WATER UTILITY FACILITIES AND WHY THEY WERE NECESSARY.

A. Water Plant 58 ("WP58") is a two-zone booster station serving our 3950' and 4100' pressure zones in the Southeast section of our CC&N. It is capable of producing 300gpm for each zone. WP58 was originally constructed in 1983 and had reached the end of its useful life. The hydropneumatic tanks had significantly rusted, the electrical components were obsolete and we could no longer obtain replacement parts. Both tanks were fully replaced with bladder tanks combined with VFDs, which should result in a more efficient operation of the pump systems. The electrical system was replaced and brought up to current code as part of this project. The facility also now includes a solar-powered LED yard light, so after-hours lighting is now "solar-powered," which reduces safety hazards to our employees and the public. Capacity was not expanded and this facility was necessary to continue, and is used and useful in providing service to our current customers.

Q. WHAT WAS THE TOTAL COST OF THESE IMPROVEMENTS?

A. The total cost of this rehabilitation project was $336,000, and represents an approximate 1% increase in water rates.

C. <u>New Office Building</u>

Q. WHEN DID RRUI MOVE ITS OFFICES?

A. The Company purchased an existing office building in its service territory in November 2011. We then made tenant improvements so the building could serve the needs of the Company and its customers. We began serving our customers from the "new" office in February 2012. We were in communication with the Commission Staff (Consumer Services) during the migration process, in order to keep them aware in case there were any customer concerns or issues.

Q. WERE THERE ANY ISSUES?

A. There were no material issues that I am aware of. In general, we have received many positive comments regarding the new offices; the look, feel, and convenience all seem to be positively received by our customers.

Q. WHY DID THE COMPANY CHANGE OFFICES?

A. In March 2009 we were notified by our then-landlord that they intended to demolish the aging building complex where our offices had been located and that they would not renew our lease. We were "allowed" to continue on a month-to-month basis and we set out to find a new location. It took a little while but in 2011, we found what we believed to be a good value used building, and purchased it. This site was unique in that it was only ½ mile from our leased facility, so that minimized the locational impact to our customers. Additionally, this facility came with a fenced yard so our trucks could park securely overnight, and it had a small shop area for our operators to keep tools and make minor repairs on meters and equipment.

Q. WHAT OTHER OPTIONS WERE CONSIDERED?

A. We considered staying in our existing facility and waiting for the landlord to finally make their business decision to raze the existing buildings and build new ones. This had some significant risks to it, including transition timing and potentially being out of our existing space before a new space was ready. Also, we didn't know how expensive the new facility would be, but were told it would be "very nice."

We also looked at comparable spaces available in the Rio Rico market both before we purchased and in the context of running "comps" during the purchase process. We also examined the rental market for suitable buildings in the area, of which there were few, and found them to be comparable to purchasing a building when all aspects were considered. The building we purchased was a good value for the money, and will provide a quality office and operator space for our employees and our customers alike.

Q. WHAT IS THE COST TO BE INCLUDED IN RATE BASE?

A. The total cost of the building was $386,000, plus $100,000 in renovations and other costs, for a total of $486,000, which is allocated based on customer count 75% to water and 25% to wastewater rate base. Additionally, rent for the prior office space has been removed from our operating expenses, as detailed in Mr. Bourassa's testimony.

D. <u>Operating Expenses</u>

Q. HAVE THERE BEEN ANY SIGNIFICANT CHANGES OR INCREASES IN OPERATING EXPENSES SINCE THE LAST TEST YEAR?

A. First, as Mr. Eichler explains in his testimony, there were significant improvements in the corporate cost allocation methodology since the last rate case. Second, we have seen a decrease in the purchased power costs for water of approximately

$22,000 due in part to volume of gallons pumped, but also due to more efficient operational and pumping practices. There has also been a slight decrease in insurance costs, primarily driven by "volume pricing" discounts that our corporate parent is able to obtain as a significant global customer. On the other hand, some costs have increased since the last rate case. We saw an increase in transportation expense, primarily driven by rising gas prices compared to the previous test year. Finally, property taxes increased significantly due to rising tax rates as cities and counties try to recoup tax revenue lost to budget cuts from the State funds.

Q. WHAT STEPS HAVE BEEN TAKEN TO REDUCE OPERATING COSTS?

A. At Liberty Utilities, we are always conscious of the cost of service we provide to our customers, and we remain constantly aware that our customers will eventually pay for every dollar we incur in operating costs and capital expenditures. As such, we constantly evaluate our operations to see if there are better and/or less expensive ways to do things, without sacrificing quality of service to our customers. Since the last test year, RRUI made four significant cost savings changes to operations. First, in mid-2010, RRUI began to do complete replacements of leaking service lines rather than merely repairing the lines. This change in practice has helped reduce non-revenue water (as described below), as well as reduced the number of service leaks from 17.2/month for the 12 months ended August 31, 2010 to 9.8/month during the test year. With an average cost of $2,500 per event, this saves about $18,000 per month in replacement costs. While this is capital as opposed to operating expense, it has been a better value to our customers.

Second, RRUI expanded the use of SCADA for our well control. This has allowed us to better utilize our wells, allowing for longer well run-times, thus reducing electric costs. An example would be for Well #5, which in 2008 had an average gallons pumped per KWH of 263, but in the test year the average was 413 gallons per KWH. This is a much more efficient operation now and we look to continuously improve each year.

Third, on the wastewater side, we historically had issues with the build-up of solids in Lift Station #3. We have installed an automated enzyme feeding system which reduced the solids build-up, leading to easier cleaning of the wet wells, and reduced call-outs for contractors with vacuum trucks to clean the lift stations. This reduced need for cleaning lift stations saved the Company, and in turn the ratepayers, approximately $7,000 per year.

Finally, as I will more fully describe below, we changed our service disconnect program for non-payments. This led to reduced bad debt expense and decreased overtime hours for our operators, while simultaneously increasing customer satisfaction, all due to the reduced number of actual disconnects.

IV. COMPLIANCE, CONSERVATION, CUSTOMER SERVICE AND CUSTOMER SATISFACTION

Q. WHAT IS RRUI'S COMPLIANCE STATUS?

A. To the best of my knowledge, we are in compliance with all ADEQ, ADWR, ADOR, and ACC rules and regulations regarding the provision of water and wastewater services in the State of Arizona. We take compliance with regulations very seriously and, if ever there is an issue, we will take immediate steps to correct the problem. Liberty has a strong compliance program led by our Operations staff and reviewed by our Environmental Health and Safety staff. We take our stated Company values of "Care, Quality, Responsibility, Service, Community and Family" very seriously, and regulatory compliance is a key aspect of adherence to those values.

Q. IN THE LAST RATE CASE THERE WERE SOME CONCERNS OVER NON-REVENUE WATER. WHAT STEPS HAVE BEEN TAKEN TO ADDRESS THIS CONCERN?

A. As mentioned above, since the last rate case we changed our procedures on service line water leaks. Previously, we tried to patch leaking service lines, but found the leaks would re-occur in some instances. Therefore, we decided that, in most cases in the RRUI system, it is more prudent to fully replace the service lines when leaks are detected.

Also, as a result of discussions with Commission Staff in our last case, we improved our tracking of non-revenue water to ensure compliance with AWWA standards for non-account water and loss calculations. Additionally, we worked closely with the Santa Cruz County Public Works department to expedite ROW permits which decreased the time it takes us to make actual repairs to leaking water pipes under county roads.

Q. WHAT WAS THE COMPANY'S TEST YEAR NON-REVENUE WATER LEVEL?

A. It was just under 10%, at 9.92%.

Q. WHAT COSTS WERE INCURRED TO ADDRESS NON-REVENUE WATER?

A. At the end of our prior test year (2008), we purchased a backhoe which allowed us to make repairs more quickly and efficiently in the time since that rate case. Also, in 2011, we created a new employee position in Rio Rico – Construction Superintendent – whose primary job responsibility is to work on and coordinate contractors for the repair and replacement of leaking water and/or wastewater lines. Again, this reduces the time it takes to repair leaks, thus reducing the gallons lost.

Q. WHAT OTHER STEPS HAS THE COMPANY TAKEN TO ADDRESS WATER CONSERVATION SINCE THE LAST RATE CASE?

A. The Company voluntarily committed to 10 ADWR BMP's both before the last rate case as well as confirmed that commitment as part of our last rate case. We have complied with both ADWR and ACC requirements regarding those BMPs. Some examples of conservation efforts include the prominent display of conservation brochures and flyers in our customer accessible office, and quarterly conservation based newsletters which are sent to all customers as a bill insert. Customers who receive e-bills are provided a link which directs them to our website in order to view the quarterly conservation newsletter on-line. We also pride ourselves in getting out into the community and meeting with our customers to encourage conservation.

Before this past winter, we held a seminar which showed customers how to wrap and insulate their pipes to avoid freezing and breaking during the winter months, thus saving on wasted water caused by leaks on the customer side of the meter after hard freezes (yes, they do occur in our Southern Arizona service territories). Also, during April, we co-hosted a seminar with EPCOR's Tubac utility where customers from both utilities attended a landscaping presentation at our "new" office building. Customers who attended were provided information on their home water system after the meter demarcation point, characteristics of a typical landscape system, instructions on programming timers, and proper watering techniques so as to conserve water on landscaping. They were also taught how to self-audit their landscaping to detect leaks and proper water use. Finally, we also offer our customers the ability to determine their "water footprint" by using a customer calculator, available exclusively on our website.

Q. DOES THE COMPANY ENGAGE IN COMMUNITY OUTREACH PROGRAMS?

A. Yes, as part of our Company Core Values, we encourage employees to be part of the community in which we serve, and embrace community programs and events that are of interest to them. For example, each year Liberty Water sponsors and staffs a water booth at the Lucky Clover Race, a race event held by the local high school, where we hand out water to race participants. We also participate in the annual Rio Rico Fire and Safety Day. We present people with conservation information, and tie it back to the theme by stating that we should conserve water to ensure we always have it in an emergency situation. We do these things not because we have to, but because we believe it provides better overall customer service and satisfaction, and increases the opportunities to gather feedback from our customers about our service and their perceptions.

Q. HOW DOES THE COMPANY MEASURE CUSTOMER SATISFACTION?

A. We do so in the typical ways, like speaking with our customers when they call or come into our office, or when our Operators have the opportunity to chat with customers while in the field performing their duties, and as highlighted above through our involvement in community events. This is our "informal" way of soliciting feedback. We also take a more formalized approach of having a third party (Luth Research of San Diego, CA) conduct an annual customer satisfaction survey each August. This survey randomly selects about 1,000 customers from across our various Liberty Water (now Liberty Utilities South) utilities, and asks them approximately 22 questions in a 10 to 20 minute phone survey. These results are then analyzed by management, and are turned into an action plan to try to improve areas of need identified by the survey.

This survey was first done by Liberty in August 2009, and each year since then. I have attached the section of the 2011 survey related to Rio Rico (as part of Southern Arizona group, they were included in the survey results with our Sierra Vista systems) as Exhibit GS-DT2 to my testimony. Additionally, we have met each of the past two years with Commission Staff – Consumer Services group, to review not only the survey results, but also share other things we might be doing regarding providing excellent customer service. During these meetings, we also seek input from Staff as how they believe we can better improve our service.

Q. CAN YOU PROVIDE AN EXAMPLE OF SOMETHING YOU SHARED WITH STAFF DURING THESE MEETINGS?

A. Certainly. During our 2010 meeting, we mentioned to Staff that we were piloting a program at LPSCO (an affiliated utility serving Litchfield Park and Goodyear) to improve our disconnect process for non-payment of utility service. And we explained to Staff that, if successful, this pilot would be rolled-out to our other utilities. Our view was that the worst experience of providing utility service, and being a customer of utility service, was the process of disconnecting utility service for non-payment. This takes a toll on both our employees in the field and the customer service offices, and has a significant impact on the customer whose service is being terminated. So, we decided there must be a better way to do it, or ideally to improve the process to where there would be very few shutoffs that needed to be done.

Our course of action was a simple one. We decided that, approximately 5 days after sending the required disconnect communication to our customers, we would personally call those customers who had not yet responded, as a courtesy, to explain the situation and their options. Also, for those customers we were unable to reach by telephone and resolve the non-payment matter, approximately 2 days before disconnect, we placed door tags at their home as another way of reminding them payment was due and requesting that they contact our customer service representatives prior to the scheduled disconnect date.

Q. WAS THIS SUCCESSFUL?

A. Much more successful than I would have thought possible: Before implementing the test process at LPSCO, we had some concerns about how customers would view our attempts and ultimately whether such simple gestures would really have a significant impact. We weren't sure if they'd view our reminder calls to them as "harassing" collection calls, or as they were intended - a courtesy call to avoid the disconnect from occurring. Because of concerns such as this, our CSRs were instructed to be very courteous and accommodating in speaking with customers. I believe that because we took this type of approach, the pilot at LPSCO (see LPSCO results at Exhibit GS-DT3), and ultimately the rollout at our other utilities, was so successful.

After the success we had at LPSCO, we rolled out the program to Rio Rico in August 2011. We hired an additional part-time CSR to, among other things, assist with this process. Prior to this program, in January to August 2011, on average 16% of all disconnect notices sent to RRUI customers resulted in an actual service disconnection. After making a few fairly simple, courteous changes to our process, that figure dropped to 4.5% during the period from September 2011 to March 2012 (see attached chart as Exhibit GS-DT4).

Q. WHAT IS YOUR ASSESSMENT OF THESE RESULTS?

A. I find those to be amazing results, and I believe our customers appreciate the courteous, cooperative approach – nobody wants their water shut off, so we work with customers to minimize the chances of that happening to them. I know that informally our CSRs have received many "thank you" comments and calls for the approach we have taken, and that helps RRUI to avoid unnecessary negative interactions with our customers.

Finally, if a customer expresses that they are having difficulty in making payments, our CSRs are empowered to establish a work-out plan to catch them up, and the customer is also made aware of our Low Income Tariff whereby they can receive reduced rates if eligible for the program. The great news is that not only do we provide our customers with improved and kinder service, but in the long run, this approach will reduce bad debt expense in our operating costs, and reduces the overtime our Operators incur as a result of disconnecting and then reconnecting services for non-payment issues.

Q. HOW MANY COMPLAINTS HAS THE COMMISSION RECEIVED FROM RRUI CUSTOMERS SINCE THE LAST TEST YEAR?

A. We checked with Commission Staff, and during 2009 and 2010, when our last rate case was being prosecuted, we had 8 and 13 complaints, respectively. During 2011 and year-to-date 2012, we had 4 and 0 complaints, respectively. I believe our Customer Service personnel, as well as the Company as a whole, do a great job of working with our customers, and we strive to maintain a positive working relationship with the Consumer Services department of Commission Staff as well, and appreciate their support in ensuring that our customers are provided excellent service.

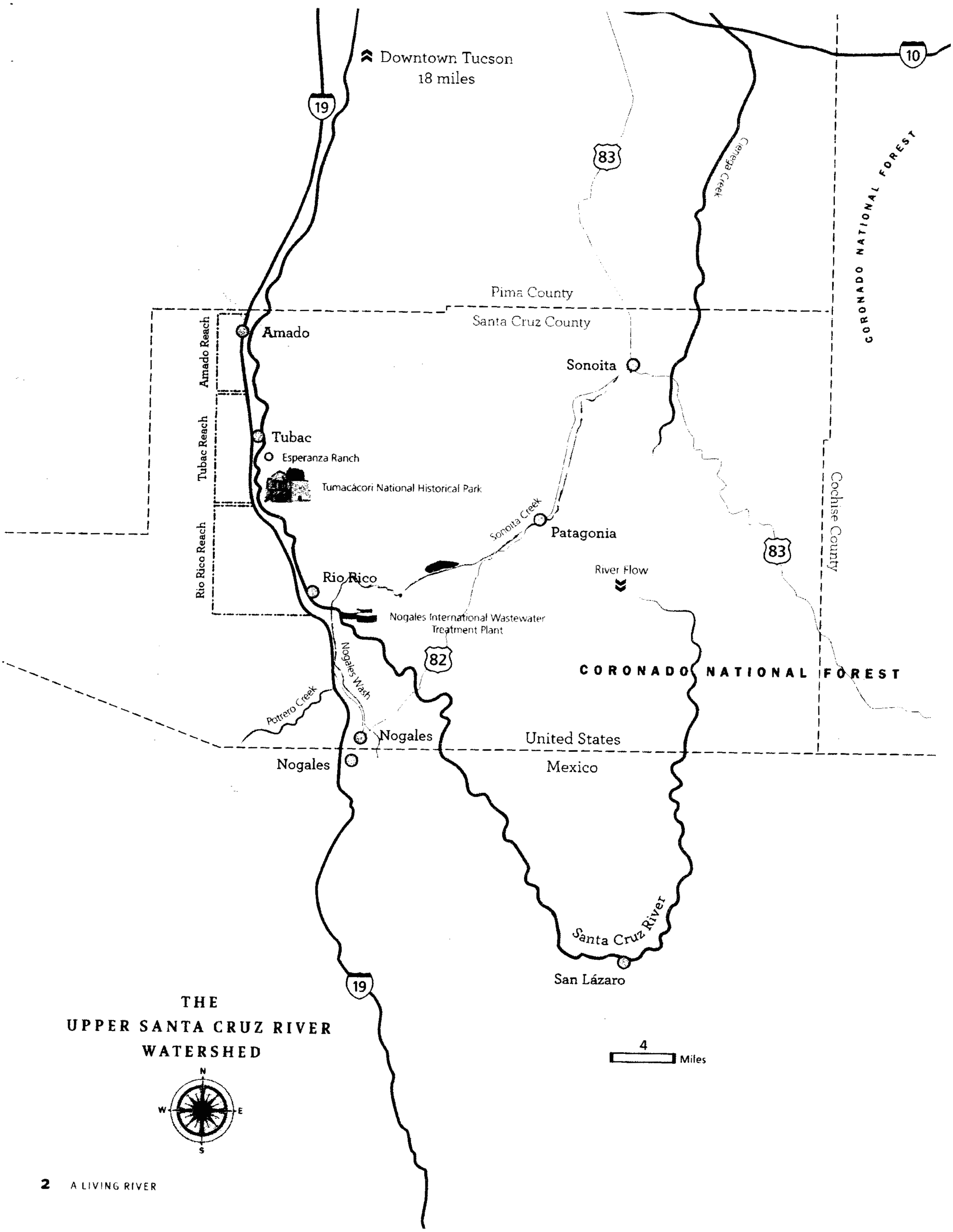
Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes.

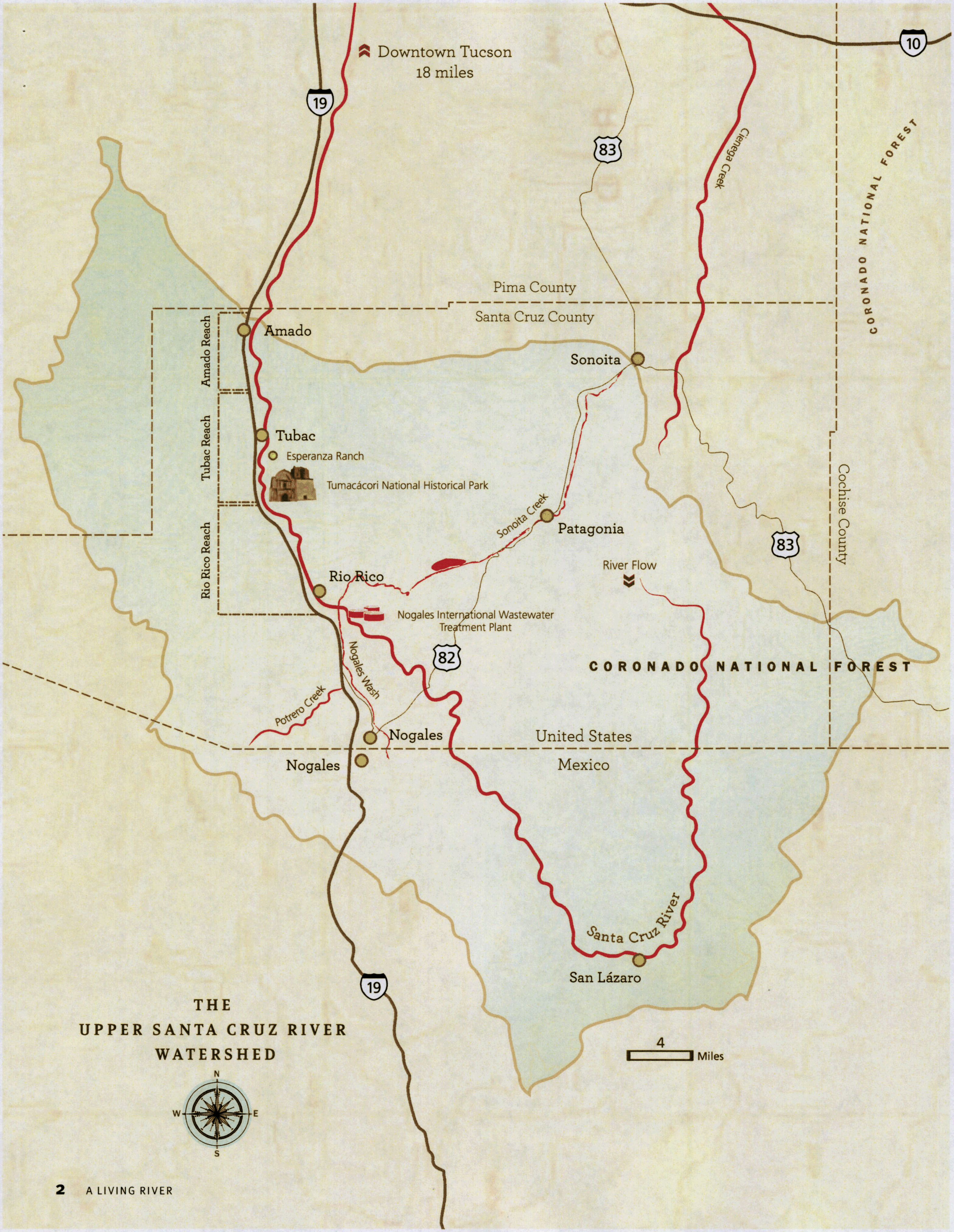
Rio Rico Utilities, Inc.
2012 Rate Application

Greg Sorensen Direct Testimony

Exhibit GS-DT1



THE
UPPER SANTA CRUZ RIVER
WATERSHED



Downtown Tucson
18 miles
19
10
83
Cienega Creek
CORONADO NATIONAL FOREST
Pima County
Santa Cruz County
Amado
Amado Reach
Sonoita
Tubac
Tubac Reach
Esperanza Ranch
Tumacácori National Historical Park
Sonoita Creek
Patagonia
Cochise County
Rio Rico Reach
83
River Flow
Rio Rico
Nogales International Wastewater Treatment Plant
82
Nogales Wash
CORONADO NATIONAL FOREST
Potrero Creek
Nogales
United States
Nogales
Mexico
Santa Cruz River
San Lázaro
19
THE
UPPER SANTA CRUZ RIVER
WATERSHED
4
Miles
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Rio Rico Utilities, Inc.
2012 Rate Application

Greg Sorensen Direct Testimony

Exhibit GS-DT2

Business Manager: Martin Garlant

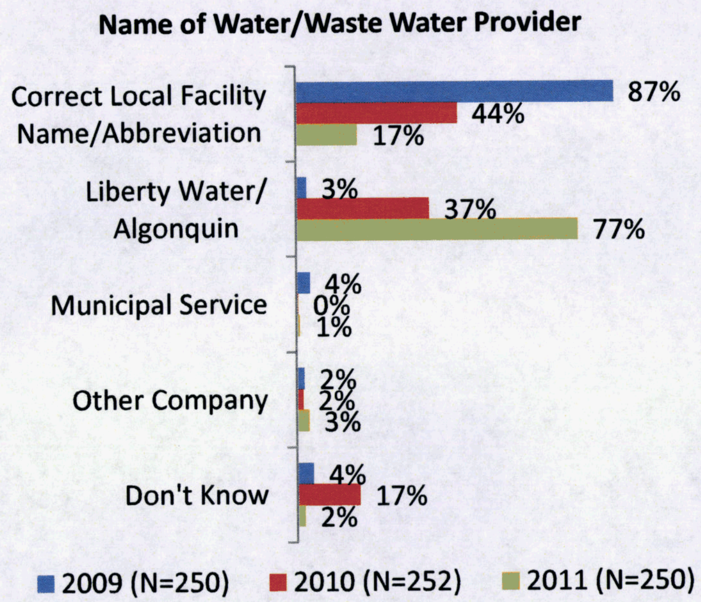
SOUTHERN ARIZONA
(BELLA VISTA, RIO RICO, NORTHERN SUNRISE, SOUTHERN SUNRISE)

Awareness & Perception

Familiarity with their water and waste water provider was high as the number of respondents citing *Liberty Water/Algonquin* (77%) more than doubled as compared to 2010. While 17% instead named their *correct local facility name/abbreviation*, the number citing *don't know* fell (2% in 2011 vs. 17% last year).

When asked to describe the provider, most comments were positive (78%) and general in nature (73%). While positive comments for *customer service* (8%) rose significantly in 2011, they were lower for *water quality* and *reasonable cost* as compared to 2009.

Nearly a third (29%) of respondents mentioned negative comments: *cost is too high* (17%) was the leading reason for negative associations with a noticeable increase as compared to 2009 and 2010.



Suggestions for Improvements	2009 (n=250)	2010 (N=252)	2011 (N=250)	Difference from 2010
Positive Comments (NET)	77%	78%	78%	0%
Positive general	73%	75%	73%	-2%
Water quality	9%	4%	2%	-2%
Cost is reasonable	6%	0%	2%	+2%
Customer service	4%	3%	8%	+5%
Negative Comments (NET)	26%	24%	29%	+5%
Cost is too high	10%	10%	17%	+7%
Water quality	9%	8%	8%	0%
Negative general	2%	4%	3%	-1%
Customer service	4%	4%	4%	0%

NOTE: Data in orange shaded cells are significantly higher; data in gray shaded cells are significantly lower: at 95% confidence level.

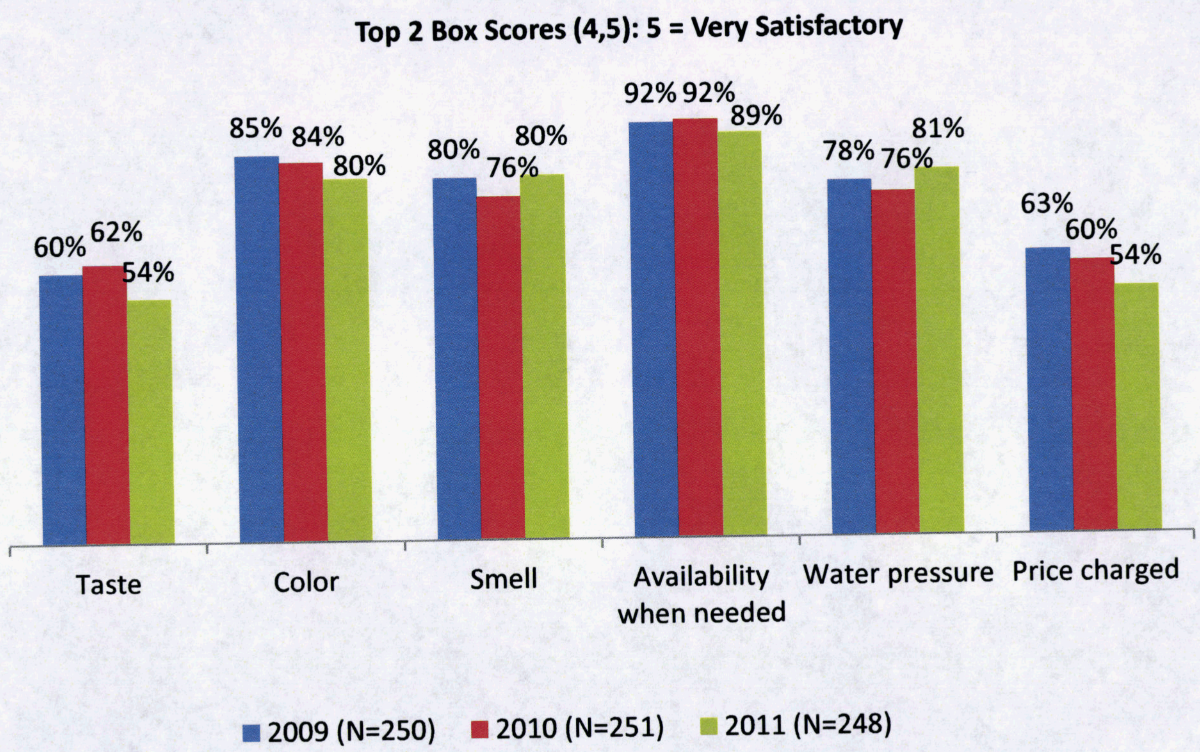
A1. What is the name of the company that provides water and/or waste water service to your household/business?

A2. How would you describe your water and/or waste water service company and the services it provides?

Water Services – Satisfaction

Respondents generally rated the water services they received highly. *Availability when needed* received the highest top 2 box score (89%; 4/5, where 5 = very satisfactory) but was slightly down (-3%). This was followed by *water pressure* (81%; up 5% as compared to 2010) and *smell* (80%, up 4%). While satisfaction with *color* was also at 80%, it is important to note that a downward trend in *color* continued (down 4% from 2010).

Taste of tap water and *price charged* tied for the lowest satisfaction scores (54% each). Each of these factors also experienced a 6% to 8% decrease as compared to 2010.

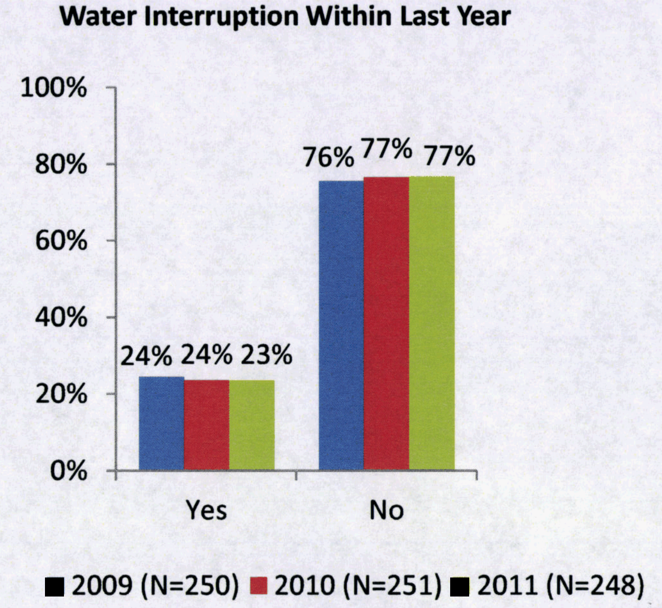


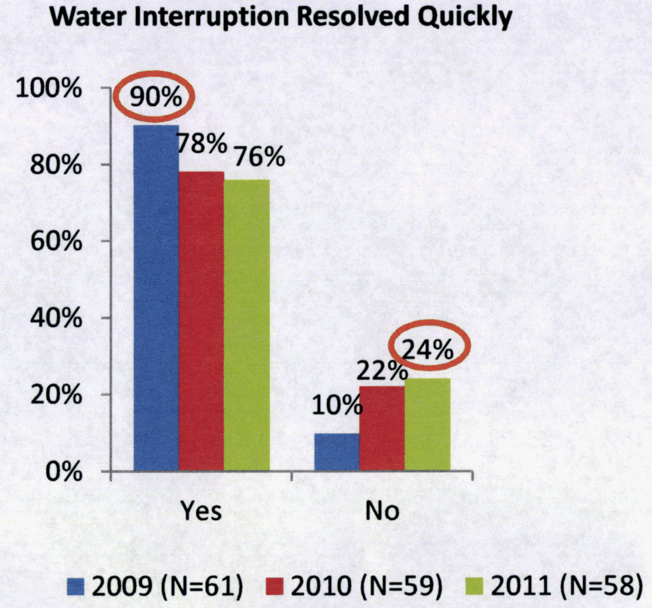
1. *Please rate your water services in the following areas by using a 5-point scale with 5 being "Very Satisfactory" and 1 being "Not Satisfactory At All".*

Water Services – Interruptions

Nearly a fourth (23%) of respondents had a water service interruption in the past year, which was on par with 2009 and 2010 data. Among these, 24% stated the interruption was not resolved quickly, an issue of increasing concern over the last two years.

Among those stating their water interruption issue was not resolved quickly, *resolution took too long* was the primary reason given.





Why Not Resolved Quickly (N = 14)
Resolution took too long (4mentions)
No explanation for interruption (1 mention)
Don't know (1 mention)
Other (8 mentions)

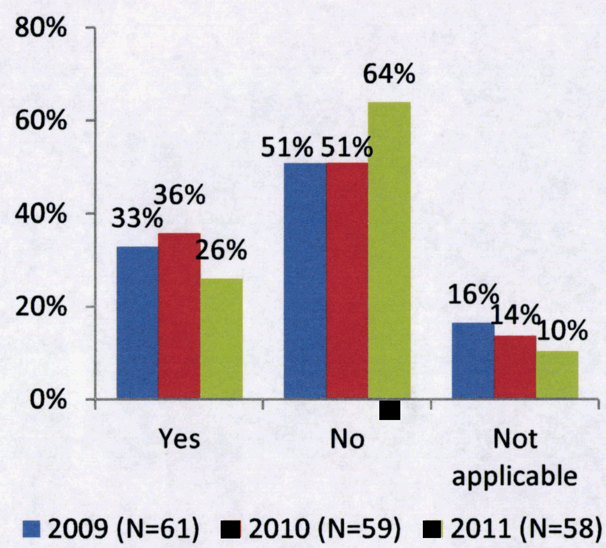
NOTE: Orange circled data indicates significant change/ difference compared to other year(s).

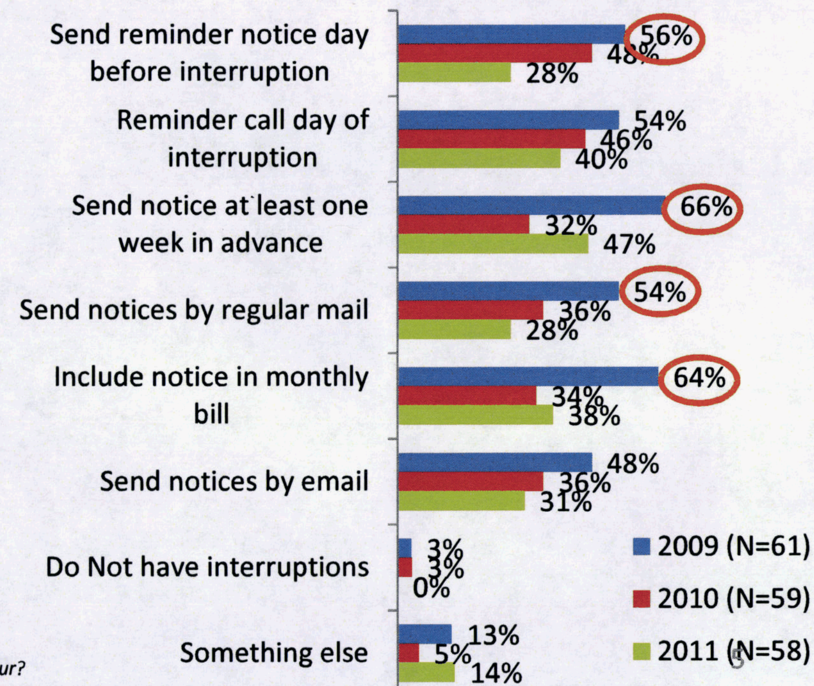
2. Within the last year, have you had any interruptions to your water service?
3. Was your water service interruption problem resolved quickly?
4. Being as detailed as possible, please tell us how and why your water interruption problem was not resolved quickly.

Water Services – Interruptions Notification

Of the customers who had a water interruption in the last year, a fourth (26%) stated they received an advance notification of scheduled interruptions. This was down by 10% as compared to 2010.

In terms of improvements for scheduled service interruptions, the top improvement requested was *send notice at least one week in advance* (47%) followed by *reminder call day of interruption* (40%).





NOTE: Orange circled data indicates significant change/ difference compared to other year(s).

5. Are you notified in advance when scheduled interruptions to water service will occur?

6. In which of the following ways could [INSERT FACILITY BASED ON ZIP CODE] improve their notifications of scheduled service interruptions? You may select all that apply.

Water Services – Improvements

Over half of the respondents (60%) had no suggestions on how to improve their water service, feeling it was fine as is. Among the improvements suggested were *lower rates/don't increase rates* (13%) and *improve water pressure* (5%).

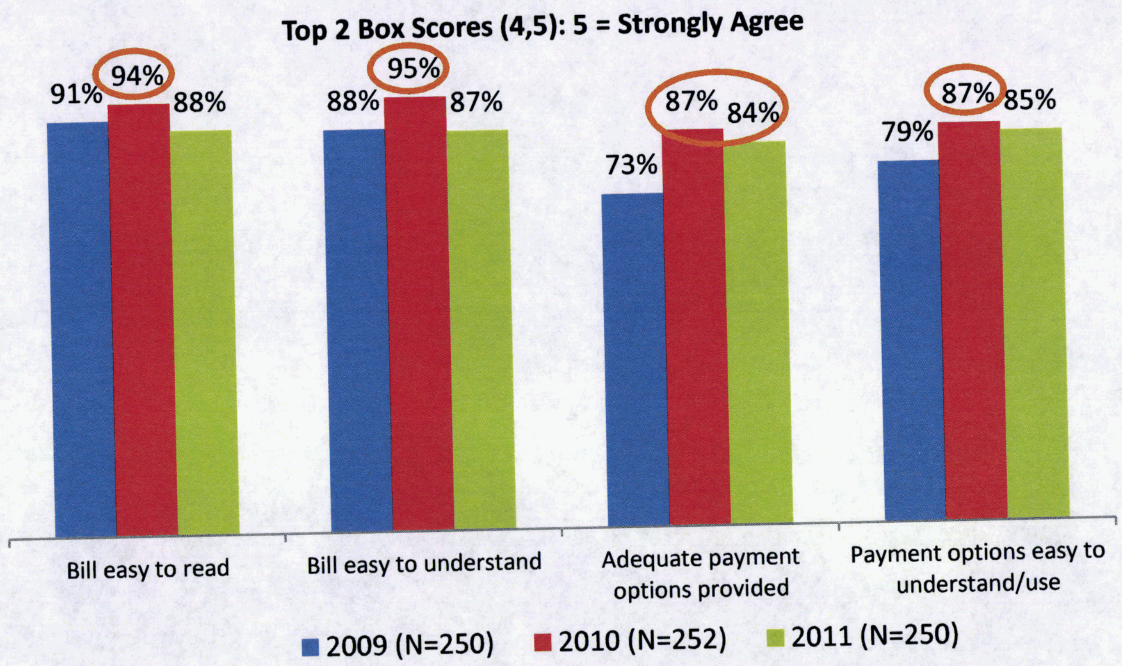
Suggestions for Improvements	2009 (n=250)	2010 (n=251)	2011 (n=248)	Difference from 2010
Lower rates/Don't increase rates	9%	11%	13%	+2%
Improve water pressure	6%	6%	5%	-1%
Maintain better/repair facilities/lines	2%	0%	2%	+2%
New/more water tower(s)/pumping station(s)	1%	3%	0%	-3%
No suggestions/fine as is	58%	61%	60%	-1%

NOTE: Data in orange shaded cells are significantly higher; data in gray shaded cells are significantly lower: at 95% confidence level.

7. Do you have any suggestions on how [INSERT FACILITY BASED ON ZIP CODE] could improve their water services?

Customer Billing – Satisfaction

Customer satisfaction with billing remained high with 84% or more of interviewed customers stating they somewhat or strongly agreed that they were satisfied with all of the factors tested. However, scores were slightly lower in 2011 as compared to 2010. While some scores were only lower by only 2%-3%, *bill easy to understand* and *bill easy to read* had more noticeably declines (8% and 6%, respectively).



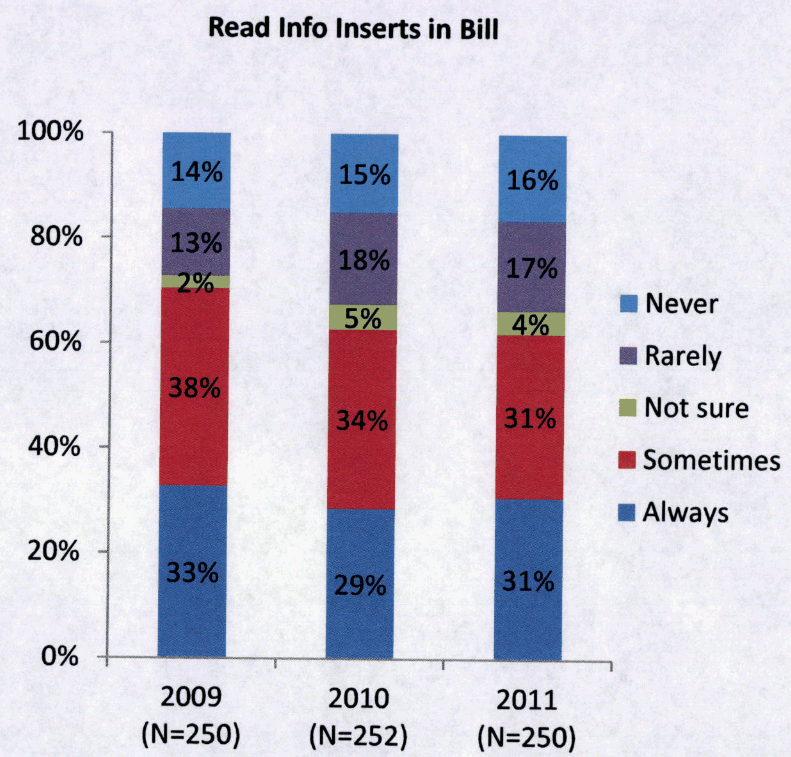
NOTE: Orange circled data indicates significant change/ difference compared to other year(s).

8a-d. Using a 5-point scale where 5 is Strongly Agree and 1 is Strongly Disagree, please tell me how much you agree or disagree with each of the following statements.

Customer Billing – Information/Services

Almost two thirds of respondents (62%) stated they read the information inserts in their bill *sometimes* or *always*. These results were relatively consistent with findings in 2010 (-1%), but nearly 9% lower than the 2009 level.

It should be noted that those more likely to always read such inserts are longer term residents (38% 6+ year residents).



Significantly Higher
Always: Residents 6 years or more (38%)

9. How often do you read the informational inserts included in your bill?

Customer Billings – Improvements

When asked about suggestions to improve customer billings, the majority of respondents did not have any improvements and felt it was fine as is (84%), which was on par with the 85% received in 2010. *Lower rates/don't increase rates* was mentioned by 6%.

Comments regarding *improve or implement electronic/online/paperless billing* continued its downward trend, down 2% compared to 2010 and down 13% compared to 2009. As noted in last years report, this is likely a reflection of changes and new services offered on the updated website.

Suggestions for Improvements	2009 (N=250)	2010 (N=252)	2011 (N=250)	Difference from 2010
Improve or implement electronic/online/paperless billing	15%	4%	2%	-2%
Lower rates/don't increase rates	3%	3%	6%	+3%
Make bill easier to understand	1%	3%	3%	0%
No suggestions/fine as is	74%	85%	84%	-1%

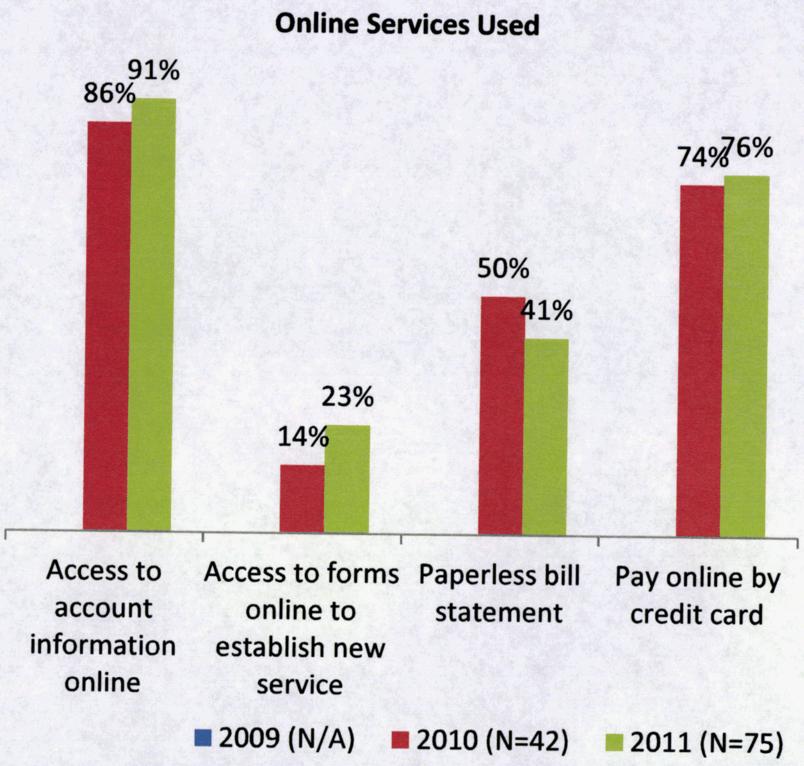
NOTE: Data in orange shaded cells are significantly higher; data in gray shaded cells are significantly lower: at 95% confidence level.

11. Do you have any suggestions for improving the billing?

Website – Online Services

Nearly a third (30%) of customers reported they had accessed the new Liberty Water website, which represented a 13% increase as compared to 2010.

The online services used by most was *access to account information* (91%) followed by *pay online by credit card* (76%). Usage by new customers may also be on the rise considering *access to forms online to establish new service* rose by 9% in 2011 (up to 23%).



NOTE: Orange circled data indicates significant change/ difference compared to other year(s).

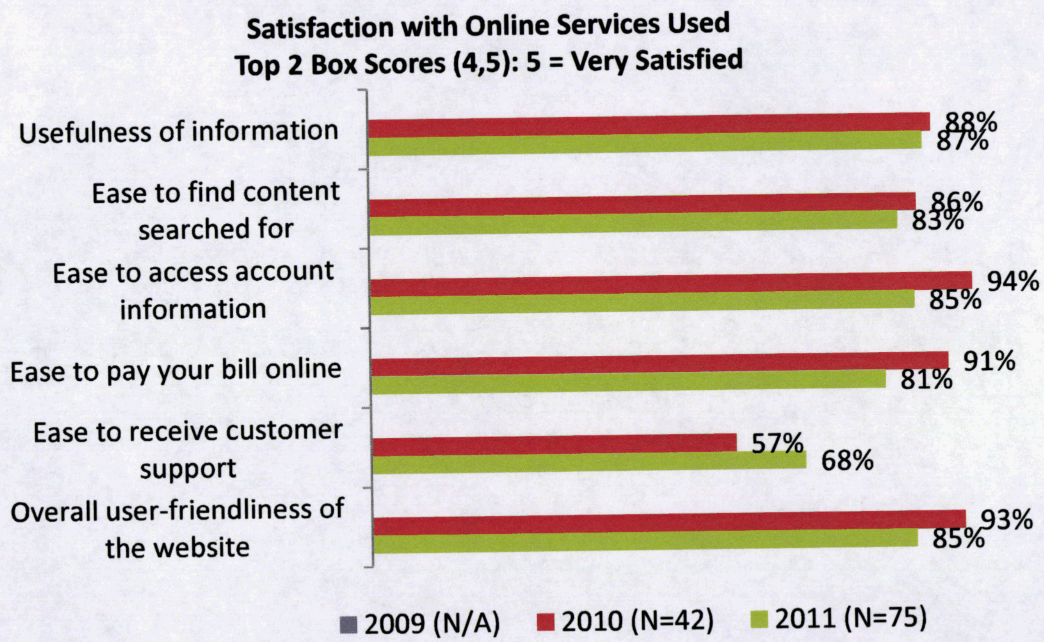
10N1. Have you accessed [INSERT FACILITY BASED ON QFAC]'s website?

*10N2. The following services are available to **[INSERT FACILITY BASED ON QFAC]** customers. Please tell me if you have used any of them?*

Satisfaction with Website – Online Services

Satisfaction with the online services customers had used was high. *Usefulness of information* received the highest satisfaction rating (87% very or somewhat satisfied) and had the smallest downturn (-1%). *Ease to access account information* and *overall user-friendliness of the website* each received scores of 85%, but both had 8% to 9% declines as compared to 2010. The only area that received relatively lower scores was *ease to receive customer support* (68%), but this was the only factor to show a positive trend (up 11%).

Not many customers had improvement suggestions for the website (85% had no suggestions and/or stated the site was fine as is). Those who had suggestions asked to *improve user interface/easier to navigate* and *add bank transfer as a payment option.*



Suggestions for improvements (N = 75)
13% Improve user interface/easier to navigate
85% No suggestions/fine as is

10a. Using a 5-point scale where 5 is Very Satisfied and 1 is Very Dissatisfied, please tell me how satisfied you are with the new [INSERT FACILITY BASED ON QFAC] website.

10b. Do you have any suggestions for improving [INSERT FACILITY BASED ON QFAC] website and/or online services?

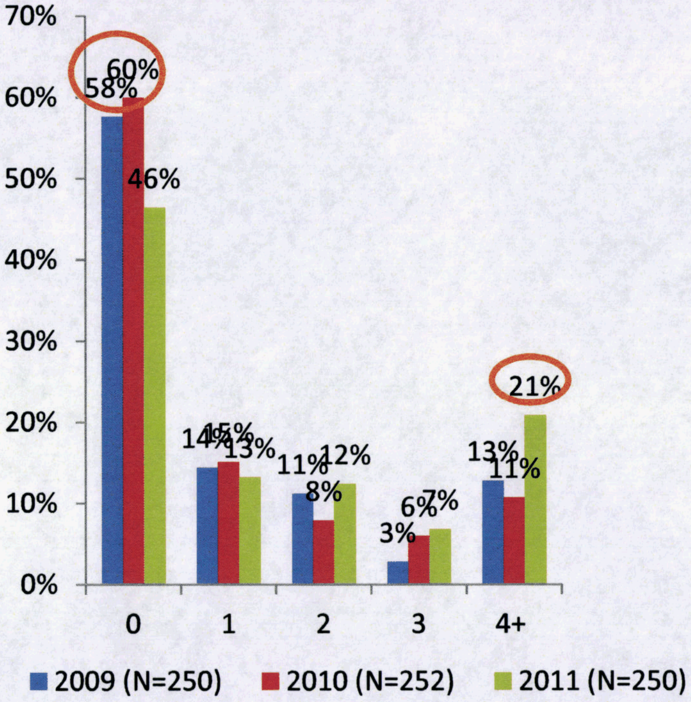
Customer Service – Calls & Visits

Nearly half of respondents did not call (46%) or visit (49%) the business office within the last year. However those with 1+ visits were significantly higher in 2011 (51% 1+ visits vs. 45% and 38% in previous years). Those who called or visited 4+ times showed the most dramatic increases (21% and 28%, up 10% each).

Respondents who had contacted the business office had both called or visited the office between two and three times, on average (2.77 calls and 2.57 visits).

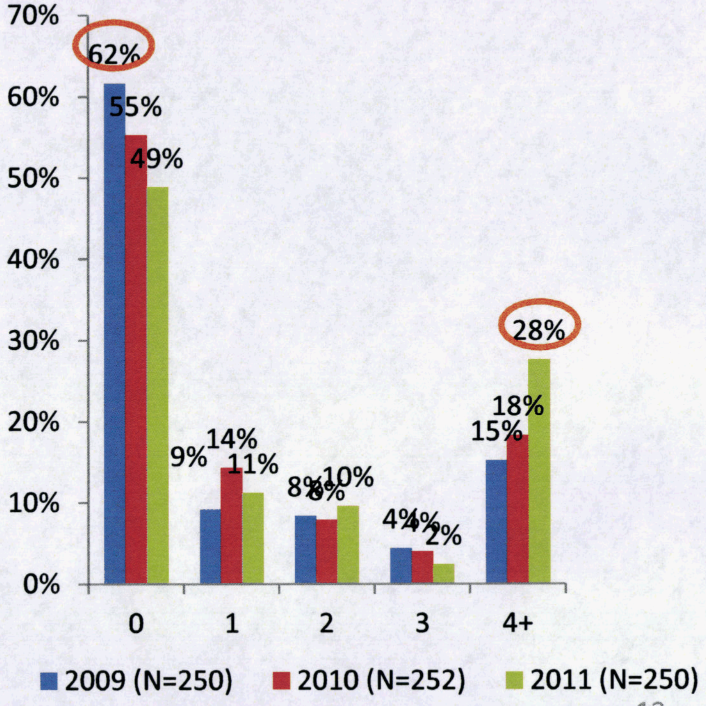
Times Called Business Office

Mean = 2.41 (2009); 2.40 (2010); 2.77 (2011); among those who have called within last year



Times Visited Business Office

Mean = 2.46 (2009); 2.44 (2010); 2.57 (2011); among those who have visited within last year

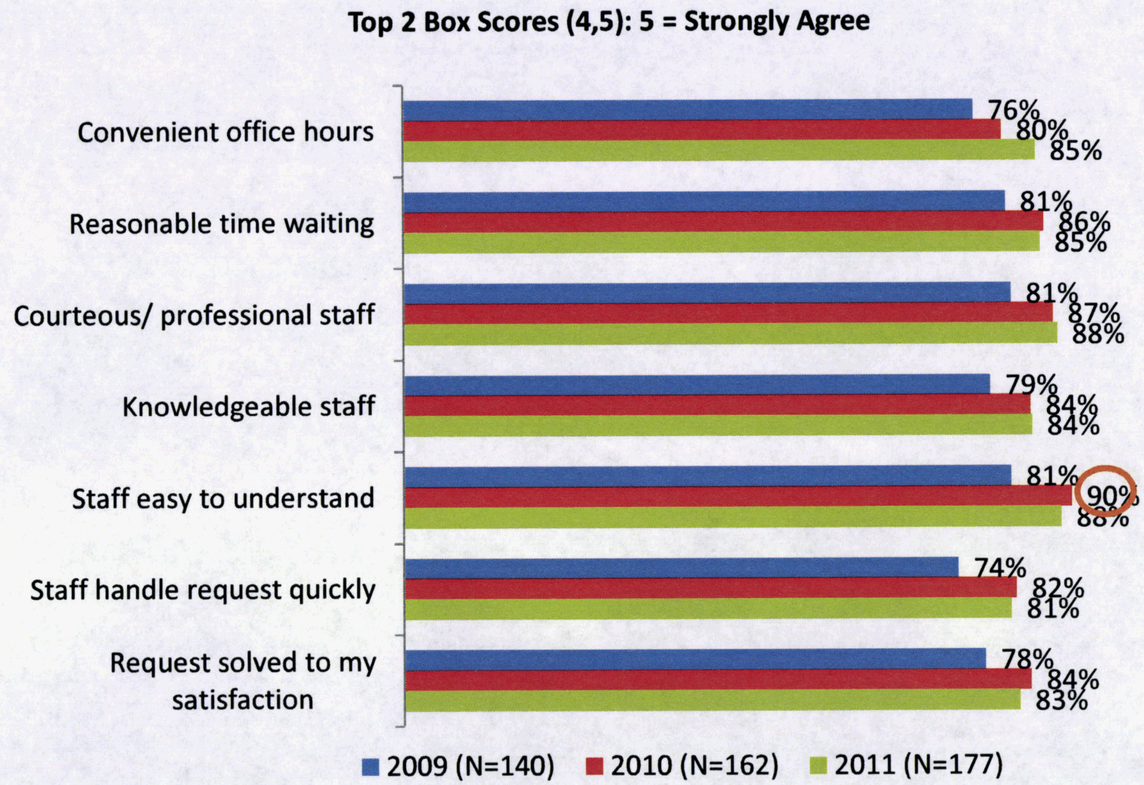


NOTE: Orange circled data indicates significant change/ difference compared to other year(s).

11b. To the best of your recollection, how many times have you called or visited the [INSERT FACILITY BASED ON ZIP CODE] business office within the last year?

Customer Service – Satisfaction

Among those customer who reported they had contact with customer service in the last year, satisfaction was strong and on par with 2010 across all aspects tested (within 2%). The one exception was *convenient office hours,* which showed a 5% increase in satisfaction as compared to 2010.



NOTE: Orange circled data indicates significant change/ difference compared to other year(s).

12a. Using a 5-point scale where 5 is Strongly Agree and 1 is Strongly Disagree, please tell me how much you agree or disagree with each of the following statements about [INSERT FACILITY BASED ON ZIP CODE]'s customer service. If you have called or visited the office more than once in the last year, please think only about your last contact with the [INSERT FACILITY BASED ON ZIP CODE] business office.

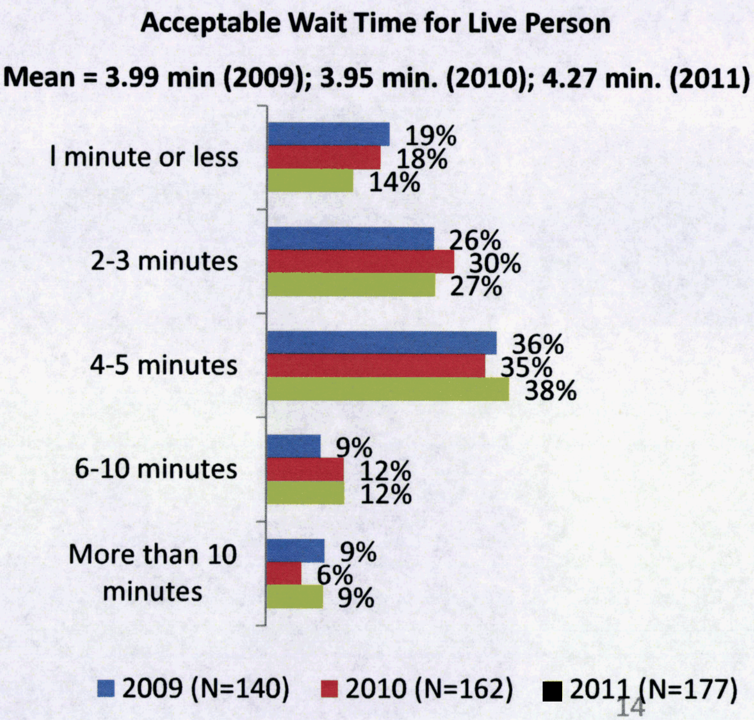
Customer Service – Hours & Wait Time

Customers who did not agree strongly that the office hours were convenient were asked what they felt would be more convenient hours. Longer weekday hours (26%) was the most preferred hours extension option.

On average, respondents reported that an acceptable wait time for a live person was just over four minutes (mean of 4.27 minutes), a slight increase from 2010 (3.95 minutes). With 79% of respondents feeling an acceptable wait time is no more than five minutes, Liberty Water should strive to keep wait times below this mark.

More Convenient Time	2009 (N=79)	2010 (N=83)	2011 (N=77)	Difference from 2010
Weekday hours: late open/past 5PM	32%	39%	26%	-13%
Saturday hours: half/full day	15%	10%	9%	-1%
Weekday hours: early open/before 8AM	8%	6%	4%	-2%
Office hours are fine	23%	21%	21%	0%

NOTE: Data in orange shaded cells are significantly higher; data in gray shaded cells are significantly lower: at 95% confidence level.

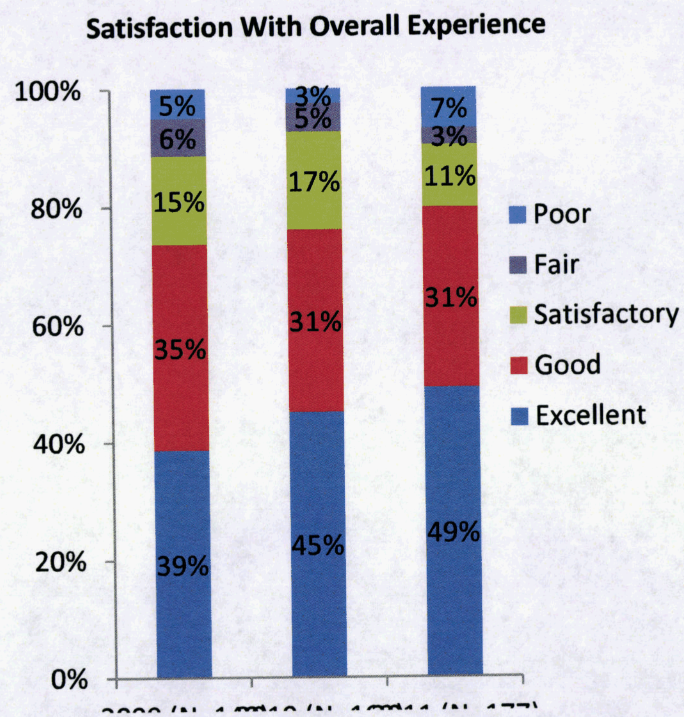


12b. What would you consider more convenient office hours?
12c. How long are you willing to wait to speak to a live person?

Customer Services – Overall Experience

More than three fourths of respondents were satisfied with their overall customer service experience (80% excellent/good), which continued its upward trend (up 4% from 2010 and up 6% from 2009).

Respondents had few suggestions on how to improve customer service; 88% had no suggestion (up 5% from 2010). The few comments given centered around being more polite and professional.



Suggestions for Improvements	2009 (n=140)	2010 (N=162)	2011 (n=177)	Difference from 2010
Be more professional/ knowledgeable	6%	3%	2%	-1%
Be more polite/ friendly/understanding	6%	3%	3%	0%
Improve communication w/customer	1%	3%	1%	-2%
Speak English better/as a default language	1%	3%	1%	-2%
No suggestions/fine as is	79%	83%	88%	+5%

NOTE: Data in orange shaded cells are significantly higher; data in gray shaded cells are significantly lower: at 95% confidence level.

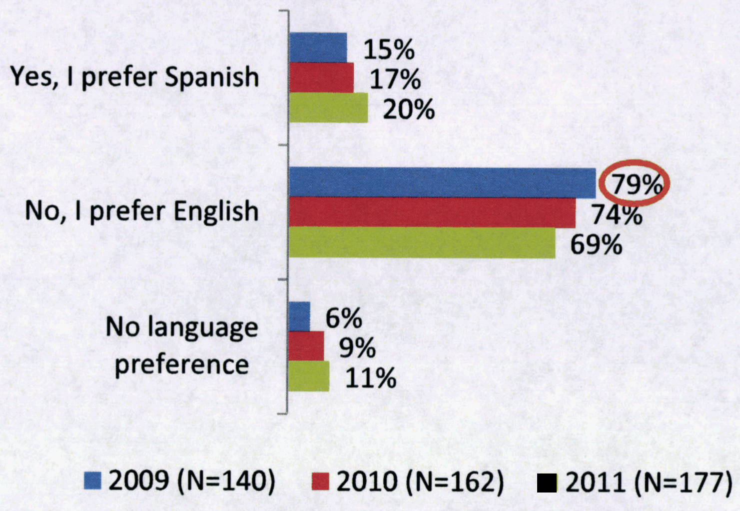
13. Overall, how would you rate your experience with the customer service you received? If you have called or visited the office more than once in the last year, please think only about your last contact with the [INSERT FACILITY BASED ON ZIP CODE] business office.

14. Do you have any suggestions for improving customer service?

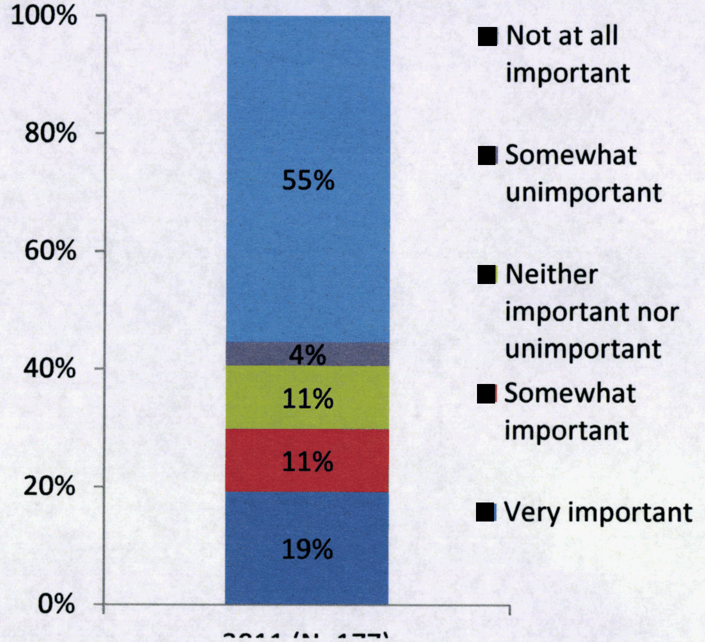
Customer Services – Spanish

Respondents continued to show a slight rise in preference for customer service in Spanish with one in five (20%, up 3%) now preferring it over English. The Rio Rico respondents showed a significantly higher interest in Spanish customer service (33%).

Nearly a third (30%) felt a Spanish website was somewhat or very important.



Significantly Higher
Prefer Spanish: Rio Rico (33%)

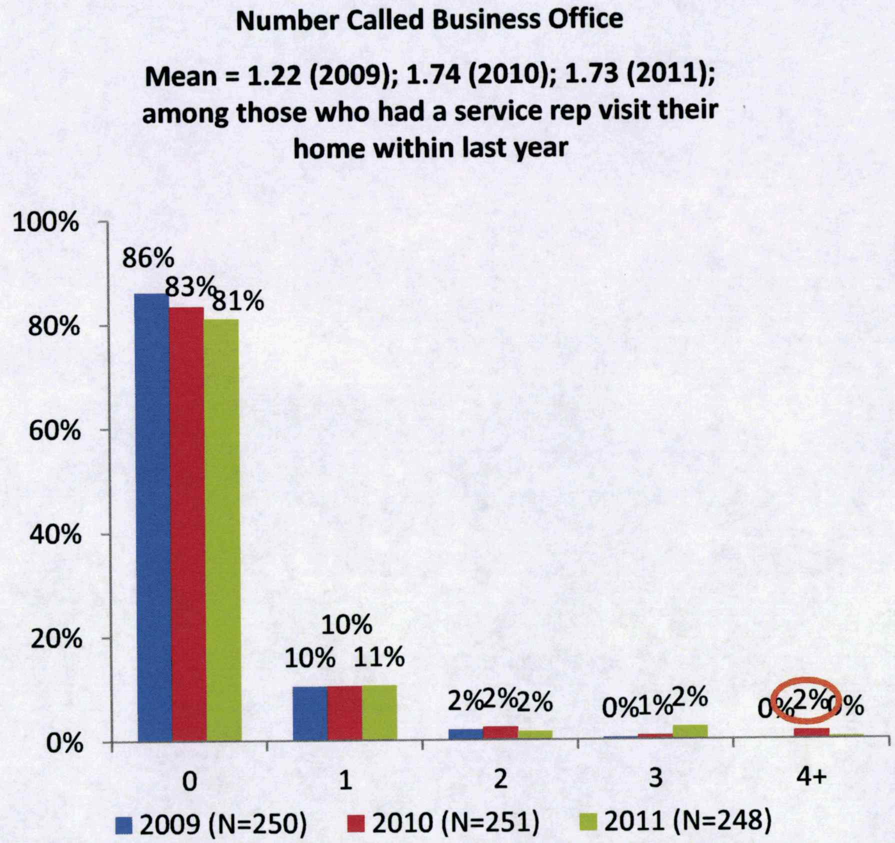


NOTE: Orange circled data indicates significant change/ difference compared to other year(s).

13a. If customer service were available in Spanish would you take advantage of it?
Q13b. How important is it to you that Liberty Water's website is available in Spanish language?

Service Rep Home Visits

Most respondents had no service representative visit their home within the last year (81% none). Of those who had a representative visit, the average number of visits was 1.73 which was on par with 2010 (1.74 visits).



NOTE: Orange circled data indicates significant change/ difference compared to other year(s).

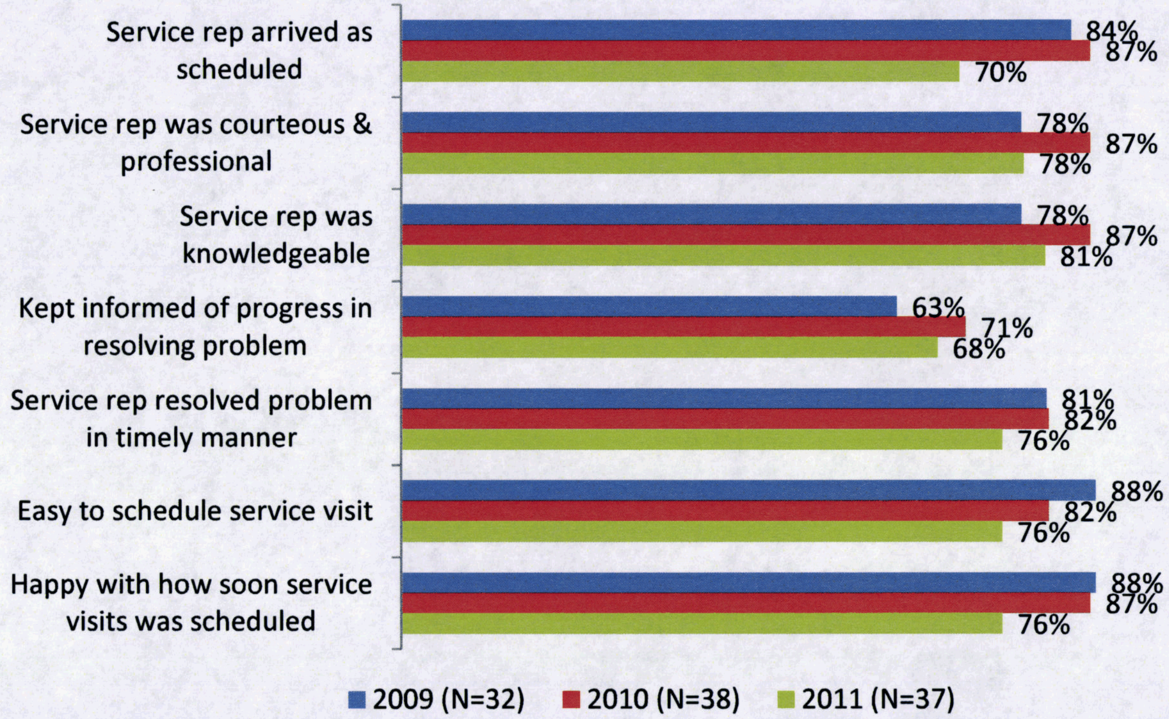
14b. How many times has an [INSERT FACILITY BASED ON ZIP CODE] employee visited your home to resolve a problem within the last year?

Service Rep Home Visits – Satisfaction

While satisfaction with service representative home visits was still strong, 2011 levels were lower for all factors tested. While some decreases were small (as low as 3%), *service rep arrived when scheduled* saw the largest decline in satisfaction (-17%, down to 70%). This placed it as the second worst in satisfaction behind *kept informed of progress in resolving problem* (68%).

Service rep knowledgeable received the highest satisfaction score (81%).

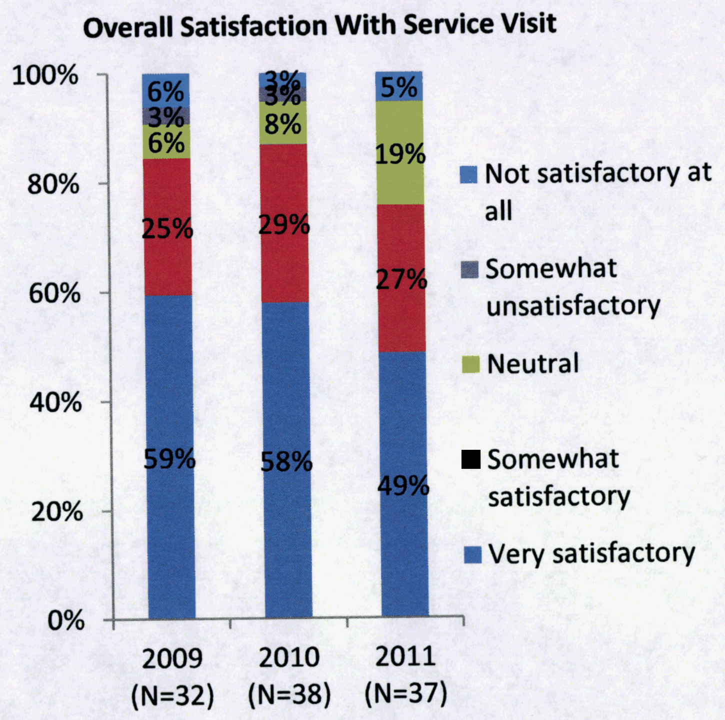
Top 2 Box Scores (4,5): 5 = Strongly Agree



15. Using a 5-point scale where 5 is Strongly Agree and 1 is Strongly Disagree, please tell me how much you agree or disagree with each of the following statements about your in home service visit. If an [INSERT FACILITY BASED ON ZIP CODE] employee has visited your home more than once within the last year, please think only about your last visit.

Service Rep Home Visits – Overall Satisfaction & Improvements

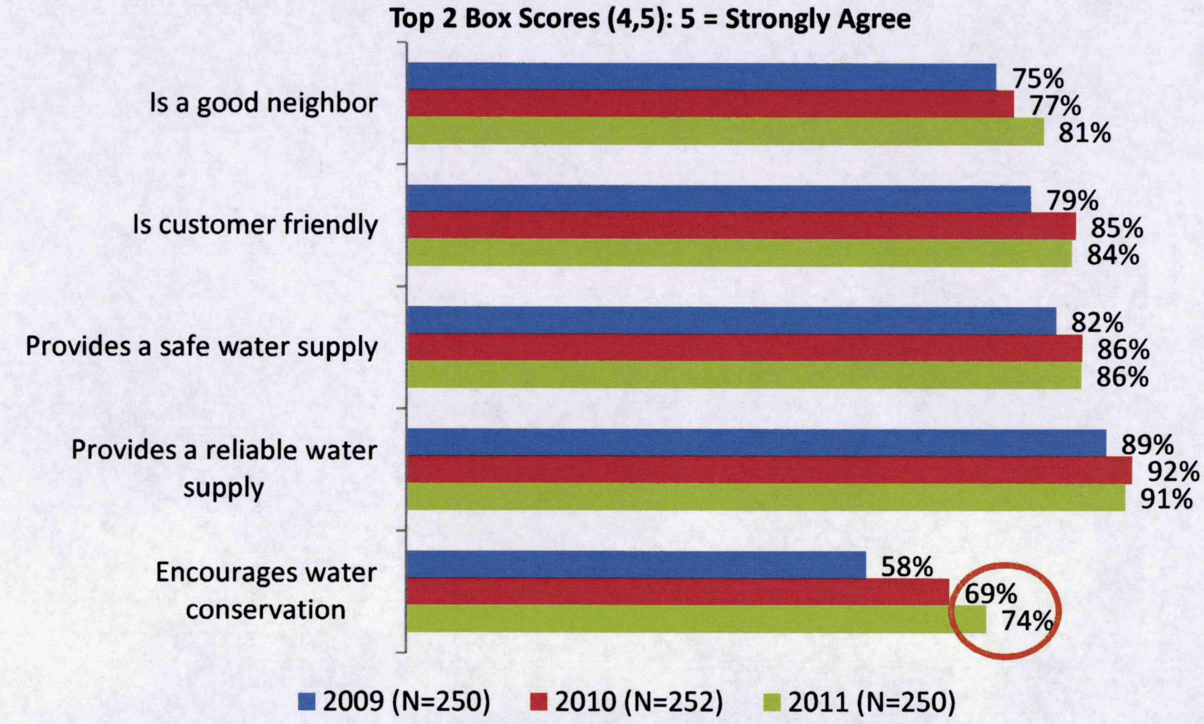
Overall satisfaction with the service rep home visit fell noticeably in 2011; three fourths (76%) of respondents indicated they were somewhat/very satisfied which was a decrease of 11% as compared to 2010.



16. Overall, how would you rate your experience with the service visit to your home using a 5-point scale with 5 being "Very Satisfactory" and 1 being "Not Satisfactory At All"? If you had more than one visit in the last year, please think only about your last visit.

Company Evaluation – Satisfaction

Respondents agreed that their water service facility provides a *reliable water supply* (91%, top 2 box agree/strongly agree) followed by *provides a safe water supply* (86%). While all agreement scores were relatively consistent with or up from 2010, *encourages water conservation* was significantly higher at 74% compared to 69% in 2010 and 58% in 2009.



Significantly Higher
Provides a safe water supply: At residence less than 5 years (91%)
Encourages water conservation: Belle Vista (81%)

NOTE: Orange circled data indicates significant change/ difference compared to other year(s).

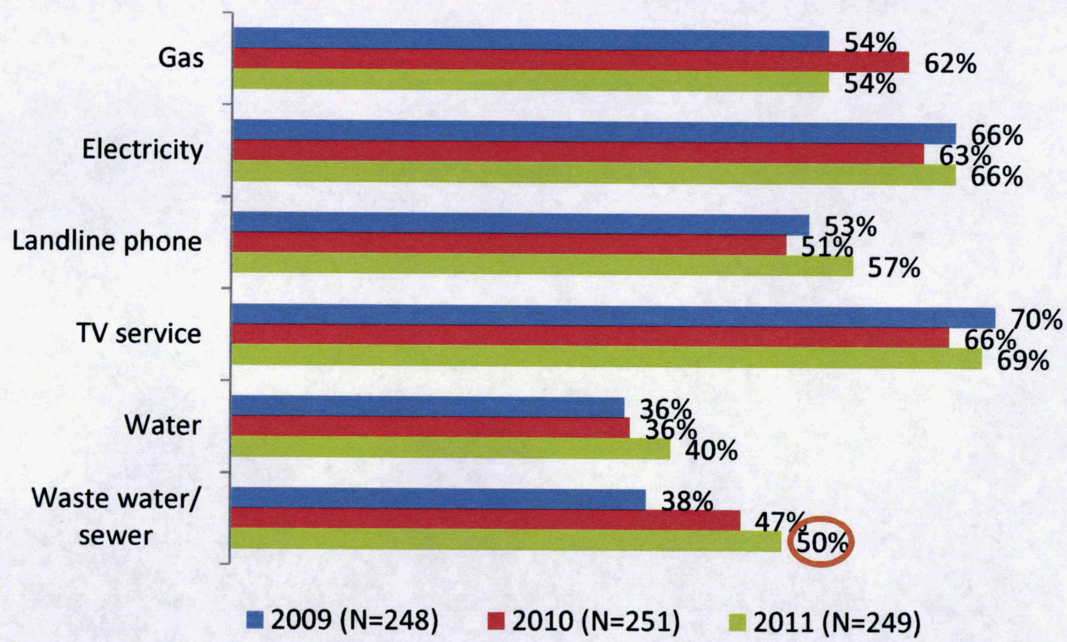
18. Using a 5-point scale where 5 is Strongly Agree and 1 is Strongly Disagree, please tell me how much you agree or disagree with each of the following statements about [INSERT FACILITY BASED ON ZIP CODE].

Company Evaluation – Utility Rates

When comparing the perception of pricing for different utilities and services that respondents received, those considered somewhat/much too high were *television* (69%), *electricity* (66%) and *landline phone* (57%).

Water and *waste water/sewer* actually had the lowest "too high" scores (40% and 50% respectively). However, both received scores that were 3% to 4% higher as compared to 2010 data.

Top 2 Box Scores (4,5): 5 = Much too High



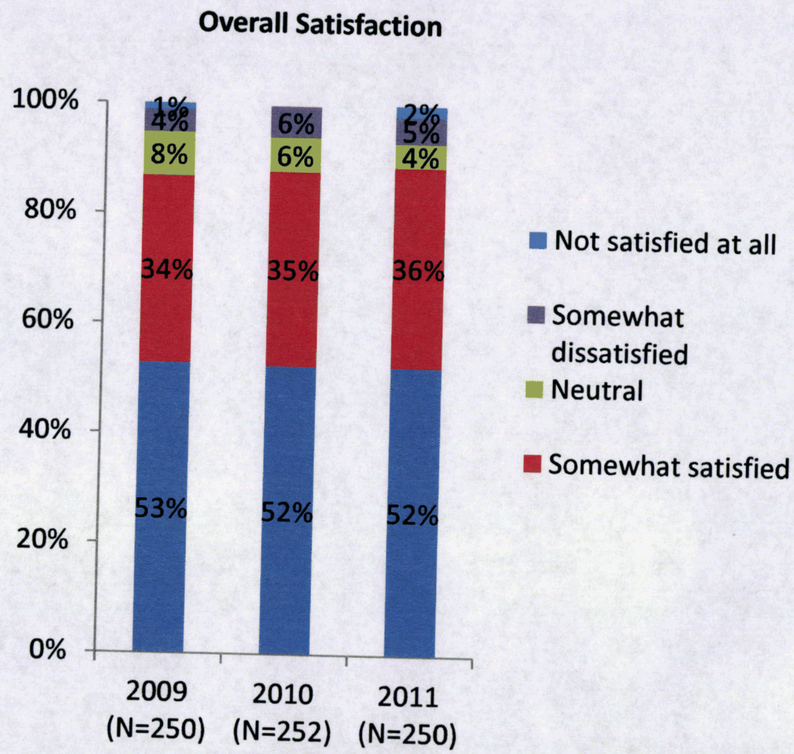
NOTE: Orange circled data indicates significant change/ difference compared to other year(s).

19. For each of the following utility services, please indicate if you feel the rates charged are much too high, somewhat too high, just right, somewhat low, or very low.

Company Evaluation – Overall Satisfaction

Respondents were satisfied with their water/waste water provider overall, with 88% of respondents stating they were somewhat/very satisfied (up 1% from 2010).

Those with significantly higher very satisfied scores were from Belle Vista (69% vs. 52% overall), 18-44 year olds (66%) and residents less than 5 years (64%).



Significantly Higher
Very satisfied: Belle Vista (69%); Ages 18-44 (66%); Residents less than 5 years (64%)

20. Overall, how satisfied are you with [INSERT FACILITY BASED ON ZIP CODE]?

Company Evaluation – Overall Satisfaction

Those somewhat/very satisfied with the provider were so because they *never had a problem/complaint* (32%). However, 14% of those satisfied still felt the *cost is too high/rate increases*.

Not surprisingly, *cost is too high/rate increases* (59%) was the main reason why respondents were dissatisfied (not satisfied at all/somewhat dissatisfied). Of even more importance is the fact *cost* as a factor rose by 19% as compared to 2010 data. *Poor/unfriendly/uncaring service* was also an important reason for dissatisfaction (24%; up 11% from 2010).

Suggestions for Improvements	2009 (n=250)	2010 (n=252)	2011 (n=250)	Difference from 2010
Why Satisfied	N=217	N=221	N=222	
Reliable/No service interruptions	17%	10%	9%	-1%
Never had a problem/complaint	18%	34%	32%	-2%
Cost is reasonable	14%	5%	6%	+1%
Good/friendly/courteous customer service	14%	9%	9%	0%
Service is satisfactory/good/excellent	11%	13%	8%	-5%
Water quality is good	11%	4%	4%	0%
Cost is too high/rate increases	10%	14%	14%	0%
Why Not Satisfied	N=13*	N=15*	N=17*	
Cost is too high/rate increases	23%	40%	59%	+19%
Poor/unfriendly/uncaring customer service	15%	13%	24%	+11%
Water is cloudy/contaminated/poor quality/hard	15%	7%	12%	+5%
Low/Fluctuating water pressure	8%	7%	6%	-1%
Smell/taste of water	8%	7%	0%	-7%

NOTE: Data in orange shaded cells are significantly higher; data in gray shaded cells are significantly lower: at 95% confidence level.

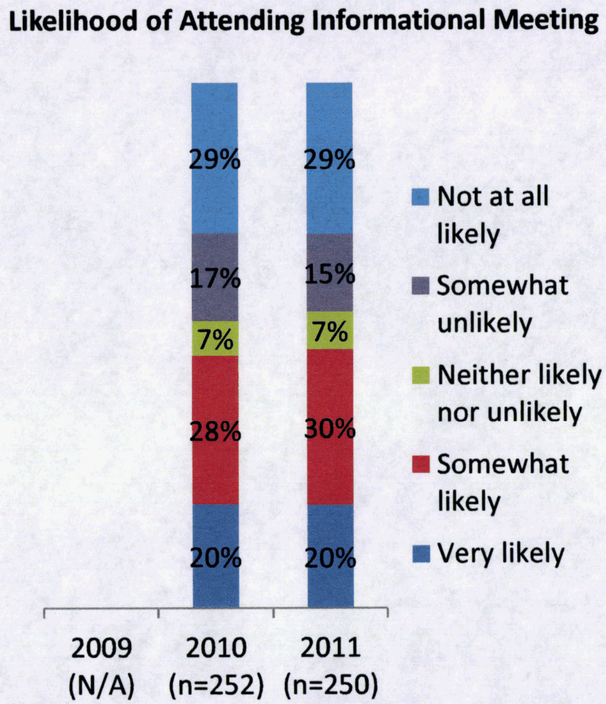
**Caution: small sample size.*

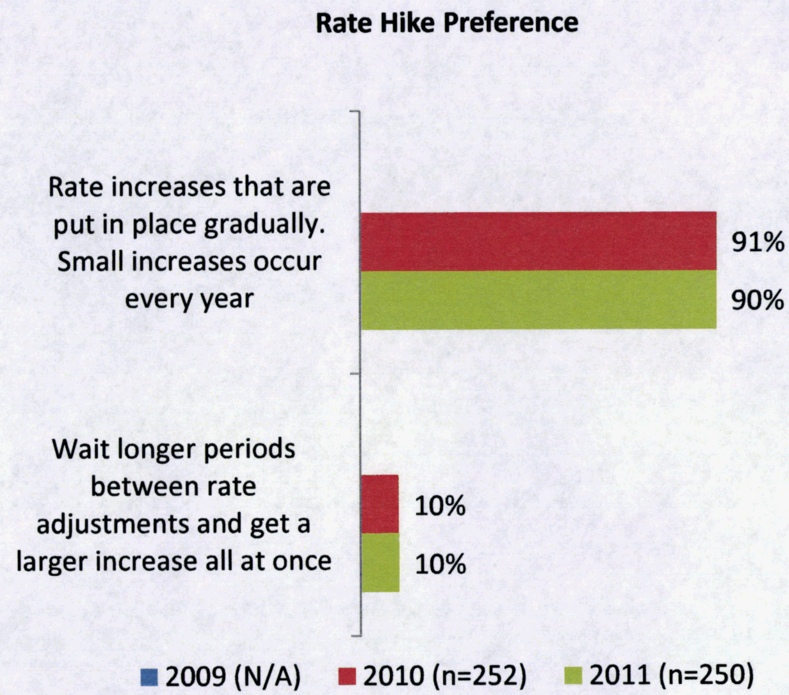
20a. Being as specific as possible, why did you say you are [INSERT FROM Q20] with [INSERT FACILITY BASED ON ZIP CODE]?

Rate Hikes

In terms of customer involvement in potential rate hikes, half (50%) stated they were very or somewhat likely to attend an informational meeting.

In case of rate increases, the vast majority (91%) preferred having the increases spread out over time with small increases occurring every year.





21a. If rate case informational meetings were held in your community how likely would it be that you would attend?

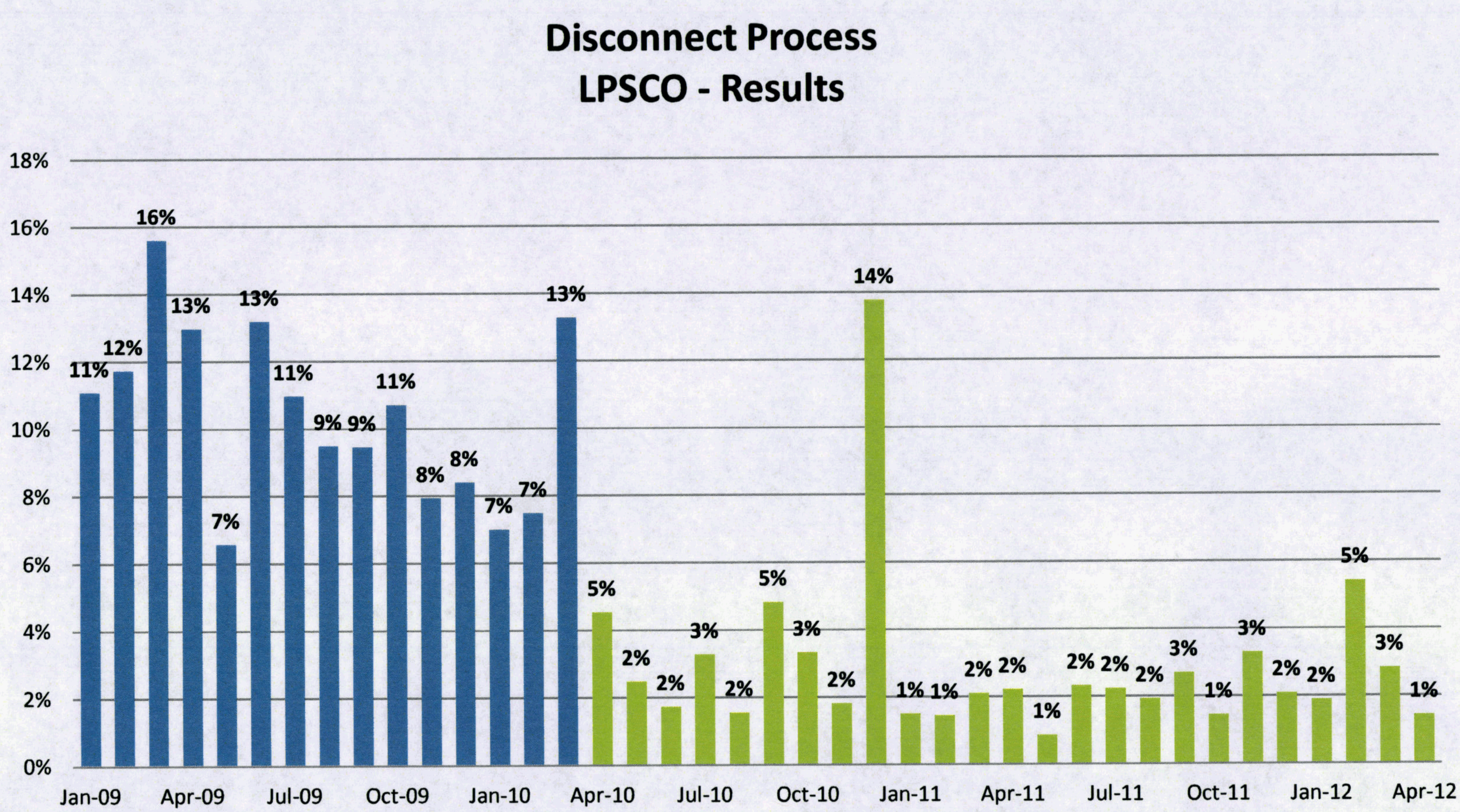
21c. Regarding rate increases, given the opportunity would you prefer:

Rio Rico Utilities, Inc.
2012 Rate Application

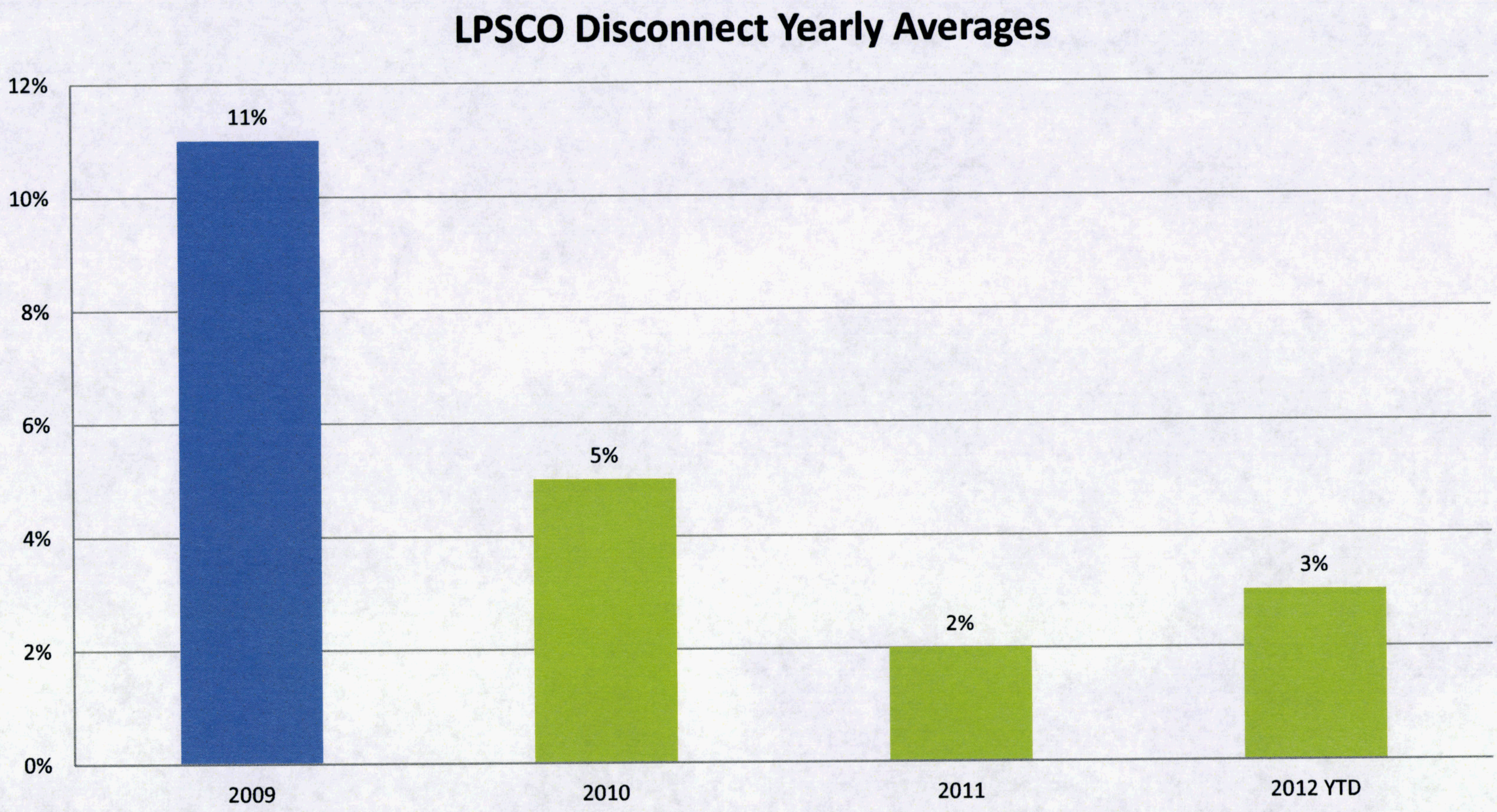
Greg Sorensen Direct Testimony

Exhibit GS-DT3

Pilot Disconnect Process - LPSCO



LPSCO Annual Disconnect %

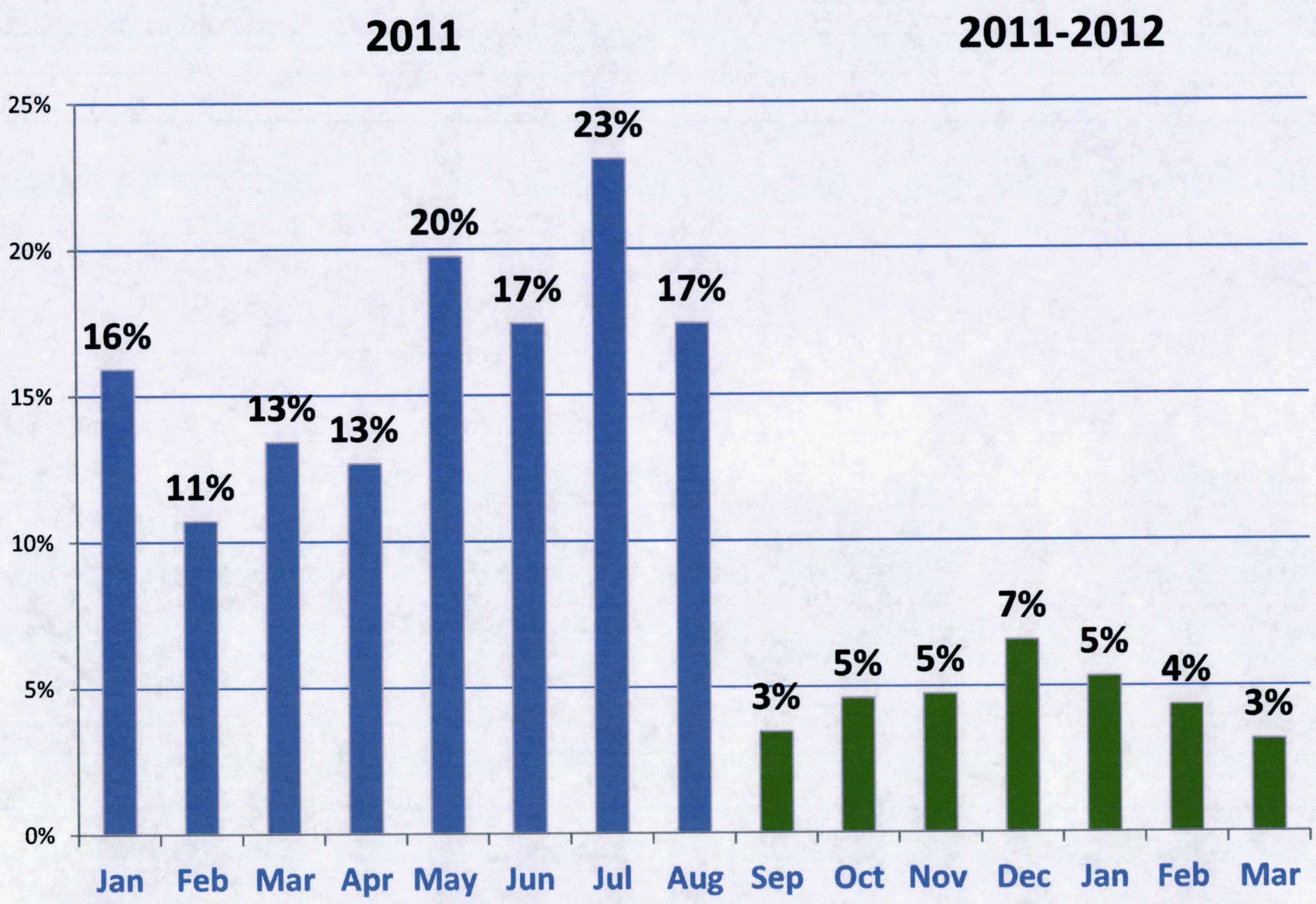


Rio Rico Utilities, Inc.
2012 Rate Application

Greg Sorensen Direct Testimony

Exhibit GS-DT4

RRUI Disconnect Process



- Liberty Water – Rio Rico
- Services Disconnected as percentage of Disconnect Notices Mailed.
- August 2011 – Starting making phone calls and leaving door tags.

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BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF RIO RICO UTILITIES, INC., AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANTS AND PROPERTY AND FOR INCREASES IN ITS WATER AND WASTEWATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.	DOCKET NO: WS-02676A-12-0196

REBUTTAL TESTIMONY OF

GREG SORENSEN

January 28, 2013

EXHIBIT
A-8
ADMITTED

Table of Contents

7887976.1/080191.0012

I. INTRODUCTION AND PURPOSE OF TESTIMONY

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Greg Sorensen. My business address is 12725 W. Indian School Road, Suite D-101, Avondale, AZ 85392.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?

A. On behalf of the Applicant, Rio Rico Utilities, Inc. ("RRUI" or "Company").

Q. BY WHOM ARE YOU EMPLOYED?

A. I am employed by Liberty Utilities ("Liberty") as Vice President and General Manager.

Q. DID YOU PREVIOUSLY PROVIDE TESTIMONY ON BEHALF OF THE COMPANY IN THIS CASE?

A. Yes, my direct testimony was filed on May 31, 2012, with the Company's application.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. To further support RRUI's application for rate relief by responding to testimony by the other parties regarding RRUI's policies on bonuses, merit pay, and benefits.

II. SECTION 1 – MERIT PAY DISALLOWANCE (RUCO ADJUSTMENT 12 FOR WATER AND SEWER)

Q. WHAT DID MR. COLEY PROPOSE?

A. Mr. Coley proposed disallowing 50% of the costs associated with the annual merit wage increase.

Q. ON WHAT GROUNDS DID MR. COLEY PROPOSE THE DISALLOWANCE?

A. Mr. Coley listed two main reasons – lack of certain reoccurrence and insufficient sharing with shareholders.

Regarding the first, I believe Mr. Coley may have misunderstood the nature of these merit pay expenses so I will try to provide further explanation. Each year, base salary compensation is reviewed for each employee. That base salary compensation may or may not be adjusted. The components of that adjustment include where that employee's pay rests within their job pay scale range, as well as how they performed in the prior year. The combination of these two items leads to an increase in the employee's base wage (hourly or salaried). This "merit increase" actually becomes the employee's new base wage for that following year.

Concerning Mr. Coley's second point, this is not an achievement or incentive pay program. This is simply a way to arrive at what hourly or annual pay rate the employee will be paid during the coming year. There is nothing here to "share" with shareholders.

Q. ARE MERIT PAY INCREASES AN IMPORTANT RECRUITING TOOL?

A. Yes. We want to hire and retain qualified and productive employees. Also, in general, employees believe that if they work hard and produce well during a given year, they will be paid more in the subsequent year. This is because they will have another year of experience and skill that they bring to their employer, and in turn the customers, and the value of that experience, skill and production should be recognized through increased compensation. Liberty's management agrees and employee performance is reviewed each year and pay adjusted the following year, where appropriate. Without such increases, employees have far less incentive to continue to maintain production levels or to improve performance or will look for an employer that rewards such efforts. This is a basic job market concept.

Q. MR. SORENSEN, IS THIS SALARY COST RECURRING ON A GOING FORWARD BASIS?

A. Once granted, the merit adjustment becomes part of an employee's recurring pay, paid on a bi-weekly basis. Granted, no level of pay is guaranteed. An employer may lower wages as well as raise them for an employee. However, I am not aware of any downward adjustments to employee pay since the end of the test year. Of course, in that way it is like any other expense – there is no certainty we will incur any test year expense in the exact same amount in the future.

Q. MR. SORENSEN, HAS RRUI / LIBERTY HISTORICALLY PAID MERIT INCREASES?

A. Yes.

Q. WHEN WERE THE MERIT INCREASES EFFECTIVE?

A. Merit increases were given to employees in late March 2012, but were retroactive to January 1, 2012, which was during the test year.

Q. AND THERE IS NO "AT RISK" ASPECT?

A. No, they become part of the recurring daily, weekly, monthly, annual pay rate of the employee.

Q. SINCE THE END OF THE TEST YEAR HAS RRUI / LIBERTY MAINTAINED THE SAME LEVEL OF EXPENSE?

A. Yes.

III. SECTION 2 – INCENTIVE PAY (BONUSES) (RUCO ADJUSTMENT 11 FOR WATER AND SEWER)

Q. WHAT DID MR. COLEY PROPOSE AND ON WHAT GROUNDS?

A. Mr. Coley proposed disallowing 50% of the costs associated with the incentive pay increase. His reasoning is the same as with the merit pay program I discussed in the prior section of my rebuttal testimony.

First, this was in fact a cost that was incurred during the test year. A similar cost was incurred in the year before and after the test year. As such, Mr. Coley's speculation that this is not a recurring cost is, in this case, inaccurate. As I further point out above, every test year expense is at risk for not matching the expense during a given future year. But bonuses were paid. This is because Liberty strives to maintain a consistently high level of service and, when achieved, will yield a consistent level of incentive pay. Post test year, we have continued providing high quality service, and we expect to pay incentives for the calendar year 2012 performance similar to those paid for 2011, which comprises the majority of the test year. I know of no known or measurable change to this test year cost.

Concerning Mr. Coley's sharing argument, the incentive program costs were incurred as a cost of service during this test year. These incentives were paid and were related to the results of the test year. The service provided to our customers was actually received by them during the test year. This is a cost of service and costs of service, if reasonable and prudent, are not shared by the shareholder.

Q. **WHY ARE BONUS PAYMENTS AN IMPORTANT RECRUITING AND RETENTION TOOL?**

A. Bonuses or incentive programs are just a part of an employee's overall or total compensation. This total compensation has to be market competitive or, all other things being equal, employees will leave for what they perceive to be a better paying job. This will then lead to higher turnover for the utility and a degradation of service to the customer. A similar concept applies to recruiting new employees to come to work at Liberty. When a candidate is considering coming to work here, one of the primary considerations they make is the compensation and benefits package. We have to design our pay and benefits packages to be market competitive.

Q. MR. SORENSEN, IS THIS COST RECURRING ON A GOING FORWARD BASIS?

A. Yes it is.

Q. HAS RRUI / LIBERTY HISTORICALLY PAID BONUSES?

A. Yes, we have paid annual bonuses for at least as long as I've been here.

Q. SINCE THE END OF THE TEST YEAR HAS RRUI / LIBERTY MAINTAINED THE SAME LEVEL OF EXPENSE?

A. Yes, as previously indicated, we have maintained the same or slightly higher level of expected incentive expense.

Q. BUT DON'T THE BENEFITS THAT LEAD TO BONUSES ACCRUE TO THE SHAREHOLDER FAR MORE THAN THE RATEPAYERS?

A. Absolutely not. Liberty's incentives are based on metrics such as Customer Experience, Employee programs, Operational Excellence, Safety, Efficiency, and personal performance. These areas of measurement significantly benefit the customers and community in general. For example, one measure of Customer Experience is the result of our annual customer satisfaction survey. Our employees are incented to maintain or increase customer satisfaction each and every day.

IV. SECTION 3 – ANNUAL REVISED BENEFITS PLAN ADJUSTMENT

Q. MR. BOURASSA PROPOSES A PRO FORMA ADJUSTMENT TO REFLECT INCREASED EMPLOYEE BENEFIT COSTS.[1] WHAT CHANGED?

A. A change in the benefits program was made by RRUI's parent company, Liberty, and we were made aware of the impact on RRUI.

---

[1] Rebuttal Adjustment No. 9 (water) and Rebuttal Adjustment No. 10 (wastewater). *See* Rebuttal Testimony of Thomas J. Bourassa – Rate Base, Income Statement and Rate Design at 32, 44.

Q. **BUT WHY DID THE COMPANY WAIT UNTIL REBUTTAL TO MAKE THE ADJUSTMENT?**

A. Because we were just informed of the change in expenses in final quarter of 2012, after the filing date of the rate application.

Q. **WERE EMPLOYEE BENEFITS COSTS INCURRED DURING THE TEST YEAR?**

A. Yes, this is just an update of the employee benefit package costs.

Q. **IS THE AMOUNT OF THE ADJUSTMENT KNOWN AND MEASUREABLE?**

A. Yes, the Company knows the amount of the change and quantifies that in the adjustment proposed by Mr. Bourassa.

Q. **WILL THIS EXPENSE OCCUR ON A GOING FORWARD BASIS?**

A. Yes.

Q. **ARE BENEFITS COSTS A NORMAL COST OF SERVICE REQUEST BY RRUI, LIBERTY AND OTHER RATE REGULATED UTILITIES?**

A. Yes. As I explained above, attracting and retaining talented employees is critical to the success of all companies and a benefits package is an important tool in attracting and retaining employees.

Q. **ARE THESE COSTS SPECIFIC TO RRUI OR LIBERTY EMPLOYEES?**

A. Yes. Approximately 75% of the adjustment relates to employees directly working in RRUI. The remaining 25% relates to employees based in our Avondale office that provide administrative support to RRUI, myself as an example.

Q. **OKAY, SO WHY DID THE EXPENSES INCREASE, MR. SORENSEN?**

A. As Liberty expands its national footprint by acquiring other companies, it continues to evaluate how compensation and benefits are set on a national level. After the latest round of acquisitions, Liberty hired a benefits consultant to help standardize the national benefits plan across all United States water, sewer, gas and electric utilities. After the analysis was performed by the consultant, Liberty implemented the changes to take effect, and employees were notified of this benefits change late last year.

Q. HOW DOES THIS EXPENSE BENEFIT CUSTOMERS?

A. In the long-run it is more cost efficient for customers to have Liberty administer one standard national plan than numerous smaller different plans.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.

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BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF RIO RICO UTILITIES, INC., AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANTS AND PROPERTY AND FOR INCREASES IN ITS WATER AND WASTEWATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.	DOCKET NO: WS-02676A-12-0196

REJOINDER TESTIMONY OF

GREG SORENSEN

March 8, 2013

EXHIBIT
A-9
ADMITTED

Table of Contents

7984559.2/080191.0012

I. INTRODUCTION AND PURPOSE OF TESTIMONY

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Greg Sorensen. My business address is 12725 W. Indian School Road, Suite D-101, Avondale, AZ 85392.

Q. DID YOU PREVIOUSLY PROVIDE TESTIMONY ON BEHALF OF RIO RICO UTILITIES IN THIS CASE?

A. Yes, my direct testimony was filed on May 31, 2012 with Rio Rico Utilities ("RRUI" or the "Company") application, and my rebuttal testimony was filed on January 28, 2013.

Q. WHAT IS THE PURPOSE OF YOUR REJOINDER TESTIMONY IN THIS PROCEEDING?

A. To further support RRUI's application for rate relief by responding to testimony by Staff and RUCO regarding merit pay, incentive pay, and employee benefits.

II. MERIT PAY (RUCO OPERATING INCOME ADJUSTMENT NO. 12)

Q. WHAT IS "MERIT PAY", MR. SORENSEN?

A. Liberty's merit pay is annual wage adjustment given based an employee's performance and current pay within a given salary range. This adjustment is reflected in employee's paychecks they receive on a bi-weekly basis.

Q. DID YOU RESPOND TO MR. COLEY'S OPERATING INCOME ADJUSTMENT NO. 12 RELATED TO MERIT PAY IN YOUR REBUTTAL TESTIMONY?

A. Yes, I did.

Q. DID MR. COLEY MAKE ANY ADJUSTMENT IN HIS SURREBUTTAL TESTIMONY RELATED TO MERIT PAY?

A. Mr. Coley removed RUCO Operating Income Adjustment No. 12 from his schedules.[1]

Q. DID STAFF MAKE ANY ADJUSTMENT RELATED TO MERIT PAY IN ITS DIRECT OR SURREBUTTAL?

A. No, Staff did not. I believe all parties are in agreement on this matter now.

III. <u>INCENTIVE PAY (RUCO OPERATING INCOME ADJUSTMENT NO. 11)</u>

Q. HOW DOES INCENTIVE PAY DIFFER FROM MERIT PAY?

A. Liberty incentive pay is compensation based on company targets and individual performance. Incentive pay is an annual one-time payment made to the employee.

Q. MR. SORENSEN, DID YOU REVIEW RUCO'S SURREBUTTAL TESTIMONY REGARDING INCENTIVE PAY?

A. Yes, I did.

Q. DID RUCO MAKE ANY NEW OR ADDITIONAL ARGUMENTS IN SURREBUTAL TESTIMONY?

A. No.

Q. DID STAFF MAKE ANY ADJUSTMENT RELATED TO INCENTIVE PAY, EITHER IN DIRECT OR SURREBUTTAL, OR ADDRESS ANY OF THE POINTS MADE IN YOUR REBUTTAL TESTIMONY?

A. No.

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[1] Surrebuttal Testimony of Timothy J. Coley at 23:12-16.

Q. DID RUCO REFUTE ANY OF THE ARGUMENTS MADE IN REBUTTAL REGARDING INCENTIVE PAY?

A. No. RUCO did not dispute that the cost was incurred during the test year.[2] My testimony establishes that the cost is known, measurable, and was incurred during the test year. Additionally, I addressed that incentive pay of a similar level occurred in previous years and is anticipated to recur in the future.[3] This cost of a recurring nature is established as a cost of service expense that will continue to exist on a going-forward basis for ratemaking purposes. Finally, RUCO did not refute that Liberty's incentives are reasonable and prudent expenses because the incentives are based on metrics such as Customer Experience, Employee Programs, and Operational and Health and Safety measures. These incentive bases provide benefits to customers each day as employees are incented to provide customers excellent service and protect the public health and safety.

Q. HAS RUCO ALWAYS PROPOSED A SIMILAR ADJUSTMENT IN CASES IT HAS PARTICIPATED IN?

A. I do not believe RUCO always make this type of adjustment. In fact, I reviewed RUCO's adjustments in the last case involving RRUI and there were no incentive pay adjustments proposed even though Liberty employees have been on an incentive pay system as long as I've been at the Company, which pre-dates the last RRUI test year.

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[2] Rebuttal Testimony of Greg Sorensen ("Sorensen Rb.") at 4:1-2.
[3] *Id.* at 5:1-7.

IV. EMPLOYEE BENEFITS PLAN ADJUSTMENT

Q. MR. SORENSEN, IN YOUR REBUTTAL TESTIMONY, DID YOU PROPOSE AN ADJUSTMENT RELATED TO A CHANGE IN THE COMPANY'S BENEFITS COSTS?

A. Yes, I did.

Q. DID ANY OF THE PARTIES TAKE A POSITION REGARDING YOUR ADJUSTMENT?

A. Yes, RUCO conditionally accepted our adjustment, dependent upon the data we supplied relating to their Thirteenth Set of Data Requests. Staff did not accept our adjustment and listed a number of arguments against it.[4]

Q. HAVE YOU SUPPLIED RUCO WITH THE REQUESTED SUPPORT FOR YOUR ADJUSTMENT?

A. Yes, the information was provided in the Company's response to RUCO Data Request 13.1. Staff received the information as well. If RUCO or Staff has additional questions, we'd be happy to supply them with any additional information they feel is needed in order to fully evaluate this ongoing operating expense.

Q. WOULD YOU PLEASE ADDRESS STAFF'S LISTED OPPOSITION TO YOUR BENEFIT PLAN ADJUSTMENT?

A. Certainly. Staff makes nine separate claims in one-half page of testimony all stating why the adjustment should not be made.[5] However, none of these claims is supported by evidence, research or analysis. They are simply one-sentence allegations or questions that lack support and should be rejected for the reasons I explain below.

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[4] *See* Surrebuttal Testimony of Mary J. Rimback at 20.

[5] *Id.*

Q. WHAT WAS STAFF'S FIRST UNSUPPORTED ARGUMENT?

A. First, Staff says that it don't have enough time to review the issue. However, I would point out that Staff did not send one data request in order to attempt to understand the adjustment, the cause of it, or the basis and support for it. On the other hand, RUCO has made a legitimate effort to understand the adjustment, has sent data requests to seek out applicable information, and is evaluating the adjustment on its merits. We appreciate RUCO's efforts in this matter. What is puzzling is that items often arise in a rate case that must be addressed by the other parties, and we always find time to do so. In this docket, Staff changed its ROE from direct to surrebuttal, but the Company can't credibly claim to reject Staff's ROE analysis simply due to lack of time to evaluate it.

Q. THANK YOU, PLEASE CONTINUE.

A. Staff's second unsupported allegation is that we had not informed them of the change to benefit costs when we learned of it in Q4 2012. First, let me say that we learned of the change in the plan the second week of November. However, we did not have the full quantification of the cost until January, at which time we notified Staff and RUCO verbally that there may be an adjustment coming in our rebuttal to be filed in late January. In hindsight, I can wish we had notified Staff earlier. But, I do not believe it would have provided them with any additional material than what is now available, and has been supplied to RUCO for their evaluation purposes.

Q. WHAT ARE STAFF'S THIRD, FOURTH AND FIFTH UNSUPPORTED ALLEGATION?

A. Staff raised a concern that perhaps benefits should not be standardized across the US, but should be regionalized. Staff also alleged that the cost to hire an employee may differ in various parts of the country, so standardizing may not be appropriate.

Additionally, Staff questioned whether benefits should be standardized for water, sewer, electric and gas utilities. Again, Staff just tossed these out without explanation or support, but Staff is now selectively ignoring that there are costs and benefits to being part of a larger entity. I would say that, in general, large publically traded companies tend to standardize things like Health and Safety programs, as well as put a huge focus on Safety in general. At Liberty, we believe "safety" is baked into our DNA, and is a part of everything we do. Certainly there comes a cost with a focus on safety, and that is part of being a big company. Of course, there are also benefits.

Our large, national footprint of over 600 employees has allowed us to gain more favorable health insurance rates from insurance carriers. If Liberty were restricted to a "regional" player as Staff suggests might be preferable, our insurance costs would actually go up, significantly.[6] Our national size and status allows us to obtain better pricing for benefits than our Arizona operations alone would allow.

In response to Staff's concerns on standardization across the different types of utilities, I would say that since we are one company at Liberty Utilities, we should strive to treat our employees as equally as possible, and this extends to benefits. Imagine if in Missouri, where we have gas, water, and sewer companies, Liberty employees in the same vicinity had vastly different benefits. You would create significant inequities and have unhappy employees. Imagine if the ACC did the same thing ... if the Hearing Division had different benefits from the Securities Division? To take the analogy further, do State of Arizona employees in Phoenix have different benefits than those in Nogales? What about Federal

[6] See **Exhibit GS-RJ1.**

employees in New Hampshire? Do they have different benefits than those employees in Arizona? Entities tend to standardize their benefits offerings to their employees to the greatest extent possible, which creates advantages of scale, and administrative efficiencies. It is far easier and more efficient to maintain one medical plan rather than ten different plans.

Staff also wonders whether the cost to hire employees in RRUI's service territory is greater than, less than, or equal to the cost in other parts of the country. We address this as part of the employee's wages. The cost of an operator in Rio Rico is not the same as the cost of an operator in Phoenix. Our operators', or CSRs', wages reflect this difference. This is about benefits, not salaries.

Q. WHAT WAS STAFF'S SIXTH UNSUPPORTED ALLEGATION?

A. Staff asked whether the consultant's report was available to review. Although Staff raises this question, the information was not sought in a data request. We did supply a contract, invoices and other documentation to RUCO in response to their requests, a copy of which was supplied to Staff.

Q. WHAT WAS STAFF'S SEVENTH UNSUPPORTED ALLEGATION?

A. Staff questioned whether the benefits are actually being provided. They are, and the cost is being reflected on the Companies' books in 2013. This cost is known, measurable, and reflects an ongoing cost of the utility to provide services to its customers.

Q. WHAT IS STAFF'S FINAL UNSUPPORTED ALLEGATION?

A. Finally, Staff asks why RRUI believes it has to provide incremental benefits to attract and retain talented employees in a high unemployment economic environment. First, we believe in treating all our employees fairly and compensating them appropriately. I know I have received many complaints or concerns from employees over the years as to why their friends at local municipalities participate in pension plans while Liberty doesn't provide such an opportunity. This puts us at a recruiting and retention disadvantage. As to Staff's concept of providing employees in a depressed market with lower benefit levels, I would point to my earlier comments. Good employers don't do things like that, and good employees don't work on those terms. We want to create a positive work experience for our employees so that they will create a positive experience for our customers. Again, I don't believe that the State of Arizona provides lesser benefits to its employees in Nogales compared to Phoenix because Nogales is a high unemployment economic environment, or that the Federal Government eliminates medical insurance for boarder agents in Nogales because it has higher unemployment than border agents in, say, San Diego.

Q. DO YOU HAVE ANY FURTHER COMMENTS?

A. I don't believe Staff refutes my testimony that the amounts are known and measurable,[7] that the expense will occur on a recurring, go-forward basis,[8] that these costs are specific to Liberty, approximately 25% for shared services staff located in Avondale, AZ, and approximately 75% to RRUI based employees,[9] and that the expense benefits customers.[10]

Q. DOES THIS CONCLUDE YOUR REJOINDER TESTIMONY?

A. Yes.

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[7] Sorensen Rb. at 6:8-11.
[8] *Id.* at 6:12-13.
[9] *Id.* at 6:19-22.
[10] *Id.* at 7:5-7.

RIO RICO UTILITIES, INC. DBA LIBERTY UTILITIES

REJOINDER TESTIMONY OF GREG SORENSEN

MARCH 8, 2013

EXHIBIT GS-RJ1

BURNHAM
BENEFIT ADVISORS
ESTABLISHED 1977

March 1, 2013

Mr. Graham Craig, CHRP CCP CBP GRP
Liberty Utilities
2845 Bristol Circle
Oakville, Ontario L6H 7H7

Re: Health Insurance: Liberty South Plan Costing

Dear Graham:

I am writing in follow up to our conversation regarding the benefits of consolidation under the Liberty National health insurance programs.

Each state's health insurance market is unique in terms of plan designs, offerings and rating methodology which is determined by group size. The pricing of premiums and renewals are based on several factors, including- industry, demographic and claims experience of the specific group.

It is difficult to derive average employer plan pricing in a specific region; therefore to provide a more accurate benchmark our office solicited an Arizona Blue Cross quote based on a Liberty South population for Rio Rico. Below is a summary and comparison:

Monthly Prem	**Liberty National Plan**	**Arizona Blue Cross**
Single	$538	$522
Two Person	$1075	$1148
Family	$1533	$1671
Office Visit	$20 PCP + $20 Specialist	$25 PCP + $40 Specialist
Deductible	$250	$250
Out of Pocket Max	$1000	$2000
Rx Card	$10/30/50	$15/35/65/120

There are numerous benefits not illustrated in the above comparison that make combining individual entities under one plan for standardization:

1. Increased economies of scale resulting in lower administrative costs.

2. Future claim stability via a larger population taking advantage of the "Law of Large Numbers". For example, several large claimants will not significantly impact the experience as the risk is spread.

3. Increased negotiating power with insurers.

4. Additional funding opportunities available with a larger group that can achieve potential cost savings (contingent premium arrangements and self-insurance). For example, the dental and vision plans have been at a creditable size for self-insuring since 2007. Transitioning from fully insured to a self insured platform resulted in average annual savings of $40,000/Year.

If you have any questions or need additional information, please do not hesitate to contact me.

Sincerely,

Mark L. Crawford
Partner

FENNEMORE CRAIG, P.C.
Jay L. Shapiro (No. 014650)
3003 N. Central Ave.
Suite 2600
Phoenix, Arizona 85012
Attorneys for Rio Rico Utilities, Inc.

BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF RIO RICO UTILITIES, INC., AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANTS AND PROPERTY AND FOR INCREASES IN ITS WATER AND WASTEWATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.	DOCKET NO: WS-02676A-12-______

DIRECT TESTIMONY OF

PETER EICHLER

May 31, 2012

EXHIBIT
A-10
ADMITTED

TABLE OF CONTENTS

I. INTRODUCTION AND PURPOSE OF TESTIMONY

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Peter Eichler. My business address is 2865 Bristol Circle, Oakville, Ontario L6H 6X5.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Liberty Utilities (Canada) Corp. ("LUC"), which is the holding company for Liberty Utilities Co. ("Liberty Utilities"), a Delaware corporation, which was formerly known as Liberty Water and which is the sole shareholder of the Applicant, Rio Rico Utilities, Inc. ("RRUI"). I am employed as the Director of Regulatory Strategy.

Q. WHAT ARE YOU PRINCIPAL RESPONSIBILITIES AS DIRECTOR OF REGULATORY STRATEGY?

A. I have overall responsibility for regulatory strategy, including compliance filings, and rate cases, for Liberty Utilities and its 22 operating subsidiaries providing water, sewer, electric and gas utility services in 5 states. I am also responsible for maintaining regulatory outreach programs in the jurisdictions in which the companies owned by Liberty Utilities operate, including planned regular meetings with key regulatory personnel.

Q. PLEASE DESCRIBE YOUR PROFESSIONAL AND EDUCATIONAL BACKGROUND.

A. I have been employed by LUC since September 2009. Prior to my employment at Liberty Utilities, I was employed by Hydro One Networks Inc., Ontario's largest distribution and transmission utility, and Powerstream Inc., a local distribution company serving over 300,000 customers near Toronto. My roles at these utilities included corporate finance, ratemaking and regulatory affairs. I am a designated accountant, having received the Certified Management Accountant designation in

Canada. In addition, I hold a Master of Business Administration degree from the University of Windsor in Ontario, Canada, as well as a Bachelor of Commerce degree with a specialization in finance from Ryerson University in Toronto, Canada. I also completed the National Association of Regulatory Utility Commissioners' Utility School in November 2009.

Q. **HAVE YOU TESTIFIED BEFORE STATE PUBLIC UTILITY REGULATORY COMMISSIONS?**

A. Yes. I testified before the Arizona Corporation Commission ("Commission") in Dockets Nos. WS 02676A-09-0257 and W-02465A-09-0411 for RRUI and Bella Vista Water Company ("Bella Vista"), and before the Illinois Commerce Commission and the New Hampshire Public Utilities Commission and a Texas judicial panel.

Q. **WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS DOCKET?**

A: The purpose of my testimony is to describe the cost allocation procedures used by RRUI's ultimate parent company, Algonquin Power & Utilities Corp. ("APUC") to allocate shared costs between all of its subsidiary and affiliated companies, including Liberty Utilities and its operating utility subsidiaries. My testimony explains these procedures and identifies the benefits of these costs in the provision of safe and reliable utility services, including those provided by RRUI.

Q. **WAS THIS THE SUBJECT OF YOUR PRIOR TESTIMONY BEFORE THE COMMISSION?**

A. Yes and our cost allocation procedures were a source of disagreement between all parties during both of those rate cases for RRUI and Bella Vista. We have worked aggressively, at every level from APUC through Liberty Utilities to the operating utilities like RRUI, to address the concerns raised in those rate case and those efforts have improved our allocation procedures. As a result, and as shown in our updated allocation manual, my testimony illustrates a more transparent process pursuant to which both the necessity and reasonableness of these costs are now plainly shown.

Q. HAS THE COMPANY WORKED WITH STAFF IN DEVELOPING THE NEW MANUAL?

A. Yes. Since the last rate case, I have personally met with Staff several times to discuss changes, solicit input, and provide updates on our cost allocation methodologies and procedures. We have greatly appreciated Staff's input and believe that it has resulted in a better understanding of APUC's business model as well as a better overall allocation methodology.

II. THE APUC-LIBERTY UTILITIES ALLOCATION MODEL

Q. CAN YOU PROVIDE AN OVERVIEW OF LIBERTY UTILITIES' BUSINESS MODEL?

A. Certainly. APUC has two major operating subsidiaries, Algonquin Power Co. ("APCo") and Liberty Utilities. APCo is the unregulated entity that provides renewable power generation from facilities owned throughout Canada and the United States. Liberty Utilities is the entity that owns regulated water, wastewater, gas and electric utilities, but only in the United States.

Q. WHAT IS THE IMPORTANCE OF THESE ENTITIES IN RELATION TO RRUI AND THE OTHER SUBSIDIARIES?

A. APUC serves a significant and very important role in relation to RRUI and its sister companies. First, APUC is the entity that is traded on the Toronto Stock Exchange, and is responsible for ensuring that those entities owned by Liberty Utilities have uninterrupted access to capital. This point, identified as a benefit to ratepayers in the last RRUI rate case,[1] cannot be made enough – but for APUC's existence, RRUI would have a much greater difficulty attracting capital. On a standalone basis, RRUI is a small utility with limited growth potential. Without APUC, RRUI would likely have no investment capital available.

Q. ARE THERE OTHER BENEFITS OF THIS OPERATING MODEL?

A. Yes, in addition to critical access to capital, RRUI and its sister utilities enjoy the following benefits:

1. Access to skilled, strategic management. This means RRUI enjoys access to expertise and resources that are typically not available to small utilities with 8,000 customers.
2. Controls and Processes. Controls and processes are in place to ensure that accounting methodologies are consistent with GAAP and generally accepted principles, a requirement of publicly traded companies.
3. Economies of Scale. By sharing regional resources with other utilities, RRUI enjoys the benefits of lower overall cost structures. Further, as Liberty Utilities' portfolio grows, the overall costs increase proportionally less than it would on a standalone basis.

Q. WHAT TYPES OF COSTS ARE INCURRED AND ALLOCATED?

A. Costs from APUC include corporate management and executive labor which are time sheeted to each operating subsidiary (i.e., Liberty Utilities and APCo). These costs also include corporate treasury, audit services, tax services, third party professional services, and services related to shareholder administration such as Board of Directors and Dividend Escrow payments. Related administration charges such as rent and depreciation are also charged from APUC.

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[1] "One of the great benefits to RRUI from being part of the APIF family is the access to capital that the parent is able to provide." *RRUI*, Decision 72059 (January 6, 2011) at 21:19-21.

Liberty Utilities itself provides strategic oversight, procedures, compliance, and standards to the utilities it owns in the areas of Finance, Regulatory Affairs, Human Resources, Customer Service, Information Technology, and related administrative functions. As such, Liberty Utilities allocates labor costs and other administrative charges incurred in order to provide these services to utilities.

Q. HOW MUCH IS BEING ALLOCATED TO RRUI?

A. As outlined in the Direct Testimony of Tom Bourassa, the amount being allocated for APUC is $92,162 for water and $30,142 for sewer, including all adjustments for non-recoverable costs.

Q. DID LIBERTY UTILITIES ANALYZE THE TYPES OF CHARGES COMPARED TO OTHER REGULATED UTILITIES?

A. Yes, as shown in Exhibit PE-DT1, attached to my testimony, Liberty Utilities compared its corporate structure and charges to several different utilities. First, Liberty Utilities compared its corporate charges as if RRUI were a standalone entity that is publicly traded. The analysis revealed that RRUI would incur the exact same charges as if it were a standalone entity or part of the Liberty Utilities family. Second, we compared the charges to those incurred by other similar Arizona regulated utilities, APS, UNS Gas, TEP, Arizona-American Water Company (now EPCOR) and Global Water, among others. Similar to the first analysis, the aforementioned utilities incurred similar corporate costs. Finally, Liberty Utilities was compared to companies used in cost of capital proxy groups and the results were no different – all of these entities incur the types of costs incurred by Liberty Utilities and its operating subsidiaries like RRUI. In other words, we didn't invent this wheel; we have just worked to make ours work better, with more transparency and efficiency.

Q. **YOU MENTIONED A MANUAL COVERING ALL THIS.**

A. Yes. The methodologies and processes are memorialized in the Cost Allocation Manual ("CAM"), which is attached to my testimony as Exhibit PE-DT2. The CAM generally describes the types of costs, the methodologies used to allocate them, and the benefits of such costs. In general, the CAM is built around the NARUC guidelines for cost allocations. The fundamental premise of those guidelines is to direct charge as much as possible and use reasonable allocators where allocation is necessary.

Q. **CAN YOU CITE SPECIFICALLY THE PRINCIPLES FROM THE NARUC GUIDELINES YOU ARE REFERRING TO?**

A. Yes. The NARUC guidelines specifically state their principles as:

> 1. To the maximum extent practicable, in consideration of administrative costs, costs should be collected and classified on a direct basis for each asset, service or product provided.
>
> 2. The general method for charging indirect costs should be on a fully allocated cost basis. Under appropriate circumstances, regulatory authorities may consider incremental cost, prevailing market pricing or other methods for allocating costs and pricing transactions among affiliates.
>
> 3. To the extent possible, all direct and allocated costs between regulated and non-regulated services and products should be traceable on the books of the applicable regulated utility to the applicable Uniform System of Accounts. Documentation should be made available to the appropriate regulatory authority upon request regarding transactions between the regulated utility and its affiliates.
>
> 4. The allocation methods should apply to the regulated entity's affiliates in order to prevent subsidization from, and ensure equitable cost sharing among the regulated entity and its affiliates, and vice versa.
>
> 5. All costs should be classified to services or products which, by their very nature, are either regulated, non-regulated, or common to both.

6. The primary cost driver of common costs, or a relevant proxy in the absence of a primary cost driver, should be identified and used to allocate the cost between regulated and non-regulated services or products.
7. The indirect costs of each business unit, including the allocated costs of shared services, should be spread to the services or products to which they relate using relevant cost allocators.

Q. YOU ALSO MENTIONED THAT THE CAM BEEN UPDATED.

A. Yes. Attached as Exhibit PE-DT2 is the new CAM that has been used in 2012 (for two months of the test year) and is also used for the purpose of estimating known and measurable changes. The changes to the allocation methodologies are attributable to the anticipated expansion of Liberty Utilities into gas and electric utilities and change only some of the allocation methodologies, not the types of costs being allocated to RRUI. In other words, since this CAM is used across our portfolio, the majority of changes have been incorporated for businesses unrelated to RRUI.

Q. HAS THE COMMISSION APPROVED THE CAM?

A. This Commission does not require approval of the CAM, and therefore no approval has been sought. However, Liberty Utilities would be willing to submit the CAM to the Commission for review and comment. This CAM has been submitted for approval in Illinois, and is the same CAM Liberty Utilities uses in Texas, Missouri, and California. It will also be the same CAM used in New Hampshire and Iowa once operations in those states commence.

Q. YOU MENTIONED HAVING DISCUSSIONS WITH STAFF ABOUT THE CAM. DID LIBERTY INCORPORATE RECOMMENDATIONS FROM COMMISSION STAFF?

A. Yes, and Staff's input was invaluable and much appreciated. We have met on several occasions with Staff to discuss our cost allocations and have attempted to address the issues and objections to the cost allocations raised by Staff, as well as RUCO, in RRUI's last rate case.

Q. DID YOU ALSO MEET WITH RUCO?

A. Yes. We met with RUCO after the previous rate case to let them know about changes that were being considered to the CAM.

Q. WHAT ARE SOME OF THE CHANGES YOU MADE IN RESPONSE TO THESE MEETINGS WITH STAFF AND RUCO?

A. There have been several changes made to the allocation manual. For example:

1. Allocators: APUC no longer uses the number of entities as its first level allocator. Instead, a 4-factor methodology - number of employees, EBITDA, and other allocation factors are used to apportion costs between the regulated and unregulated entities.

2. Unshared costs: APUC now retains approximately 8% of costs incurred such as corporate donations and certain corporate travel and such costs do not get allocated between subsidiaries and are borne solely by APUC shareholders. This alleviates a previous concern raised that all the costs were allocated between the operating entities.

3. Labor: Previously, Executive Management was provided through an affiliated third party that charged a fixed fee to APUC. Executive Management has now been internalized, and the Chief Executive Officer, Chief Financial Officer, General Counsel, and other APUC functions use timesheets to apportion costs between Liberty Utilities and APCo. These timesheets establish a direct link between management costs and the entities served, again the underlying goal of the NARUC guidelines. This also alleviates a previous concern of Staff and RUCO in that it directly correlates services provided to the utilities served.

4. Liberty Utilities level allocations: In previous cases, Liberty Water was the only operating entity for APUC's regulated utilities. With the recent and proposed acquisitions described above, Liberty Utilities is now organized by region and will soon operate under the Liberty Utilities brand, irrespective of the type of distribution utility. As a result, RRUI will operate as part of Liberty Utilities' South region. This regionalization and its shared cost implications are reflected in the CAM.

Q. HAS THE RECORDING OF APPROPRIATE COSTS CHANGED?

A. Yes. As stated above, approximately 8% of costs are no longer allocated between APUC's operating entities. This accounts for charitable contributions, some corporate travel, and other similar costs which are appropriately borne by APUC's shareholders.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes.

Rio Rico Utilities, Inc.
2012 Rate Application

Peter Eichler Direct Testimony

Exhibit PE-DT1

Corporate Cost Allocation Analysis

Liberty Utilities
WATER | GAS | ELECTRIC

Cost Type	APUC	Rio Rico Utilities, Inc. (stand alone entity)	APS, UNS Gas, TEP, Global, Arizona American	Cost of Capital Proxy Companies
Strategic Management				
a) Board of Directors	√	√	√	√
b) Legal Services	√	√	√	√
c) Professional Services	√	√	√	√
Access to Capital Markets				
a) Licenses & Permits	√	√	√	√
b) Escrow Fees	√	√	√	√
c) Shareholder Communications	√	√	√	√
Financial Controls				
a) Audit Fees	√	√	√	√
b) Tax Services	√	√	√	√
Administrative Support	√	√	√	√

Rio Rico Utilities, Inc.
2012 Rate Application

Peter Eichler Direct Testimony

Exhibit PE-DT2

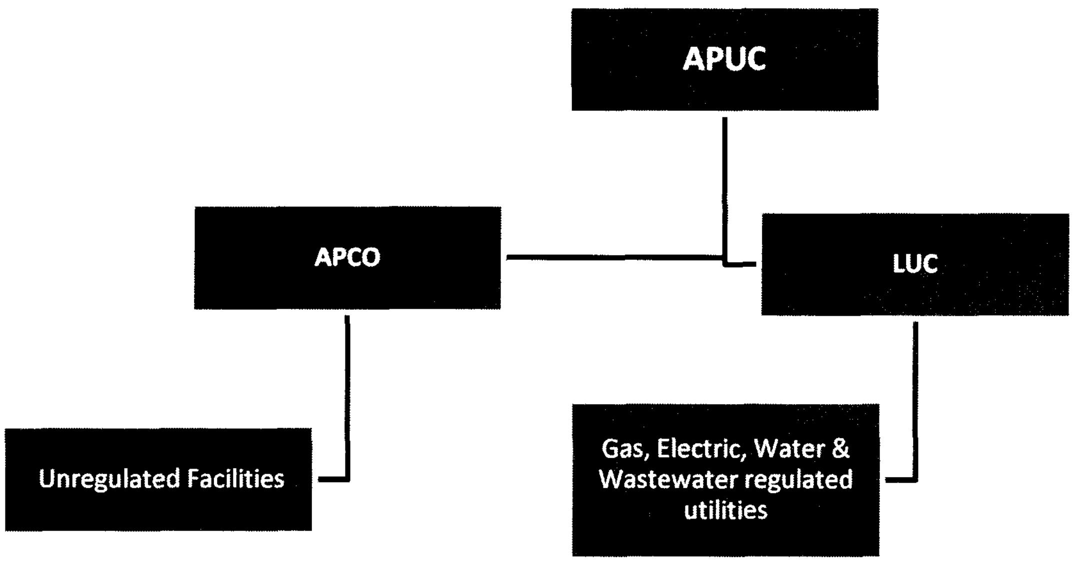
ALGONQUIN POWER & UTILITIES CORP. DIRECT CHARGE AND COST ALLOCATIONS MANUAL

This document outlines the methods of direct charge and cost allocations: (i) between Algonquin Power & Utilities Corp. and its affiliates Algonquin Power Company and Liberty Utilities (Canada) Corp.; (ii) between Liberty Utilities (Canada) Corp. and its regulated utility subsidiaries; and (iii) between Liberty Utilities (Canada) Corp.'s service companies and its regulated utility subsidiaries.

Table of Contents

I. INTRODUCTION

The purpose of this paper is to provide a detailed explanation of services provided by Algonquin Power & Utilities Corp ("APUC"), Liberty Utilities (Canada) Corp. ("LUC"), and LUC's service companies (the "Service Companies") to the regulated utility assets and to describe the Direct Charge and Cost Allocation Methodologies used by APUC, LUC and the Service Companies. The following organization chart describes the relationships between the separate entities:



The following Cost Allocation Manual ("CAM") has been completed in accordance and conformance with the "NARUC Guidelines for Cost Allocations and Affiliate Transactions". More specifically, the founding principles of this Cost Allocation Manual is to a) directly charge as much as possible to the entity that procures any specific service, and b) to ensure that inappropriate subsidization of unregulated activities by regulated activities and vice versa does not occur. For ease of reference, the NARUC Guidelines are attached as Appendix 1.

Costs charged and allocated pursuant to this CAM shall include direct labor, direct materials, direct purchased services associated with the related asset or services, and overhead amounts.

i. Tariffed rates or other pricing mechanisms established by rate setting authorities shall be used to provide all regulated services.

ii. Services not covered by (ii) shall be charged by the providing party to the receiving party at fully distributed cost.

iii. Facilities and administrative services rendered to a rate-regulated subsidiary shall be charged on the following basis:

(1) the prevailing price for which the service is provided for sale to the general public by the providing party (i.e., the price charged to non-affiliates if such transactions with non-affiliates constitute a substantial portion of the providing party's total revenues from such transactions) or, if no such prevailing price exists, (2) an amount not to exceed the fully distributed cost incurred by the providing party in providing such service to the receiving party.

II. THE APUC CORPORATE STRUCTURE

APUC's primary business is direct interest or equity ownership in renewable and thermal power generating facilities and regulated utilities. APUC owns a widely diversified portfolio of independent power production facilities and regulated utilities consisting of water distribution and wastewater treatment facilities and electric and gas utilities in Canada and the United States. APUC is publicly traded on the Toronto Stock Exchange. Its structure as a publicly traded holding company provides substantial benefits to its regulated utilities through access to capital markets and access to engineers, technicians, professional managers, and administrative staff, including trained plant operators and field supervisors.

APUC is the ultimate corporate parent and affiliate that provides financial, strategic management, corporate governance, administrative and support services to LUC and its subsidiaries as well as to the numerous unregulated utility assets held by APCo. The services provided by APUC are necessary for LUC and its subsidiaries to have access to capital markets for capital projects and operations, and are necessary in providing a high level of shared services at the lowest cost. These services are expensed at APUC and are performed for the benefit of APCo and LUC and their respective businesses.

APUC and its affiliates capitalize on APUC's expertise and access to the capital markets through the use of certain shared services, which maximizes economies of scale and minimizes redundancy. In short, it provides for maximum expertise at lower costs. Further, the use of shared expertise allows each of the entities to receive a benefit they may not be able to achieve on a standalone basis such as strategic management advise and access to capital at more competitive rates.

III. SCOPE OF SERVICES PROVIDED BY APUC TO ITS SUBSIDIARIES AND HOW THOSE COSTS ARE ALLOCATED

A. Non-Labor Services and Cost Allocation from APUC to LUC and APCo

APUC's non-labor services include Financing Services and Administrative Services. As used herein "Financing Services" means the selling of units to public investors in order to generate the funding and capital necessary for LUC and APCo as well as providing legal and treasury services in connection with the issuance of public debt. As used herein "Administrative Services" includes the following types of services: strategic management services, corporate governance, and administration and management services such as consultation on management and administration of all aspects of utility business, including economic and strategic analysis.

The capital and funds obtained from the sale of shares in APUC are used by LUC and APCo for current and future capital investments. The services provided by APUC are critical and necessary to LUC and APCo because without those services they would not have a readily available source of capital funding. Put another way, absent the services provided by APUC, each business, including each utility, would be forced to operate as stand-alone utilities, with resulting higher costs and operating expenses incurred by customers. In addition, the utilities would bare much greater risk due to a potential inability to obtain capital on a standalone basis.

The services provided by APUC specifically optimize performance of LUC, keeping rates low for customers while ensuring access to capital is available. If the utilities did not have access to the services provided by APUC, then they would be forced to incur associated costs for financing, capital investment, audits, taxes and other similar services on a stand-alone basis, which would substantially increase such costs. Simply put, without incurring these costs, APUC would not be able to invest capital in its subsidiaries, including the regulated utilities.

In connection with the provision of Financing and Administrative Services, APUC incurs the following types of costs: (i) strategic management costs (board of director, third-party legal services, accounting services, tax planning and filings, insurance, and required auditing); (ii) capital access costs (communications, trustee fees, escrow and transfer agent fees); (iii) financial control costs (audit and tax expenses); and (iv) administrative (rent, depreciation, general office costs. See Appendix 2 for a more detailed discussion of the costs incurred by APUC.

Non-labor costs, including corporate capital, are pooled and allocated to LUC and APCo using a Three Factor Methodology. The three factors in the Three Factors

Methodology are revenue, expenses, and plant-in-service. Each of the three factors are given equal weight, or 33.3%. Notwithstanding the above, if a charge is related either solely to the regulated utility business, *i.e.*, LUC, or to the power generation business, *i.e.*, APCo, then all of those costs will be allocated to the business segment for which they are incurred. Furthermore, costs directly attributable to a specific region ("Regional Costs") are identified as such and allocated by LUC to the utilities in that region using the Utility Four Factor Methodology, as defined in Section IV. Lastly, if a cost can be directly attributable to a specific entity, it will be directly charged to that entity. For an example of how an invoice would be allocated, please see Appendix 3.

Certain costs, which are incurred for the benefit of APUC's businesses, are not allocated to any subsidiary. These include costs such as donations, certain corporate travel, and certain overheads.

B. Labor Services And Cost Allocation From APUC To LUC and APCo

As described above, APUC provides benefits to the utilities it owns by use of certain shared services. Labor for services such as executive management, corporate accounting, treasury services, investor relations, and corporate finance are provided by APUC to LUC and APCo.

APUC charges labor rates at cost, which is the dollar hourly rate per employee as recorded in APUC's payroll systems, grossed up for burdens such as payroll taxes, health benefits, retirement plans, and other insurance provided to employees. APUC allocates these costs to LUC and APCo using the Three Factor Methodology. As discussed in Section IV, LUC then allocates these costs to its regulated utilities using the Utility Four Factor Methodology.

C. Labor Services And Cost Allocation From APCo To LUC

From time to time, APCo may provide Engineering and Technical Labor to Liberty Utilities. These charges plus an allocation for corporate overheads such as rent, materials/supplies, etc. are capitalized and directly charged to the relevant utility.

IV. SCOPE OF SERVICES PROVIDED BY LUC TO ITS SUBSIDIARIES AND APUC AND APCO AND HOW THOSE COSTS ARE ALLOCATED

LUC provides its regulated utilities with the following services: accounting, corporate finance, human resources, information technology, rates and regulatory affairs, environment, health and safety, and security, customer service, procurement, and utility planning. The following are examples of those services: (i) budgeting, forecasting, and financial reporting services including preparation of reports and preservation of records, cash management (including electronic fund transfers, cash receipts processing, managing short-term borrowings and investments with third parties); (ii) development of customer service policies and procedures; (iii) development of human resource policies and procedures; (iv) selection of information systems and equipment for accounting, engineering, administration, customer service, emergency restoration and other functions and implementation thereof; (v) development, placement and administration of insurance coverages and employee benefit programs, including group insurance and retirement annuities, property inspections and valuations for insurance; (vi) purchasing services including preparation and analysis of product specifications, requests for proposals and similar solicitations; and vendor and vendor-product evaluations; (vii) energy procurement oversight and load forecasting; and (viii) development of regulatory strategy.

Unless a charge can be directly attributable to a specific utility, LUC allocates its direct labor and direct non-labor costs, including capital costs, to its regulated utilities using a Utility Four Factor Methodology. LUC uses the Utility Four Factor Methodology to allocate Regional Costs to the utilities in that region and to allocate costs incurred for the benefit of all of its regulated assets ("System-Wide Costs") to all of its utilities.

The "Four Factor Utility Methodology" allocates costs by relative size of the utilities. The methodology used by LUC involves (1) Utility Plant, (2) Total Customers, (3) Non-Labor Expenses, and (4) Labor as allocating factors, with each factor assigned a specific weight. LUC uses the following weights under this Four Factor Utility Methodology:

Utility Plant	50%
Customer Count	40%
Non-Labor Expenses	5%
Labor	5%
Total	**100%**

LUC also uses the Utility Four Factor Methodology to allocate to its regulated utilities the System-Wide indirect labor and indirect non-labor costs allocated to LUC from APUC. As discussed in Section III(A), Regional Costs charged to LUC from APUC are allocated to the utilities in that region using the Utility Four Factor Methodology.

The following simplified hypothetical example demonstrates how the Utility Four Factor Methodology would be calculated based on ownership of only two hypothetical utilities:

FACTOR	Utility 1	Utility 2	TOTAL ALL UTILTIES	UTILITY 1 % OF TOTAL	FACTOR WEIGHT	UTILITY 1 ALLOCATION
UTILITY PLANT	727	371	1098	66%	50%	33%
CUSTOMER COUNT	6000	1000	7000	86%	40%	34%
LABOR COSTS	57	32	89	64%	5%	3%
EXPENSES	108	41	149	72%	5%	4%
TOTAL ALLOCATION						74%

As can be seen from these hypothetical numbers, Utility 1 would be allocated 74% of total Administrative/Overhead Costs incurred by LUC, based on its relative size and application of the Utility Four Factor Methodology in comparison to Utility 2. Utility 2 would be allocated the remaining 26%. LUC has developed and utilized this methodology to better allocate costs, recognizing that larger utilities require more time and management attention and incur greater costs than smaller ones.

In addition, LUC provides information technology and some human resource services to APCo and APUC. These costs are directly charged to APCo and APUC.

V. SERVICE COMPANY SERVICES AND COST ALLOCATION

Some of LUC's regulated utilities may receive services such as: billing and customer service; operations and engineering; environment, health and safety, and security; finance; information technology; regulatory; legal; and administrative services, *e.g.*, rent, insurance, and office services, from a Service Company.

Unless a charge can be directly attributable to a specific utility, billing and customer service costs are allocated on customer count. For an example of how this allocation works please see Appendix 4. Operations and engineering costs are directly charged based on timesheets to the relevant regulated utility. Unless a charge can be directly attributable to a specific utility, both labor and non-labor (including capital) environment, health and safety, and security, finance, information technology, regulatory, legal, and administrative costs are allocated using the Utility Four Factor Methodology.

VI. ALLOCATION OF GAS PROCUREMENT SERVICES PROVIDED BY LIBERTY ENERGY UTILITIES (NEW HAMPSHIRE) CORP TO THE NATURAL GAS UTIILITY SUBSIDIARIES OF LUC AND HOW THOSE COSTS ARE ALLOCATED

LUC's natural gas utilities receive gas procurement services from a shared group that is housed out of New Hampshire. The group's non-labor costs are directly charged to specific assets. The gas procurement employees directly charge their time to specific assets as well. Any shared services that are provided, such as development of an overall hedging strategy, are allocated based on natural gas volumes.

I. Appendix

Appendix 1: NARUC Guidelines for Cost Allocations

Guidelines for Cost Allocations and Affiliate Transactions:

The following Guidelines for Cost Allocations and Affiliate Transactions (Guidelines) are intended to provide guidance to jurisdictional regulatory authorities and regulated utilities and their affiliates in the development of procedures and recording of transactions for services and products between a regulated entity and affiliates. The prevailing premise of these Guidelines is that allocation methods should not result in subsidization of non-regulated services or products by regulated entities unless authorized by the jurisdictional regulatory authority. These Guidelines are not intended to be rules or regulations prescribing how cost allocations and affiliate transactions are to be handled. They are intended to provide a framework for regulated entities and regulatory authorities in the development of their own policies and procedures for cost allocations and affiliated transactions. Variation in regulatory environment may justify different cost allocation methods than those embodied in the Guidelines.

The Guidelines acknowledge and reference the use of several different practices and methods. It is intended that there be latitude in the application of these guidelines, subject to regulatory oversight. The implementation and compliance with these cost allocations and affiliate transaction guidelines, by regulated utilities under the authority of jurisdictional regulatory commissions, is subject to Federal and state law. Each state or Federal regulatory commission may have unique situations and circumstances that govern affiliate transactions, cost allocations, and/or service or product pricing standards. For example, The Public Utility Holding Company Act of 1935 requires registered holding company systems to price "at cost" the sale of goods and services and the undertaking of construction contracts between affiliate companies.

The Guidelines were developed by the NARUC Staff Subcommittee on Accounts in compliance with the Resolution passed on March 3, 1998 entitled "Resolution Regarding Cost Allocation for the Energy Industry" which directed the Staff Subcommittee on Accounts together with the Staff Subcommittees on Strategic Issues and Gas to prepare for NARUC's consideration, "Guidelines for Energy Cost Allocations." In addition, input was requested from other industry parties. Various levels of input were obtained in the development of the Guidelines from the Edison Electric Institute, American Gas Association, Securities and Exchange Commission, the Federal Energy Regulatory Commission, Rural Utilities Service and the National

Rural Electric Cooperatives Association as well as staff of various state public utility commissions.

In some instances, non-structural safeguards as contained in these guidelines may not be sufficient to prevent market power problems in strategic markets such as the generation market. Problems arise when a firm has the ability to raise prices above market for a sustained period and/or impede output of a product or service. Such concerns have led some states to develop codes of conduct to govern relationships between the regulated utility and its non-regulated affiliates. Consideration should be given to any "unique" advantages an incumbent utility would have over competitors in an emerging market such as the retail energy market. A code of conduct should be used in conjunction with guidelines on cost allocations and affiliate transactions.

A. DEFINITIONS

1. Affiliates - companies that are related to each other due to common ownership or control.

2. Attestation Engagement - one in which a certified public accountant who is in the practice of public accounting is contracted to issue a written communication that expresses a conclusion about the reliability of a written assertion that is the responsibility of another party.

3. Cost Allocation Manual (CAM) - an indexed compilation and documentation of a company's cost allocation policies and related procedures.

4. Cost Allocations - the methods or ratios used to apportion costs. A cost allocator can be based on the origin of costs, as in the case of cost drivers; cost-causative linkage of an indirect nature; or one or more overall factors (also known as general allocators).

5. Common Costs - costs associated with services or products that are of joint benefit between regulated and non-regulated business units.

6. Cost Driver - a measurable event or quantity which influences the level of costs incurred and which can be directly traced to the origin of the costs themselves.

7. Direct Costs - costs which can be specifically identified with a particular service or product.

8. Fully Allocated costs - the sum of the direct costs plus an appropriate share of indirect costs.

9. Incremental pricing - pricing services or products on a basis of only the additional costs added by their operations while one or more pre-existing services or products support the fixed costs.

10. Indirect Costs - costs that cannot be identified with a particular service or product. This includes but not limited to overhead costs, administrative and general, and taxes.

11. Non-regulated - that which is not subject to regulation by regulatory authorities.

12. Prevailing Market Pricing - a generally accepted market value that can be substantiated by clearly comparable transactions, auction or appraisal.

13. Regulated - that which is subject to regulation by regulatory authorities.

14. Subsidization - the recovery of costs from one class of customers or business unit that are attributable to another.

B. COST ALLOCATION PRINCIPLES

The following allocation principles should be used whenever products or services are provided between a regulated utility and its non-regulated affiliate or division.

1. To the maximum extent practicable, in consideration of administrative costs, costs should be collected and classified on a direct basis for each asset, service or product provided.

2. The general method for charging indirect costs should be on a fully allocated cost basis. Under appropriate circumstances, regulatory authorities may consider incremental cost, prevailing market pricing or other methods for allocating costs and pricing transactions among affiliates.

3. To the extent possible, all direct and allocated costs between regulated and non-regulated services and products should be traceable on the books of the applicable regulated utility to the applicable Uniform System of Accounts. Documentation should be made available to the appropriate regulatory authority upon request regarding transactions between the regulated utility and its affiliates.

4. The allocation methods should apply to the regulated entity's affiliates in order to prevent

subsidization from, and ensure equitable cost sharing among the regulated entity and its affiliates, and vice versa.

5. All costs should be classified to services or products which, by their very nature, are either regulated, non-regulated, or common to both.

6. The primary cost driver of common costs, or a relevant proxy in the absence of a primary cost driver, should be identified and used to allocate the cost between regulated and non-regulated services or products.

7. The indirect costs of each business unit, including the allocated costs of shared services, should be spread to the services or products to which they relate using relevant cost allocators.

C. COST ALLOCATION MANUAL (NOT TARIFFED)

Each entity that provides both regulated and non-regulated services or products should maintain a cost allocation manual (CAM) or its equivalent and notify the jurisdictional regulatory authorities of the CAM's existence. The determination of what, if any, information should be held confidential should be based on the statutes and rules of the regulatory agency that requires the information. Any entity required to provide notification of a CAM(s) should make arrangements as necessary and appropriate to ensure competitively sensitive information derived therefrom be kept confidential by the regulator. At a minimum, the CAM should contain the following:

1. An organization chart of the holding company, depicting all affiliates, and regulated entities.

2. A description of all assets, services and products provided to and from the regulated entity and each of its affiliates.

3. A description of all assets, services and products provided by the regulated entity to non-affiliates.

4. A description of the cost allocators and methods used by the regulated entity and the cost allocators and methods used by its affiliates related to the regulated services and products provided to the regulated entity.

D. AFFILIATE TRANSACTIONS (NOT TARIFFED)

The affiliate transactions pricing guidelines are based on two assumptions. First, affiliate transactions raise the concern of self-dealing where market forces do not necessarily drive prices. Second, utilities have a natural business incentive to shift costs from non-regulated competitive operations to regulated monopoly operations since recovery is more certain with captive ratepayers. Too much flexibility will lead to subsidization. However, if the affiliate transaction pricing guidelines are too rigid, economic transactions may be discouraged.

The objective of the affiliate transactions' guidelines is to lessen the possibility of subsidization in order to protect monopoly ratepayers and to help establish and preserve competition in the electric generation and the electric and gas supply markets. It provides ample flexibility to accommodate exceptions where the outcome is in the best interest of the utility, its ratepayers and competition. As with any transactions, the burden of proof for any exception from

the general rule rests with the proponent of the exception.

1. Generally, the price for services, products and the use of assets provided by a regulated entity to its non-regulated affiliates should be at the higher of fully allocated costs or prevailing market prices. Under appropriate circumstances, prices could be based on incremental cost, or other pricing mechanisms as determined by the regulator.

2. Generally, the price for services, products and the use of assets provided by a non-regulated affiliate to a regulated affiliate should be at the lower of fully allocated cost or prevailing market prices. Under appropriate circumstances, prices could be based on incremental cost, or other pricing mechanisms as determined by the regulator.

3. Generally, transfer of a capital asset from the utility to its non-regulated affiliate should be at the greater of prevailing market price or net book value, except as otherwise required by law or regulation. Generally, transfer of assets from an affiliate to the utility should be at the lower of prevailing market price or net book value, except as otherwise required by law or regulation. To determine prevailing market value, an appraisal should be required at certain value thresholds as determined by regulators.

4. Entities should maintain all information underlying affiliate transactions with the affiliated utility for a minimum of three years, or as required by law or regulation.

E. AUDIT REQUIREMENTS

1. An audit trail should exist with respect to all transactions between the regulated entity and its affiliates that relate to regulated services and products. The regulator should have complete access to all affiliate records necessary to ensure that cost allocations and affiliate transactions are conducted in accordance with the guidelines. Regulators should have complete access to affiliate records, consistent with state statutes, to ensure that the regulator has access to all relevant information necessary to

evaluate whether subsidization exists. The auditors, not the audited utilities, should determine what information is relevant for a particular audit objective. Limitations on access would compromise the audit process and impair audit independence.

2. Each regulated entity's cost allocation documentation should be made available to the company's internal auditors for periodic review of the allocation policy and process and to any jurisdictional regulatory authority when appropriate and upon request.

3. Any jurisdictional regulatory authority may request an independent attestation engagement of the CAM. The cost of any independent attestation engagement associated with the CAM, should be shared between regulated and non-regulated operations consistent with the allocation of similar common costs.

4. Any audit of the CAM should not otherwise limit or restrict the authority of state regulatory authorities to have access to the books and records of and audit the operations of jurisdictional utilities.

5. Any entity required to provide access to its books and records should make arrangements as necessary and appropriate to ensure that competitively sensitive information derived therefrom be kept confidential by the regulator.

F. REPORTING REQUIREMENTS

1. The regulated entity should report annually the dollar amount of non-tariffed transactions

associated with the provision of each service or product and the use or sale of each asset for the following:

a. Those provided to each non-regulated affiliate.

b. Those received from each non-regulated affiliate.

c. Those provided to non-affiliated entities.

2. Any additional information needed to assure compliance with these Guidelines, such as cost of service data necessary to evaluate subsidization issues, should be provided.

Source:
http://www.naruc.org/Publications/Guidelines%20for%20Cost%20Allocations%20and%20Affiliate%20Transactions.pdf

Appendix 2 – Detailed Explanation of APUC Costs

1. APUC STRATEGIC MANAGEMENT COSTS

Strategic management decisions are critical for any public utility. The need for strategic management is even more pronounced for APUC as a publicly traded company, which depends on access to capital funding through public sales of units. APUC seeks to hire talented strategic managers that aid in running each facility owned by the company as efficiently and effectively as possible. This ensures the long term health of each utility and ensures that rates are kept as low as possible without compromising the level of service. It also facilitates each regulated utility's access to necessary capital funding at reduced costs. The costs included in Strategic Management Costs fall into the following categories.

a. Board of Directors

The Board of Directors provides strategic oversight on all company affairs including high level approvals of strategy, operation and maintenance budgets, capital budgets, etc. In addition, the Board of Directors provides corporate governance and ensures that capital and costs are incurred prudently, which ultimately protects ratepayers.

b. General Legal Services

General legal services involve legal matters not specific to any single facility, including review of audited financial statements, annual information filings, Sedar filings, review of contracts with credit facilities, incorporation, tax issues of a legal nature, market compliance, and other similar legal costs. These legal services are required in order for APUC to provide capital funding to individual utilities, without which the utilities could not provide adequate service. Additionally, the services ensure that APUC's subsidiaries remain compliant in all aspects of operations and prevents those entities from being exposed to unnecessary risks.

c. Professional Services

Professional Services including strategic plan reviews, capital market advisory services, ERP System maintenance, benefits consulting, and other similar professional services. By providing these services at a parent level, the subsidiaries are able to benefit from economies of scale. Additionally, some of these services improve APUC's access to capital which benefits all of its subsidiaries.

2. Access to Capital Markets

One of APUC's primary functions is to ensure its subsidiaries have access to quality capital. APUC is listed on the Toronto Stock Exchange, a leading financial market. In order to allow it subsidiaries to have continued access to those capital markets, APUC incurs the following costs. These services and costs are a prerequisite to the subsidiaries continued access to those capital markets.

a. License and Permit Fees

In connection with APUC's participation in the Toronto Stock Exchange, APUC incurs certain license and permit fees such as Sedar fees, annual filing fees, licensing fees, etc. These licensing and permit fees are required in order to sell units on the Toronto Stock Exchange, which in turn provides funding for utility operations.

b. Escrow Fees

In connection with the payment of dividends to unit holders, APUC incurs escrow fees. Escrow fees are incurred to ensure continued access to capital and ensure continuing and ongoing investments by shareholders. Without such escrow fees, APUC's subsidiaries would not have a readily available source of capital funding.

c. Unitholder Communications

Unit holder communication costs are incurred to comply with filing and regulatory requirements of the Toronto Stock Exchange and meet the expectations of shareholders. These costs include items such as news releases and unit holder conference calls. In the absence of shareholder communication costs, investors would not invest in the units of APUC, and in turn, APUC would not have capital to invest in its subsidiaries. With such communications services, the subsidiaries would not have a readily available source of capital funding.

3. APUC Financial Controls

Financial control costs incurred by APUC include costs for audit services and tax services. These costs are necessary to ensure that the subsidiaries are operating in a manner that meets audit standards and regulatory requirements, which have strong financial and operational controls, and financial transactions are recorded accurately and prudently. Without these services, the regulated utilities would not have a readily available source of capital funding.

a. Audit Fees

Audits are done on a yearly basis and reviews are performed quarterly on all facilities owned by APUC on an aggregate level. These corporate parent level audits reduce the cost of the standalone audits significantly for utilities which must perform its own separate audits. Where standalone audits are not required, ratepayers receive benefits of additional financial rigor, as well as access to capital, and financial soundness checks by third parties. Finally, during rate cases, the existence of audits provides staff and intervenors additional reliance on the company records, thus reducing overall rate case costs. The aggregate audit is necessary for the regulated utilities to have continued access to capital markets and unit holders.

b. Tax Services

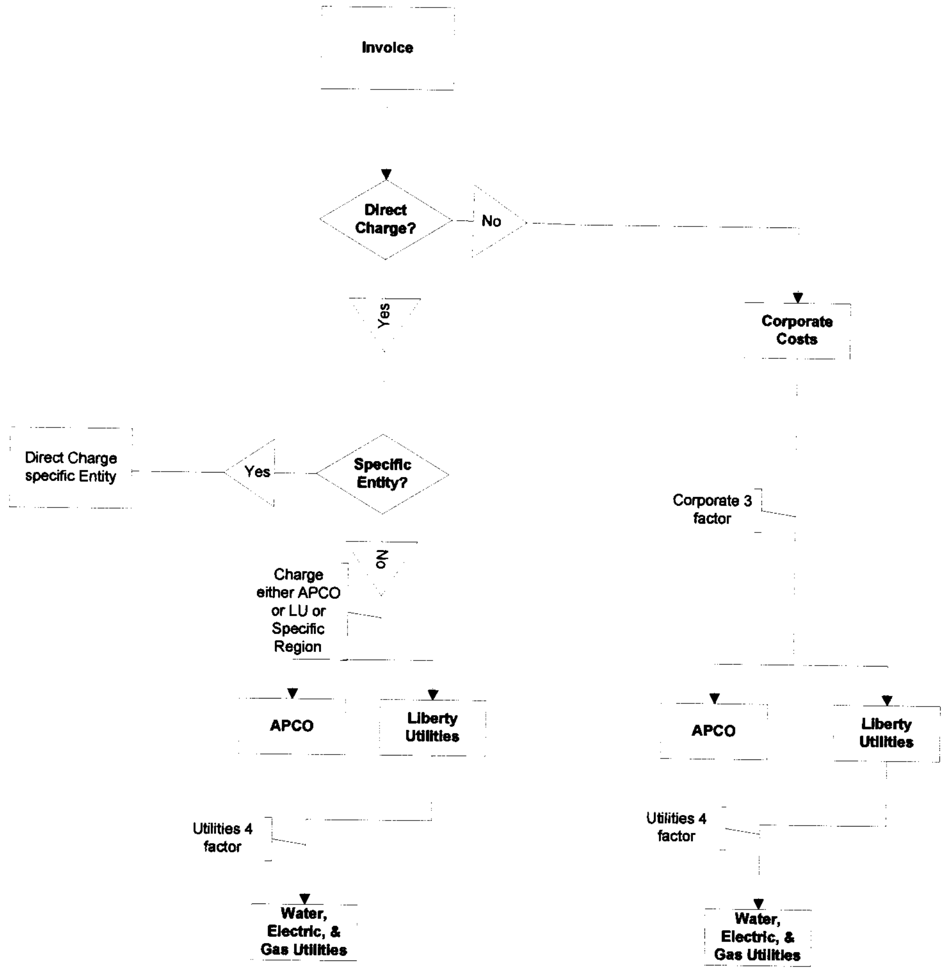
Taxes are paid on behalf of the regulated utilities at the parent level as part of a consolidated United States tax return. Tax services such as planning and filing are provided by third parties. Filing tax returns on a consolidated basis benefits each regulated utility by reducing the costs that otherwise would be incurred by such utility in filing its own separate tax return.

4. APUC ADMINISTRATIVE COSTS

Finally, administrative costs incurred by APUC such as rent, depreciation of office furniture, depreciation of computers, and general office costs are required to house all the services mentioned above. Without these administrative costs, the employees of APUC could not perform their work and provide the necessary services to the regulated utilities. These administrative costs also include training for corporate employees. The Three Factor Methodology is used to allocate these costs.

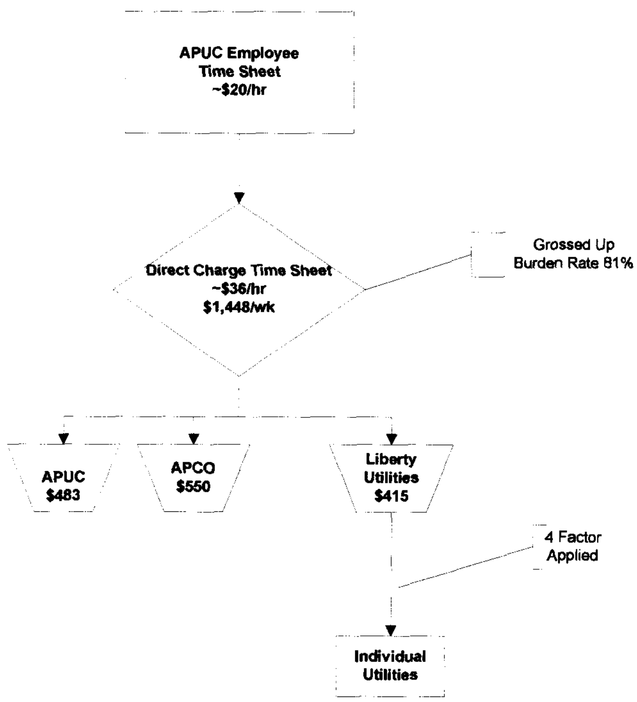
APPENDIX 3 – LIFE OF AN INVOICE

A hypothetical example is being provided of an invoice received by APUC for services to be allocated to its subsidiaries. The below diagram is intended to visually communicate APUC's allocation to APCo and Liberty Utilities.



APPENDIX 4 - LABOR ALLCOATION EXAMPLE

The following simplified example demonstrates how an APUC employee's labor costs would be allocated to the regulated utilities:



RESIDENTIAL UTILITY CONSUMER OFFICE'S ("RUCO") RESPONSE TO RIO RICO UTILITY COMPANY, INC.'S SIXTH SET OF DATA REQUESTS

DOCKET NO. WS-02676A-12-0196

February 27, 2013

6.1. Admit that there is no material difference on the revenue requirement between the Company's proposed hypothetical capital structure with 80 percent equity and 20 percent debt and an actual capital structure with 20 percent debt, assuming the same cost of debt. If your response is anything but an unqualified admission, state the basis for not admitting.

Response (Rigsby)

Assuming that there is no difference in either the cost of common equity, the cost of debt, and the application of a synchronized interest calculation (using the weighted cost of debt to arrive at an appropriate interest deduction for pro forma income tax expense), RUCO will admit that there would be no material difference on the revenue requirement between the Company's proposed hypothetical capital structure with 80 percent equity and 20 percent debt and an actual capital structure with 20 percent debt.

EXHIBIT
A-11
ADMITTED

Ibbotson® SBBI®

2012 Valuation Yearbook

Market Results for
Stocks, Bonds, Bills, and Inflation
1926–2011

MORNINGSTAR®

EXHIBIT
tabbles®
A-12
ADMITTED

Table 7-14 shows the returns of capitalization deciles 2 through 10 in excess of the return on decile 1; the excess returns are segregated into months. For each decile and for each month, the exhibit shows both the average excess return and the number of times the excess return was positive. These two statistics measure the seasonality of the excess return in different ways—the average excess return illustrates the size of the seasonality effect, while the number of positive excess returns shows its reliability.

Virtually all of the small stock effect occurs in January, as the excess outcomes for small company stocks are mostly negative in the other months of the year. Excess returns in January relate to size in a precisely rank-ordered fashion, and the January effect seems to pervade all size groups. Yet, simply demonstrating that the size premium is largely produced by the January effect does nothing to refute the existence of such a premium.

Possible Explanations for the January Effect

There is no generally accepted explanation of the January effect. One potential explanation is that it results from year-end window dressing by portfolio managers. Window dressing is the process of dumping money-losing stocks just before year-end so that such stocks are not included in the portfolio managers' annual reports.

Another explanation of the January effect is that it results from tax-loss selling at year-end, whereby money-losing stocks are sold at the end of the year for tax purposes. They are then repurchased in the market in January. Investors who have earned a capital loss on a security may be motivated to sell their shares shortly before the end of December in order to realize the capital loss for income tax purposes. This creates a preponderance of sellers in need of willing buyers at year-end. Amid such selling pressure, transactions will generally occur at the bid price, or the price a buyer is willing to pay for a particular stock, which is generally lower than the ask price. Therefore, a preponderance of sell orders will register more transactions at lower bid prices, which may create some temporary downward pressure on the prices of these stocks. They will only appear to recover in January, when trading returns to a more balanced mix of buy and sell orders, though there may be some actual recovery of prices as money generated by tax-loss selling returns to the market, driving up demand.

How does this cause "small" stocks to have higher apparent returns? Stocks that are "losers" will tend to have depressed stock prices. Also, stocks whose prices are quoted at the "bid" price will tend to have lower apparent market values than stocks quoted at the "ask" price. These two effects may lead to a bias when we use the market value of equity as our measure of "size." If losing stocks have both depressed prices and a tendency to sell at the "bid" at year-end, then they will likely be pushed down in the rankings according to market value. At the same time, winners will be pushed up. Thus, portfolios composed of "small" market value companies will tend to have more "losers" whose returns in January are distorted by tax-loss selling.

This argument vanishes if one uses a non-value criterion (such as net sales, total assets, or number of employees) to measure "size." As long as the "size" measure is not based on market value, there will be no tendency for firms with depressed stock prices to be ranked lower than other firms or for "small" stock portfolios to include a preponderance of "bid" prices at year-end. One study that corroborates the effect of different size measures is the PricewaterhouseCoopers study.[6] The PricewaterhouseCoopers study focused on different measures of size and calculated size premia using these different measures. The measures of size considered by the study are market value of equity, book value of equity, five-year average net income, market value of invested capital, total assets, five-year average EBITDA, sales, and number of employees. This study is updated annually and now sold as the Duff & Phelps, L.LC. Risk Premium Report.[7]

Other Criticisms of the Size Premium

Financially Distressed Companies

Traditionally, Morningstar has not cleansed our size premium data, as published in the SBBI Valuation Yearbook, from the impact of financially distressed firms. Recently, Morningstar's valuation research team reexamined the value of removing distressed companies from the portfolios we use to construct our size premia. Using a measure for identifying distressed (high risk) companies called Distance to Default, we performed a study in conjunction with the Center for Research in Security Prices (CRSP) at the University of Chicago Booth School of Business. This study took well over a year to design, execute, and study.

Major U.S. Stock-Market Indexes

MARKETS DASHBOARD

WSJMarkets.com

	LATEST WEEK					52-WEEK RANGE				% CHG	
	High	Low	Close	Net chg	% chg	Low	Close (●)	High	% chg	YTD	3-yr. ann.
Dow Jones											
Industrial Average	14546.82	14382.09	14512.03	-2.08	-0.01	12101.46		14539.14	10.9	10.7	10.4
Transportation Avg	6291.65	6090.61	6179.26	-93.41	-1.49	4847.73		6281.24	18.4	16.4	12.1
Utility Average	498.91	491.58	497.36	2.18	0.44	438.05		498.09	9.9	9.8	9.4
Total Stock Market	16472.50	16224.33	16412.49	-47.48	-0.29	13329.32		16490.33	12.0	9.7	10.6
Barron's 400	407.90	400.44	405.88	-1.02	-0.25	321.50		407.91	10.8	10.9	13.0
Nasdaq Stock Market											
Nasdaq Composite	3257.99	3205.42	3245.00	-4.07	-0.13	2747.48		3258.93	5.8	7.5	10.65
Nasdaq 100	2811.48	2763.12	2800.81	1.40	0.05	2458.83		2864.03	2.6	5.3	12.8
Standard & Poor's											
500 Index	1561.56	1538.57	1556.89	-3.81	-0.24	1278.04		1563.23	11.4	9.2	10.1
MidCap 400	1146.94	1126.41	1139.67	-2.16	-0.19	891.32		1145.88	15.0	11.7	12.8
SmallCap 600	531.73	523.44	528.62	-3.11	-0.58	414.87		531.73	14.4	10.9	13.2
Other Indexes											
Russell 2000	952.46	936.73	946.27	-6.21	-0.65	737.24		953.0675	14.0	11.4	11.5
NYSE Composite	9094.27	8968.39	9065.80	-50.88	-0.56	7285.53		9127.9721	10.8	7.4	6.9
Value Line	408.80	402.07	405.94	-1.99	-0.49	323.50		408.57	9.7	10.4	6.6
NYSE Arca Biotech	1801.63	1758.86	1791.65	-6.47	-0.36	1320.31		1811.3935	33.7	15.8	13.3
NYSE Arca Pharma	407.73	399.42	407.25	2.81	0.69	322.03		407.2452	20.5	10.2	9.4
KBW Bank	57.37	56.36	56.62	-0.90	-1.56	41.00		57.52	14.3	10.4	3.1
PHLX§ Gold/Silver	138.23	133.92	136.96	2.50	1.86	128.89		195.20	-22.7	-17.3	-6.3
PHLX§ Oil Service	248.88	235.79	239.58	-10.08	-4.04	186.27		255.88	-0.8	8.8	5.5
PHLX§ Semiconductor	432.94	422.90	430.08	-4.10	-0.94	351.45		441.88	-1.3	12.0	5.7
CBOE Volatility	15.40	12.30	13.57	2.27	[illegible]	11.30		26.66	-8.4	-24.7	-7.0

§Philadelphia Stock Exchange

Sources: **SIX Financial Information;** WSJ Market Data Group

EXHIBIT
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ADMITTED

MARKETS DASHBOARD

WSJMarkets.com

Corporate Borrowing Rates and Yields

Bond total return index	YIELD (%)		SPREAD +/- TREASURYS, in basis pts, 52-WK RANGE			TOTAL RETURN	
	Last	Wk ago	Last	Low	High	52-wk	3-yr
10-yr Treasury, Ryan ALM	1.91	1.998				6.10	9.16
DJ Corporate	2.58	2.592				7.88	8.35
Aggregate, Barclays Capital	1.88	1.910	54	45	87	3.88	5.3
High Yield 100, Merrill Lynch	4.80	4.70	410.00	388.00	707.00	12.28	10.63
Fixed-Rate MBS, Barclays	2.59	2.610	58	13	95	2.00	4.0
Muni Master, Merrill	1.78	1.81	17.00	16.00	33.00	4.74	5.65
EMBI Global, J.P. Morgan	4.95	4.90	300.00	245.00	475.00	10.32	10.55

Sources: J.P. Morgan; Ryan ALM; S&P Dow Jones Indices; Barclays Capital; Merrill Lynch

EXHIBIT
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The Size Study

The January Effect

The "January effect" is the empirical observation that rates of return for small-cap stocks have on the average tended to be greater in January than in the other months of the year. The existence of a January effect, however, does not necessarily present a challenge to the size effect unless it can be established that the effect is the result of a bias in the measurement of returns.

Some academics have speculated that the January effect may be due to a bias related to tax-loss selling. Investors who have experienced a loss on a security may be motivated to sell their shares shortly before the end of December. An investor makes such a sale in order to realize the loss for income tax purposes. This tendency creates a preponderance of sell orders for such shares at year-end. If this is true, then (1) there may be some temporary downward pressure on prices of these stocks, and (2) the year-end closing prices are likely to be at the bid rather than at the ask price. The prices of these stocks will then appear to recover in January when trading returns to a more balanced mix of buy and sell orders (i.e., more trading at the ask price).

Such "loser" stocks will have temporarily depressed stock prices. This creates the tendency for such companies to be pushed down in the rankings when size is measured by market value. At the same time, "winner" stocks may be pushed up in the rankings when size is measured by market value. Thus, portfolios composed of small-cap companies tend to have more losers in December, with the returns in January distorted by the tax-loss selling. A recent study finds that the January returns are smaller after 1963–1979 but have reverted to levels that appear before that period.[104] More important, they find that trading volume for small-cap companies in January does not differ from other months. They conclude that the January effect continues.

This argument vanishes if you use a measure other than market value (e.g., net income, total assets, or sales) to measure size because a company's fundamental size does not change in December because of tax loss selling. The size effect is evident in the *Duff & Phelps Size Study* using size measures other than market capitalization.

Is the Size Effect a Proxy for "Liquidity"?

Banz's 1981 musing as to whether *"...size* per se *is responsible for the effect or whether size is just a proxy for one or more true unknown factors correlated with size"* may have been cannily prescient. Research on returns as related to "size" is abundant, but over time a growing body of work investigating the impact of "liquidity" on returns has emerged. As early as 1986, Amihud and Mendelson, demonstrated that "...market-observed average returns are an increasing function of the spread..." (i.e., less liquid stocks, as measured by a larger bid-ask spread, outperform more liquid stocks), and further concluded that the "...higher yields required on higher-spread stocks give firms an incentive to increase the liquidity of their securities, thus reducing their opportunity cost of capital".[105]

Recent research by Abbot and Pratt suggests that the "...difference between mean returns on size sorted portfolios is considerably smaller than the difference between mean returns on liquidity sorted portfolios", implying that between size and liquidity (as measured by a natural log transformation of stock turnover), "...liquidity may be the dominant factor in asset pricing."[106]

Ibbotson, Chen, and Hu suggest that while the typical measures of liquidity employed in the literature are each "...highly correlated with company size", they demonstrate that liquidity, as measured by annual stock turnover, "...is an economically significant investment style that is just as strong, but *distinct* from traditional investment styles such as size, value/growth, and momentum" [emphasis added].[107] The authors go on to say that "...there is an incremental return from investing in less liquid stocks even after adjusting for the market, size, value/growth, and momentum factors", and conclude that "...equity liquidity is the missing equity style."

Ibbotson, Chen, and Hu identify two main sources of the greater returns of less liquid stocks. The first is that "investors like liquidity and dislike illiquidity", and "...a premium has to be paid for any characteristic that investors demand, and a discount must be given for any characteristic investors seek to avoid". Thus, "...the investor in less liquid stocks gets lower valuations, effectively buying stocks at a discount."

EXHIBIT
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A-15
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[104] Kathryn E. Easterday, Pradyot K. Sen, and Jens A. Stephan, "The Persistence of the Small Firm/January Effect: Is It Consistent with Investors' Learning and Arbitrage Efforts?" Working paper, June 2007. Available at [illegible]

[105] Amihud, Yakov and Haim Mendelson, 1986, "Asset Pricing and the Bid-Ask Spread," *Journal of Financial Economics* 17, 223-249.

[106] Ashok Abbott and Shannon Pratt. "Does Liquidity Masquerade as Size", working paper, 2012.

[107] Roger G. Ibbotson, Zhiwu Chen, and Wendy Y. Hu, "Liquidity as an Investment Style", Yale Working Paper, April 2011. Copy available at www.zebracapital.com

Liberty Utilities℠

28 March 2013
Revision 1
Rio Rico Utilities, Inc. dba Liberty Utilities
Docket No. WS-02676A-12-0196
Water

	Prior to Resolution	Post Resolution
Rate Base Adjustments		
(Rate Base Numbers are RRUI Rejoinder Amounts)		
Utility Plant In-Service	$34,455,296	In progress
Accumulated Depreciation	$13,756,125	In progress
Net Utility Plant	$20,699,171	In progress
Advances in Aid of Construction	$660,955	$660,955
Contributions in Aid of Construction	$20,179,119	$20,179,119
Contributions in Aid of Construction – Amort.	$8,617,752	$8,617,752
Customer Meter Deposits	$284,084	$284,084
ADIT	$462,717	$462,717
Total Rate Base	$7,730,108	In progress
Operating Income Adjustments		
Staff Direct Testimony Adjustment No.3 (Depreciation Expense)	($173,736)	(~~$109,788~~) In Progress
Staff Direct Testimony Adjustment No. 4 (Corporate Costs)	($38,083)	($32,583)
RRUI Rebuttal Testimony Adjustment No. 3 (Declining Usage Adjustment)	($77,275) [Revenue Reduction]	$0
RRUI Rebuttal Testimony Adjustment No. 6 (Purchased Power)	$17,083	$0
RRUI Rebuttal Testimony Adjustment No. 9 (Employee Benefits)	$32,891	$32,891
Rate Design	In progress	In progress

EXHIBIT
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~~ADMITTED~~

Liberty Utilities

28 March 2013
Revision 1
Rio Rico Utilities, Inc. dba Liberty Utilities
Docket No. WS-02676A-12-0196
Wastewater

	Prior to Resolution	Post Resolution
Rate Base Adjustments		
(Rate Base Numbers are RRUI Rejoinder Amounts)		
Utility Plant In-Service	$12,655,367	In progress
Accumulated Depreciation	$4,658,438	In progress
Net Utility Plant	$7,996,929	In progress
Advances in Aid of Construction	$293,794	$293,794
Contributions in Aid of Construction	$5,152,673	$5,152,673
Contributions in Aid of Construction – Amort.	$2,491,137	$2,491,137
Customer Meter Deposits	$22,963	$22,963
ADIT	$283,444	$283,444
Total Rate Base	$4,735,192	In progress
Operating Income Adjustments		
Staff Direct Testimony Adjustment No. 3 (Depreciation Expense)	($135,855)	~~($155,665)~~ In progress
Staff Direct Testimony Adjustment No. 4 (Corporate Costs)	($27,931)	($22,431)
RRUI Rebuttal Testimony Adjustment No. 3 (Declining Usage Adjustment)	($32,713) [Revenue Reduction]	$0
RRUI Rebuttal Testimony Adjustment No. 6 (Purchased Power)	$2,819	$0
RRUI Rebuttal Testimony Adjustment No.10 (Employee Benefits)	$11,811	$11,811
Rate Design		In progress

Liberty Utilities

EXHIBIT
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ADMITTED

29 March 2013
Revision 2
Rio Rico Utilities, Inc. dba Liberty Utilities
Docket No. WS-02676A-12-0196
Water

	Prior to Resolution	Post Resolution
Rate Base Adjustments		
(Rate Base Numbers are RRUI Rejoinder Amounts)		
Utility Plant In-Service	$34,455,296	$34,454,989
Accumulated Depreciation	$13,756,125	$13,754,657
Net Utility Plant	$20,699,171	$20,700,332
Advances in Aid of Construction	$660,955	$660,955
Contributions in Aid of Construction	$20,179,119	$20,179,119
Contributions in Aid of Construction – Amort.	$8,617,752	$8,617,752
Customer Meter Deposits	$284,084	$284,084
ADIT	$462,717	$462,717
Total Rate Base	$7,730,108	$7,731,209
Operating Income Adjustments		
Staff Direct Testimony Adjustment No.3 (Depreciation Expense)	($173,736)	($109,768)
Staff Direct Testimony Adjustment No. 4 (Corporate Costs)	($38,083)	($32,583)
RRUI Rebuttal Testimony Adjustment No. 3 (Declining Usage Adjustment)	($77,275) [Revenue Reduction]	$0
RRUI Rebuttal Testimony Adjustment No. 6 (Purchased Power)	$17,083	$0
RRUI Rebuttal Testimony Adjustment No. 9 (Employee Benefits)	$32,891	$32,891[1], [2]
RUCO Rejoinder Testimony Adjustment No. 11 (Incentive Compensation)	($19,997)	$0
RUCO Rejoinder Testimony Adjustment No. 3 (Rate Case Amortization)	($21,875)	$0
Rate Design		Accept Staff's[3]

[1] RRUI agreed to an accounting order authorizing the Company to create a regulatory liability account in order to track any amounts paid that are lower than amounts authorized in rates between now and RRUI's next rate application.
[2] RRUI agreed to file as a compliance item in the docket evidence that payments have been made relative to the plan.
[3] Staff and the Company are discussing the creation of a separate rate tariff for the School District and will reach an agreed resolution and include in the final schedules.

29 March 2013
Revision 2
Rio Rico Utilities, Inc. dba Liberty Utilities
Docket No. WS-02676A-12-0196
Wastewater

	Prior to Resolution	Post Resolution
Rate Base Adjustments		
(Rate Base Numbers are RRUI Rejoinder Amounts)		
Utility Plant In-Service	$12,655,367	$12,751,357
Accumulated Depreciation	$4,658,438	$4,698,882
Net Utility Plant	$7,996,929	$8,052,475
Advances in Aid of Construction	$293,794	$293,794
Contributions in Aid of Construction	$5,152,673	$5,152,673
Contributions in Aid of Construction – Amort.	$2,491,137	$2,491,137
Customer Meter Deposits	$22,963	$22,963
ADIT	$283,444	$283,444
Total Rate Base	$4,735,192	$4,790,738
Operating Income Adjustments		
Staff Direct Testimony Adjustment No. 3 (Depreciation Expense)	($135,855)	($135,855)
Staff Direct Testimony Adjustment No. 4 (Corporate Costs)	($27,931)	($22,431)
RRUI Rebuttal Testimony Adjustment No. 3 (Declining Usage Adjustment)	($32,713) [Revenue Reduction]	$0
RRUI Rebuttal Testimony Adjustment No. 6 (Purchased Power)	$2,819	$0
RRUI Rebuttal Testimony Adjustment No.10 (Employee Benefits)	$11,811	$11,811
RUCO Rejoinder Testimony Adjustment No. 11 (Incentive Compensation)	($9,448)	$0
RUCO Rejoinder Testimony Adjustment No. 3 (Rate Case Amortization)	($7,292)	$0
RUCO Rejoinder Testimony Adjustment No. 13 (Nogales Monthly WWTP Expense)	$0	($56,897)[4]
Rate Design		Accept Staff's

[4] RRUI and RUCO agreed that RRUI should be authorized an accounting deferral order allowing RRUI to create regulatory asset and liability accounts to track monthly changes in payments made to the City of Nogales between now and RRUI's next rate application.

Rio Rico Utilities, Inc. dba Liberty Utilities

Exhibit TJB-COC-RJ2
Revised

Table 1 – Staff Recommendations and Actual Equity in Capital Structure

[1]	Total Equity per Direct Schedule D-1	$13,493,513
[2]	% Equity per Rejoinder D-1	100%
[3]	Book Value of Equity [1] x[2]	$13,493,513
[4]	Expected Dividend Yield per Staff	3.10%
[5]	Current market-to-book ratio publicly traded water utilities	2.28
[6]	Book Value Dividend Yield [4] x [5]	7.07%
[7]	Cash Dividend [3] x[6]	$953,721
[8]	Staff Recommended Operating Income (W and WW)	$1,013,480
[9]	Less: Annual Interest Expense	$0
[10]	Earnings Available for Dividends [8] - [9]	$1,013,480
[11]	Less: Dividends [7]	$953,721
[12]	Retained Earnings [10] - [11]	$59,759
[13]	Pay-out ratio [11]/[10]	94%

Table 2 – RUCO Recommendations and Actual Equity in Capital Structure

[1]	Total Equity per Direct Schedule D-1	$13,493,513
[2]	% Equity per Rejoinder D-1	100%
[3]	Book Value of Equity [1] x[2]	$13,493,513
[4]	Expected Dividend Yield per RUCO	3.07%
[5]	Current market-to-book ratio publicly traded water utilities	2.28
[6]	Book Value Dividend Yield [4] x [5]	7.00%
[7]	Cash Dividend [3] x[6]	$944,492
[8]	RUCO Recommended Operating Income (W and WW)	$1,010,331
[9]	Less: Annual Interest Expense	$0
[10]	Earnings Available for Dividends [8] - [9]	$1,010,331
[11]	Less: Dividends [7]	$944,492
[12]	Retained Earnings [10] - [11]	$65,839
[13]	Pay-out ratio [11]/[10]	93%

Table 3 – RRUI Recommendations and Actual Equity in Capital Structure

[1]	Total Equity per Direct Schedule D-1	$13,493,513
[2]	% Equity per Rejoinder D-1	100%
[3]	Book Value of Equity [1] x[2]	$13,493,513
[4]	Expected Dividend Yield per D-4.7	2.75%
[5]	Current market-to-book ratio publicly traded water utilities	2.28
[6]	Book Value Dividend Yield [4] x [5]	6.27%
[7]	Cash Dividend [3] x[6]	$846,043
[8]	RRUI Recommended Operating Income (W and WW)	$1,184,203
[9]	Less: Annual Interest Expense	$0
[10]	Earnings Available for Dividends [8] - [9]	$1,184,203
[11]	Less: Dividends [7]	$846,043
[12]	Retained Earnings [10] - [11]	$338,160
[13]	Pay-out ratio [11]/[10]	71%

EXHIBIT
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ADMITTED