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STATE OF ALASKA

THE REGULATORY COMMISSION OF ALASKA

Before Commissioners:

Kate Giard, Chairman  
Dave Harbour  
Mark K. Johnson  
Anthony A. Price  
James S. Strandberg

In the Matter of the Tariff Revisions, Designated )  
as TA91-126 and TA96-126, Filed by the )  
MUNICIPALITY OF ANCHORAGE d/b/a )  
ANCHORAGE WATER & WASTEWATER )  
UTILITY, for Its Wastewater Division, for Interim )  
and Permanent Rate Relief )

U-04-22  
ORDER NO. 16

In the Matter of the Tariff Revisions, Designated )  
as TA96-122 and TA100-122, Filed by the )  
MUNICIPALITY OF ANCHORAGE d/b/a )  
ANCHORAGE WATER & WASTEWATER )  
UTILITY, for Its Water Division, for Interim and )  
Permanent Rate Relief )

U-04-23  
ORDER NO. 16

**ORDER ESTABLISHING REVENUE REQUIREMENT  
AND REQUIRING FILINGS**

BY THE COMMISSION:

Summary

We deny the request by AWWU<sup>1</sup> to include the Municipal Utility Services Assessment (MUSA) on contributed plant in AWWU's revenue requirement. We require AWWU to submit a calculation of the refund due to ratepayers as a result of this decision and a timeline indicating when the refund process will be complete. We

<sup>1</sup>Municipality of Anchorage d/b/a Anchorage Water and Wastewater Utility.

1 continue the suspension of TA91-126, TA96-126, TA96-122 and TA100-122. We  
2 require AWWU to submit new tariff sheets reflecting this decision.

3 Background

4 We scheduled a hearing regarding AWWU's request for permanent rate  
5 relief.<sup>2</sup> AWWU and the Attorney General (AG) resolved all issues except those related  
6 to the MUSA.<sup>3</sup> The hearing convened on June 14, 15, and 16, 2005. AWWU presented  
7 the testimony of Jeffrey E. Sinz, Chief Fiscal Officer; Don Martin McGee, Municipal  
8 Assessor; Mark Premo, General Manager; Sharon Weddleton, Finance Division  
9 Manager; and Daniel L. Watsjold, Regulatory Affairs Supervisor, Finance Division. The  
10 AG presented the testimony of Ralph C. Smith, consultant.

11 Discussion

12 The only disputed issue in these proceedings is whether AWWU should  
13 be permitted to include its MUSA on contributed plant in consumer rates. AWWU bears  
14 the burden of proving that its proposed rates are just and reasonable and should be  
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17 <sup>2</sup>Order U-04-22(8)/U-04-23(8), *Order Affirming Electronic Rulings Denying Motion*  
18 *to Strike and Granting, In Part, the Motion to Modify Procedural Schedule; Granting*  
19 *Motion for Expedited Consideration; Affirming Electronic Ruling Conditionally Granting*  
20 *Unopposed Motion to Reschedule Hearing Date; Denying Motion for Leave to File*  
21 *Response; Affirming Electronic Rulings Modifying Remainder of Procedural Schedule;*  
22 *Denying Motion for Expedited Consideration; Granting, In Part, Motion for Subpoena*  
23 *Duces Tecum; Denying Request for Costs; and Granting Request for Order Governing*  
24 *Confidential Discovery Material; Affirming Electronic Ruling Denying Motion for*  
25 *Expedited Consideration; Finding Moot the Motion for Extension of Time to Respond to*  
26 *Petition for Reconsideration; and Holding in Abeyance Petitions for Partial*  
*Reconsideration, dated January 28, 2005.*

<sup>3</sup>On June 8, 2005, we issued an electronic ruling granting the request of the parties to limit the issues at hearing to MUSA because the parties had reached a stipulation on all other disputed issues. MUSA is a payment in lieu of taxes assessed by the Municipality of Anchorage (Municipality) to its utility operations.

1 approved. We find that AWWU did not meet its burden of proof and therefore is not  
2 permitted to include the MUSA on contributed plant in consumer rates.

3           The Municipality changed the way it assesses MUSA, through a municipal  
4 ordinance that assesses MUSA on contributed plant. AWWU seeks to recover these  
5 increased assessments in rates.<sup>4</sup> AWWU attempts to recover the increased payments  
6 in lieu of taxes in a two-stage rate increase, which reflects the Municipality Assembly's  
7 desire to phase the increased payments in lieu of taxes.<sup>5</sup>

8           We considered and approved a petition by AWWU to allow the MUSA  
9 charge in rates on an interim and refundable basis in Orders U-04-22(1)/U-04-23(1) and  
10 Order U-04-22(12)/U-04-23(12).<sup>6</sup> AWWU's rate payers are thus paying this increased  
11 amount, and our decision in this Order will determine whether the MUSA charge on  
12 contributed plant will be permanently allowed in rates.

13           The AG opposes the inclusion of MUSA in consumer rates on several  
14 grounds. The AG cites two previous orders we have issued, Orders U-88-18(14)<sup>7</sup> and  
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17 <sup>4</sup>T-3, at 4; T-4, at 4.

18 <sup>5</sup>*Id.*

19 <sup>6</sup>Order U-04-22(1)/U-04-23(1), *Order Suspending Tariff Filing; Granting Interim*  
20 *and Refundable Rate Revisions; and Appointing Hearing Examiner*, dated February 20,  
21 2004. Order U-04-22(12)/U-04-23(12), *Order Denying Petition for Reconsideration*  
22 *Regarding Subpoena Duces Tecum and Granting Request for Interim Rate Relief*, dated  
23 February 18, 2005.

24 <sup>7</sup>*Order Addressing Revenue Requirement and Other Issues and Requiring*  
25 *Further Filings*, dated May 1, 1989.

26           Docket U-88-18 is titled *In the Matter of the Filing of Tariff Revisions, Designated*  
as TA207-120, as Supplemented, TA209-120, TA218-120, and TA216-120, by the  
MUNICIPALITY OF ANCHORAGE d/b/a ANCHORAGE TELEPHONE UTILITY for an  
Interim and Permanent Rate Increase, for the Furnishing of Integrated Business  
Services, and for a Local Directory Assistance Charge, Respectively.

1 U-89-2(2),<sup>8</sup> as Commission precedent on the issue of whether MUSA on contributed  
2 plant should be allowed in rates. The AG argues that these two orders provide clear  
3 precedent that MUSA on contributed plant should not be allowed in rates.<sup>9</sup>

4 The AG asserts that we should reach the same conclusion now which we  
5 reached in Order U-89-2(2), that the portion of MUSA on contributed plant is an equity  
6 distribution by the Municipal utilities to the Municipality and, therefore should be treated  
7 as a dividend.<sup>10</sup>

8 AWWU's arguments seek to justify the appropriateness of taxing both  
9 contributed and non-contributed plant through concepts of equity between municipally-  
10 owned utilities and privately-owned utilities.<sup>11</sup> AWWU offers extensive argument on the  
11 concepts of taxation of utilities to reasonably contribute to the cost of municipal  
12 government that are made available to the general public, including AWWU.<sup>12</sup> AWWU  
13 concludes with assertions that MUSA should be increased to make it comparable to the  
14 amount of MUSA being paid by other municipal utilities and the amount of property  
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17 <sup>8</sup>*Order Approving, With Modifications, Rules and Regulations Portion of*  
18 *TA13-195; Approving Tariff Sheet No. 23 for Revised Labor Charges; Suspending*  
19 *Operation of TA13-195; Approving Medical Waste Rate Provisions on an Interim*  
20 *Refundable Basis; Affirming Bench Order Granting Interim Rate Increase; Consolidating*  
*Docket U-89-2 for Consideration with TA13-195; Reestablishing Filing Schedules in*  
*Docket U-89-2; Establishing Hearing and Filing Schedules; and Appointing Hearing*  
*Officer, dated April 17, 1989.*

21 Docket U-89-2 is titled *In the Matter of the Filing of a Tariff Revision, Designated*  
22 *as TA12-195, by CHANNEL SANITATION CORPORATION to Add a New Service for*  
*Collection and Disposal of Medical Waste.*

23 <sup>9</sup>T-11, at 11, L 23-25; at 12, L 16-18.

24 <sup>10</sup>T-11, at 18.

25 <sup>11</sup>T-1, at 4-5.

26 <sup>12</sup>T-1, at 13.

1 taxes being paid by privately-owned entities and finally to provide a reasonable  
2 contribution to the cost of providing municipal services.<sup>13</sup>

3 Private utilities pay taxes which they are permitted to recover through their  
4 revenue requirements. However, private utilities do not have any control over the taxing  
5 authority. In this case, the water utility and wastewater utilities are enterprise funds of  
6 the Municipality; the Municipality is doing business as the water and wastewater  
7 utilities.<sup>14</sup> The annual budget and strategic plans of the utilities must be submitted to the  
8 Anchorage Assembly and Mayor for approval.<sup>15</sup> The Municipality is also the entity that  
9 determined it should change the formula regarding the calculation of payments in lieu of  
10 taxes or MUSA that it charges itself in the operation of its utilities.

11 We are required to closely scrutinize affiliated interest transactions with  
12 utilities<sup>16</sup> to ensure that ratepayers are not charged a greater amount had the utility  
13 engaged in an arm's length transaction. In this case, we are evaluating an even closer  
14 relationship; one where the taxing authority and the utilities are one and the same.<sup>17</sup>

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17 <sup>13</sup>T-1, at 15.

18 <sup>14</sup>Tr. 163; Tr. 273.

19 <sup>15</sup>Tr. 273.

20 <sup>16</sup>AS 42.05.511(c) states: In a rate proceeding the utility involved has the burden  
21 of proving that any written or unwritten contract or arrangement it may have with any of  
22 its affiliated interests for the furnishing of any services or for the purchase, sale, lease,  
23 or exchange of any property is necessary and consistent with the public interest and  
24 that the payment made therefore, or consideration given, is reasonably based, in part,  
upon the submission of satisfactory proof as to the cost to the affiliated interest of  
furnishing the service or property and, in part, upon the estimated cost the utility would  
have incurred if it furnished the service or property with its own personnel and capital.

25 <sup>17</sup>Municipality of Anchorage d/b/a Anchorage Water and Wastewater Utility -  
26 Certificate of Public Convenience and Necessity No. 122 and No. 126, respectively.

1 Such a relationship must be carefully evaluated to ensure that ratepayers are charged  
2 just, fair, and reasonable rates.<sup>18</sup>

3 AWWU's Current MUSA Request

4 In 2003, the Municipality enacted Municipal Ordinance No. AO 2003-  
5 160.<sup>19</sup> This ordinance amended the formula for calculating MUSA and repealed the  
6 exemption from calculation of contributed plant enacted through the 1988 MUSA  
7 ordinance.<sup>20</sup> AWWU asserted that the rationale for the change was inconsistent with  
8 the treatment of other municipally-owned utilities and privately-owned utilities.<sup>21</sup> AWWU  
9 states that calculating the MUSA using the net total plant of each municipally-owned  
10 utility produces a consistent basis for the MUSA calculation.<sup>22</sup>

11 AWWU has a relatively high concentration of contributed plant in its capital  
12 structure.<sup>23</sup> During the relevant test year, state and federal government contributions-in-  
13 aid-of construction were \$172,339,302 for the water utility and \$132,339,537 for the  
14 wastewater utility.<sup>24</sup> If the proposed modification in the MUSA formula is adopted, the  
15 MUSA rate would approximately triple.<sup>25</sup>

16 The overall 2004 revenue requirement for the water utility after a 14.20  
17 percent rate increase is \$34,643,810; the overall 2005 revenue requirement after an  
18 additional 7.17 percent rate increase is \$36,746,483; and the MUSA adjustment is

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19 <sup>18</sup>AS 42.05.381.

20 <sup>19</sup>T-1, at 3.

21 <sup>20</sup>*Id.*

22 <sup>21</sup>T-1, at 3-4.

23 <sup>22</sup>T-1, at 4.

24 <sup>23</sup>Tr. 138; T-1, JES-2, at 2.

25 <sup>24</sup>Tr. 303-304.

26 <sup>25</sup>Tr. 145; T-1, at 5.

1 \$3,397,359.<sup>26</sup> The overall 2004 revenue requirement for the wastewater utility after a  
2 8.06 percent rate increase is \$27,409,886; the overall 2005 revenue requirement after  
3 an additional 6.83 percent rate increase is \$29,064,278, and the MUSA adjustment is  
4 \$2,679,996.<sup>27</sup> Over \$6 million of the total \$10 million revenue requirement increases  
5 requested are the result of revision of the MUSA formula.<sup>28</sup>

6 Precedent on Contributed Plant MUSA

7 We addressed the assessment of MUSA in Order U-88-18(14). In that  
8 decision, we determined that:

9 [T]he amount of MUSA which should be allowed for ratemaking purposes  
10 should be computed on the same property which is allowed in rate base, and  
that no MUSA should be allowed on property excluded from rate base.<sup>29</sup>

11 In that case, certain plant was excluded from rate base because it was  
12 excess capacity that was not “used and useful” in providing utility service. The  
13 Commission determined that if the plant was excluded from rate base, no MUSA could  
14 be assessed on the plant.  
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17 <sup>26</sup>Tr. 296-297, H-7, H-15.

18 <sup>27</sup>H-8, H-16, Tr. 298-299.

19 <sup>28</sup>T-11, at 11.

20 <sup>29</sup>That Order was issued as a part of a joint decision published as Order  
U-88-18(14)/U-87-61(9)/U-88-9(8), *Order Addressing Revenue Requirement and Other  
21 Issues and Requiring Further Filings*, dated May 1, 1989.

22 Docket U-87-61 is titled *In the Matter of the Consideration of the Financial  
Practices and Condition of the MUNICIPALITY OF ANCHORAGE d/b/a ANCHORAGE  
23 TELEPHONE UTILITY*.

24 Docket U-88-9 is titled *In the Matter of the Filing of a Tariff Revision, Designated  
as TA206-120, by the MUNICIPALITY OF ANCHORAGE d/b/a ANCHORAGE  
25 TELEPHONE UTILITY to Provide Integrated Business Service to UNTIED UTILITIES,  
INC. by Special Contract*.  
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The Commission upheld that position in a later case as follows:  
[T]he portion of the MUSA payment calculated as an assessment against the net book value of utility plant, **excluding contributed plant**, is reasonable. (Emphasis added.)<sup>30</sup>

AWWU asserts in these current proceedings that contributed plant should be included in the calculation because it requires municipal services to the same extent and in the same manner as non-contributed plant.<sup>31</sup> However, AWWU stated that an increase in MUSA payments need not be accompanied by an increase in municipal services.<sup>32</sup>

The “source” of utility plant is an important consideration for ratemaking purposes. If the utility did not expend any funds to acquire plant, it is contributed plant that is not included in a utility’s rate base.<sup>33</sup> A utility is not permitted to earn a return on that plant and a utility does not accumulate depreciation on that plant.<sup>34</sup> AWWU stated that the “source” of plant is an important consideration for regulatory purposes but asserted that it is irrelevant to tax assessment officials.<sup>35</sup> The AG asserted that if plant is excluded from rate base, then a corresponding adjustment should be made to exclude the MUSA associated with the plant.<sup>36</sup> We fail to see how AWWU’s current request is distinguishable from our precedent established in our earlier Order

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<sup>30</sup>*Re Municipality of Anchorage d/b/a/ Municipal Light and Power Department, Anchorage Sewer Utility, Anchorage Telephone Utility, and Anchorage Water Utility, 9 APUC 442, 444 (1989).*

<sup>31</sup>T-1, at 6-7.

<sup>32</sup>T-1, at 13.

<sup>33</sup>Tr. 314.

<sup>34</sup>*Id.*

<sup>35</sup>Tr. 174.

<sup>36</sup>Tr. 313-314; T-11, at 14 and RCS-4; Order U-88-18(14).



1 U-88-18(14) and Order U-89-2(2). We thus follow our precedent to deny inclusion of  
2 MUSA on contributed plant in rates despite AWWU's argument to the contrary.

3 Regulatory Treatment of Proposed MUSA on Contributed Plant

4 In the earlier cases, AWWU followed appropriate ratemaking procedures  
5 and excluded contributions-in-aid-of construction from its calculation of rate base.  
6 AWWU asserted here that MUSA should be allowed on this property but failed to  
7 demonstrate why property excluded from rate base should be assessed MUSA. The  
8 primary distinction between this case and the prior proceedings is the enactment of a  
9 new municipal ordinance that lifts the exemption from MUSA for contributed property.

10 The Municipality has the authority to enact ordinances it deems  
11 appropriate. We do not reach any conclusion on the evidence in the record about the  
12 new ordinance. Instead, because we have an obligation to regulate utilities under our  
13 jurisdiction and ensure that ratepayers are charged just and reasonable rates, we view  
14 the evidentiary record under our regulatory standards. We have previously noted that:

15 In performing that regulatory role the Commission may, at times, issue orders  
16 or regulations that are in conflict with ordinances of the Municipality, and in  
17 those instances the order or regulation of the Commission prevails.  
AS 42.05.641.<sup>37</sup>

18 In these proceedings, AWWU has failed to demonstrate that it is  
19 reasonable to burden ratepayers with costs associated with property properly excluded  
20 from rate base under our regulatory standards. We find that our well established  
21 rate-making principals regarding the exclusion of MUSA on contributed plant prevails  
22 over the Municipality's recently enacted ordinance regarding its treatment of MUSA.

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<sup>37</sup> See n.30.  
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1 AWWU's Tax Equity Argument

2 We next address the “tax equity” argument presented by AWWU. AWWU  
3 asserted that the revised MUSA would place AWWU in the same position as private  
4 utilities.<sup>38</sup> The AG argued that the Municipality does not collect property taxes on the  
5 contributed property of other utilities.<sup>39</sup>

6 In 1989, the Municipality asserted that it was attempting to remedy the tax  
7 inequity between municipal and private utilities by limiting MUSA to non-contributed  
8 plant.<sup>40</sup> AWWU now states that we need to reverse that position in order to achieve  
9 equitable treatment between municipal and private utilities. The AG presents the most  
10 persuasive argument on this issue. Significantly, the same argument was initially  
11 presented by the Municipality in 1989, as follows:

12 [T]he general theory behind exclusion of contributed plant is that contributed  
13 plant is not entitled to earn a rate of return, and therefore has zero market  
14 value. This is true for all utilities, public or private. Because net book value  
15 is used as a proxy for assessed valuations in determining MUSA, it is logical  
16 if the market value is zero, then the assessed value would also be zero.  
(T-11, RCS-7.)

16 The same reasoning applies today. General ratemaking principles provide  
17 that a utility is permitted to earn a rate of return on its rate base. If plant is excluded  
18 from rate base, the utility does not earn a rate of return on that plant. Here, AWWU  
19 properly excluded contributed plant from its rate base. The exclusion means for  
20 ratemaking purposes, that the plant has zero market value. If the plant has zero market  
21 value, then it must also have zero assessed value. Therefore, we further conclude that  
22 MUSA should not be assessed on contributed plant.

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24 <sup>38</sup>T-1, at 3-4.

25 <sup>39</sup>T-11, at 12.

26 <sup>40</sup>T-11, RCS-7; T-11 at 14.

1 The AG's Dividend Argument

2           The AG asserted that the MUSA is a dividend from AWWU to the  
3 Municipality.<sup>41</sup> The AG stated that a dividend is a payment by a corporation to its  
4 owners.<sup>42</sup> The AG asserted that an additional payment by AWWU to the Municipality  
5 without the receipt of additional services has the characteristics of a dividend  
6 payment.<sup>43</sup> According to the AG, if the Commission concludes that the proposed MUSA  
7 is a dividend, AWWU cannot pay the MUSA to the Municipality because of the dividend  
8 restriction.<sup>44</sup>

9           AWWU maintained that MUSA is not a dividend.<sup>45</sup> AWWU asserted that a  
10 dividend is a distribution of earnings and that the MUSA assessments in these  
11 proceedings are not related to earnings.<sup>46</sup>

12           The Commission established a hypothetical capital structure of 65/35 for  
13 AWWU approximately 17 years ago and imposed a dividend restriction until AWWU  
14 achieved an actual capital structure at approximately the same levels.<sup>47</sup> AWWU's  
15 current debt/equity ratio is approximately 65/35 for its water operations and 70/30 for its  
16 wastewater operations; however, AWWU is not seeking to modify the hypothetical  
17 capital structure.<sup>48</sup>

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20 <sup>41</sup>T-11, at 12.

21 <sup>42</sup>T-11, at 18.

22 <sup>43</sup>T-11, at 19.

23 <sup>44</sup>Tr. 151.

24 <sup>45</sup>T-1, at 14.

25 <sup>46</sup>*Id.*

26 <sup>47</sup>Tr. 150, Tr. 170-171, Tr. 276.

<sup>48</sup>Tr. 275.

1 AWWU proposed a significant increase in the MUSA assessment; an  
2 increase of approximately triple the current MUSA assessment.<sup>49</sup> Such an increase in  
3 MUSA without any corresponding increase in service levels bears the characteristics of  
4 a dividend to the Municipality. We previously concluded that the “. . . dramatic increase  
5 in MUSA . . . with no apparent increase in Municipal service levels directly assignable to  
6 those utilities, is unsupported and unreasonable.”<sup>50</sup> We similarly conclude here that  
7 AWWU is barred, by its dividend restriction, from the payment of MUSA on its  
8 contributed plant.

9 Refunds

10 We allowed AWWU to implement rates including contributed plant on an  
11 interim and refundable basis. The exclusion of that plant in this decision will mean that  
12 ratepayers will be due a refund calculated as the difference between the interim and  
13 refundable rates and the permanent rates approved by the Commission. AWWU must  
14 submit a recalculated revenue requirement and tariff sheets reflecting the decisions in  
15 this Order and in Order U-04-22(14)/U-04-23(14).<sup>51</sup>

16 Tariff Revisions

17 TA91-126, TA96-122, TA96-126 and TA100-122 were suspended until  
18 September 15, 2005.<sup>52</sup> These tariffs will remain suspended until we have approved the  
19 revised tariffs.

21 <sup>49</sup>Tr. 145.

22 <sup>50</sup>*Re Municipality of Anchorage d/b/a/ Municipal Light and Power Department,*  
23 *Anchorage Sewer Utility, Anchorage Telephone Utility, and Anchorage Water Utility,*  
*9 APUC 442, 445 (1989).*

24 <sup>51</sup>*Order Accepting Stipulation; Subject to Conditions; and Affirming Electronic*  
*Ruling, dated July 8, 2005.*

25 <sup>52</sup>*Order Extending Suspension Period, dated July 11, 2005.*

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This Order constitutes the final decision in this proceeding. This decision is appealable within thirty days of the date of this Order in accordance with AS 22.10.020(d) and the Alaska Rules of Court, Rules of Appellate Procedure, Rule 602(a)(2). In addition to the appellate rights afforded by the aforementioned statute, a party may file a petition for reconsideration in accordance with 3 AAC 48.105. In the event such a petition is filed, the time period for filing an appeal is then calculated in accordance with Alaska Rules of Court, Rules of Appellate Procedure, Rule 602(a)(2).

**ORDER**

THE COMMISSION FURTHER ORDERS:

1. The permanent rates of the Municipality of Anchorage d/b/a Anchorage Water & Wastewater Utility shall exclude contributed plant from the calculation of the Municipal Utility Services Assessment as more fully discussed in the body of this Order.
2. By 4 p.m, September 26, 2005, the Municipality of Anchorage d/b/a Anchorage Water & Wastewater Utility shall file its recalculated revenue requirement, a refund calculation and a timeline indicating when the refund process will be complete.
3. By 4 p.m., September 26, 2005, the Municipality of Anchorage d/b/a Anchorage Water & Wastewater Utility shall file new tariff sheets reflecting the decisions in this Order and Order U-04-22(14)/U-04-23(14).

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4. TA91-126, TA96-122, TA96-126 and TA100-122 remain suspended until the revised tariffs are approved.

DATED AND EFFECTIVE at Anchorage, Alaska, this 2nd day of September, 2005.

BY DIRECTION OF THE COMMISSION  
(Commissioners Kate Giard and  
Dave Harbour, not participating.)

( S E A L )