

# *Schacht & McElroy*

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October 6, 2006

Luly Massaro, Clerk  
RI Public Utilities Commission  
89 Jefferson Boulevard  
Warwick, RI 02888

Re: Interstate Navigation Company  
Docket No. 3762

Dear Luly:

As you know, this office represents Interstate Navigation Company (Interstate).

Enclosed for filing are an original and nine copies of Interstate's responses to the 1<sup>st</sup> set of information requests of the Town of New Shoreham.

If you have any questions, please feel free to call.

Very truly yours,

  
Michael R. McElroy

MRMc:tmg

In26:06-Massarol1

cc: Susan E. Linda  
Joshua Linda  
Walter E. Edge, Jr.  
Service List

**FIRST SET OF INFORMATION REQUESTS OF THE TOWN OF NEW  
SHOREHAM**

TOWN-1 Please provide Interstate's general ledger Chart of Accounts.

**Response:** See attached.

Prepared by WEE

## Interstate Navigation Company

## Chart of Accounts

As of Sep 30, 2005

Filter Criteria includes: Report order is by ID. Report is printed with Accounts having Zero Amounts and in Detail Format.

Account ID	Account Description	Active?	Account Type
1100	Cash-Washington Trust Checking	Yes	Cash
1110	Cash-Wash Trust Payroll Check	Yes	Cash
1120	Cash-Fleet Refund checking	Yes	Cash
1130	Cash-Wash Trust MM Acct	Yes	Cash
1140	Cash-Washington Trust CC	Yes	Cash
1150	Cash-Wash Tr Savings#61200465	Yes	Other Assets
1160	Cash-Wash Tr Savings #13034004	Yes	Cash
1165	Cash-Washington Trust #9084689	Yes	Other Assets
1170	Cash on Hand	Yes	Cash
1200	Accounts Receivable	Yes	Accounts Receivable
1250	A/R Credit Cards	Yes	Accounts Receivable
1300	Prepaid Expenses	Yes	Other Current Assets
1400	Advances	Yes	Other Current Assets
1410	Employee Loans	Yes	Other Current Assets
1500	Vessels & Equipment	Yes	Fixed Assets
1510	MV Block Island	Yes	Fixed Assets
1512	MV ANNA C	Yes	Fixed Assets
1515	MV Carol Jean Repowering	Yes	Fixed Assets
1520	Dock Improvements & Ramps	Yes	Fixed Assets
1530	Motor Vehicles	Yes	Fixed Assets
1540	Bulkhead	Yes	Fixed Assets
1550	Block Island Freight Shed	Yes	Fixed Assets
1560	Buildings	Yes	Fixed Assets
1565	Block Island Office	Yes	Fixed Assets
1570	Pt Judith Project	Yes	Fixed Assets
1580	Block Island Office & Building	Yes	Fixed Assets
1590	Office & Terminal Equipment	Yes	Fixed Assets
1600	Accumulated Depreciation	Yes	Accumulated Depreciation
1700	Security Deposits	Yes	Other Assets
1800	Loan Acquisition Fees	Yes	Other Assets
1850	Accumulated Amortization	Yes	Other Assets
2000	Transfers	Yes	Cash
2050	SUSPENSE	Yes	Other Current Liabilities
2100	Accounts Payable	Yes	Accounts Payable
2105	Lease Payable	Yes	Other Current Liabilities
2110	Accounts Payable-Nelseco Nav C	Yes	Accounts Payable
2120	Accounts Payable-Waterfront Re	Yes	Accounts Payable
2130	Accounts Payable Inter.Nav.Co.	Yes	Accounts Payable
2140	Accounts Payable-Thames Shipyd	Yes	Accounts Payable
2190	Direct Deposit	Yes	Other Current Liabilities
2200	Payroll Taxes Payable	Yes	Other Current Liabilities
2210	Taxes Payable-CT Withholding	Yes	Other Current Liabilities
2220	Taxes Payable-RI Withholding	Yes	Other Current Liabilities
2225	CT Unemployment Compensation	Yes	Other Current Liabilities
2230	Accrued Taxes Payable	Yes	Other Current Liabilities
2240	Federal Income Tax	Yes	Other Current Liabilities
2250	CT Corporation Tax Payable	Yes	Other Current Liabilities
2260	Sales Tax Payable	Yes	Other Current Liabilities
2300	Gasnishments Payable	Yes	Other Current Liabilities
2400	Landing Fee Payable/Block Isla	Yes	Other Current Liabilities
2450	Landing Fee Payable/PJ	Yes	Other Current Liabilities
2500	Accured Accounts Payable	Yes	Other Current Liabilities
2510	Accured Payroll	Yes	Other Current Liabilities
2520	Accured Pension Payable	Yes	Other Current Liabilities
2600	Deferred Revenue	Yes	Other Current Liabilities
2680	Washington Tr-Line of Credit	Yes	Other Current Liabilities
2700	Notes Payable Washington Trust	Yes	Long Term Liabilities
2710	Note Payable Washington Trust	Yes	Long Term Liabilities
2720	Note Payable Washington Trust	Yes	Long Term Liabilities
2800	Exchange-Island Marine	Yes	Long Term Liabilities
2900	Deferred Taxes	Yes	Long Term Liabilities
3000	Capital Stock	Yes	Equity-doesn't close
3100	Capital Surplus	Yes	Equity-doesn't close
3199	Beginning Balance Equity	Yes	Equity-doesn't close
3200	Retained Earnings	Yes	Equity-Retained Earnings
4100	Passenger	Yes	Income
4102	Passengers- non-commuter	Yes	Income
4104	Passengers- commuter	Yes	Income
4106	Passengers- block ticket/group	Yes	Income
4108	Passengers-web tickets	Yes	Income
4110	Vehicles	Yes	Income
4112	Cars- non-commuter	Yes	Income

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Account ID	Account Description	Active?	Account Type
4114	Cars- commuter	Yes	Income
4116	Trucks	Yes	Income
4120	Bar	Yes	Income
4130	Freight	Yes	Income
4140	Charter	Yes	Income
4150	Bikes, Mopeds, Etc.	Yes	Income
4160	Mail	Yes	Income
4163	Tours-Bus	Yes	Income
4165	Tours-Meals	Yes	Income
4170	Other	Yes	Income
4180	Commissions	Yes	Income
4200	Refunds, Credits & Voids	Yes	Expenses
5100	Payroll	Yes	Expenses
6100	Depreciation & Amortization	Yes	Expenses
7100	Vessel Maintenance-Block Islan	Yes	Expenses
7110	Vessel Maintenance-Carol Jean	Yes	Expenses
7120	Vessel Maintenance-Manitou	Yes	Expenses
7130	Vessel Maintenance-Anna C	Yes	Expenses
7140	Vessel Maintenance-Nelseco	Yes	Expenses
7150	Vessel Maintenance-General	Yes	Expenses
7200	Building Maintenance-Block Isl	Yes	Expenses
7210	Building Maintenance-Pt Judith	Yes	Expenses
7220	Dock Maintenance-Block Island	Yes	Expenses
7230	Dock Maintenance-Pt Judith	Yes	Expenses
7240	Yard Maintenance-Montville	Yes	Expenses
7250	Terminal Maintenance	Yes	Expenses
7260	Auto & Truck Maintenance	Yes	Expenses
7270	General Repairs & Maintenance	Yes	Expenses
7280	Forklifts Maintenance	Yes	Expenses
7300	Fuel-MV Block Island	Yes	Expenses
7310	Fuel-MV Carol Jean	Yes	Expenses
7320	Fuel-MV Manitou	Yes	Expenses
7330	Fuel-MV Anna C	Yes	Expenses
7340	Fuel-MV Nelseco	Yes	Expenses
7350	Lube Oil	Yes	Expenses
7360	Crew Expenses	Yes	Expenses
7370	Boat Supplies	Yes	Expenses
7380	Other Vessel Expenses	Yes	Expenses
7390	Wharfage	Yes	Expenses
7395	Boat Charter	Yes	Expenses
7397	Bus Charter	Yes	Expenses
7400	Food for Resale	Yes	Expenses
7410	Beverages for Resale	Yes	Expenses
7415	Meals-Tour Package	Yes	Expenses
7420	Bar Supplies	Yes	Expenses
7505	Homeland Security-Startup	Yes	Expenses
7506	Homeland Security-Equipment	Yes	Expenses
7507	Homeland Security-Personnel	Yes	Expenses
7508	Homeland Security-Operations	Yes	Expenses
7510	Trash Removal/Waste Removal	Yes	Expenses
7600	Local Transfer	Yes	Expenses
7700	Auto & Truck Expense	Yes	Expenses
7710	Travel	Yes	Expenses
7800	Advertising & Promotion	Yes	Expenses
7900	Other Traffic Expenses	Yes	Expenses
8100	Office	Yes	Expenses
8105	Meetings/Seminars	Yes	Expenses
8110	Rent	Yes	Expenses
8120	Utilities	Yes	Expenses
8130	Dues & Subscriptions	Yes	Expenses
8140	Telephone	Yes	Expenses
8150	Computer Expenses	Yes	Expenses
8160	PUC Expenses	Yes	Expenses
8165	Landing Fee Expense	Yes	Expenses
8170	Contributions	Yes	Expenses
8180	Payroll Services	Yes	Expenses
8190	Credit Card Admin. Fees	Yes	Expenses
8200	Bank Charges	Yes	Expenses
8210	Finance Charges	Yes	Expenses
8220	Freight	Yes	Expenses
8230	Miscellaneous	Yes	Expenses
8240	Bad Debt Expense	Yes	Expenses

## Interstate Navigation Company

## Chart of Accounts

As of Sep 30, 2005

Filter Criteria includes: Report order is by ID. Report is printed with Accounts having Zero Amounts and in Detail Format.

Account ID	Account Description	Active?	Account Type
8300	Accounting	Yes	Expenses
8310	Legal	Yes	Expenses
8320	Other Professional Fees	Yes	Expenses
8400	Profit Sharing/Pension Expense	Yes	Expenses
8410	Employee Insurance	Yes	Expenses
8500	Insurance-Vessel	Yes	Expenses
8510	Insurance-Auto	Yes	Expenses
8520	Insurance-Property	Yes	Expenses
8530	Insurance-Other	Yes	Expenses
8540	Insurance-Workers Comp	Yes	Expenses
8550	Damages-Auto & Freight	Yes	Expenses
8560	Injuries	Yes	Expenses
8600	Fica Expense	Yes	Expenses
8610	CT Unemployment Compensation	Yes	Expenses
8620	Federal Unemployment Compens	Yes	Expenses
8630	RI Unemployment Compensation	Yes	Expenses
8700	Gross Earnings	Yes	Expenses
8710	Annual Report	Yes	Expenses
8720	Licenses & Registration	Yes	Expenses
8730	Sales & Use Tax-Rhode Island	Yes	Expenses
8740	Sales & Use Tax-Connecticut	Yes	Expenses
8750	Federal Income Tax	Yes	Expenses
8760	CT Corporation Tax	Yes	Expenses
8770	Permits	Yes	Expenses
8780	Real Estate Tax	Yes	Expenses
8790	Personal Property Tax	Yes	Expenses
8800	Penalties	Yes	Expenses
8810	Cash Over/Short	Yes	Expenses
8900	Returned Items	Yes	Expenses
8910	Chargebacks	Yes	Expenses
9100	Interest Expense	Yes	Expenses
9200	Interest Income	Yes	Income
9300	Miscellaneous Income	Yes	Income

TOWN-2

Please identify all financial and operating reports customarily used by Interstate's management to monitor and control finances and operations. This should include financial statement, reports of expenses relative to budget and operating analyses such as labor hours, number of employees, fuel consumption and the like. Please indicate what period is covered by a report and the lag time between that period and the issuance of the report. Please provide an example copy of each such report.

**Response:** Interstate's management is a "hands on", family run operation. Interstate's management does not rely on numerous written reports that increase professional fee expenses, take valuable time to prepare and even more time to read. Interstate's management stays on top of all financial and operational matters through daily oral communications and a review of the detail records that would be the basis of any reports.

Interstate relies upon unaudited semi annual financial reports prepared by its accounting firm. The figures from these reports are compared to previous years and analyzed for trends. This is the primary long term decision making tool utilized by management. Interstate's management also utilizes other tools, although they are not necessarily formal reports, including the following:

- Weekly timesheets, especially overtime and the total payroll calculated for each week by Interstate's payroll company.
- Fuel invoices as rendered to Interstate and monthly compilations of the fuel invoices for the Division of Public Utilities fuel surcharge filings, which are then compared to previous years.
- Annual landing fee reports to the Town of Block Island, which are then compared to previous years.
- Cash balances which are checked by on-line computer access daily.
- Monthly bank statements which are reconciled, and if anything appears questionable, are compared to previous years.
- Credit card company statements which are reviewed, and if there is a question, compared to previous years.
- the check register which is printed monthly and compared to previous years.

Susan Linda is the President, Treasurer, and Financial Officer of the company. She has been working for the company for over 45 years and, using the information developed above, is able to keep a firm hand on the finances of the company. In fact, during her operation of the company, she has only had to draw down on Interstate's line of credit once for a very short period of time, and that was due to cost overruns for the rehabilitation of the *M/V Carol Jean*.

Prepared by WEE

TOWN-3

Please explain whether Interstate proposes to exclude the M.V. Athena from rate base and its new long term debt issued to acquire the M.V. Athena from capital structure for purposes of the present and future conventional ferry rate cases, assuming Division approval of the proposed purchase of IHSF assets and the issuance of long term debt to fund that purchase.

**Response:** Yes, that is part of Interstate's proposal to the Commission.

Prepared by WEE

TOWN-4

Please provide an explanation how Interstate has been accounting for revenues, capital costs and expenses associated with its high speed ferry operations from pre-operation to date. Explain what steps, if any, have been taken to separate conventional and high speed operations for accounting and ratemaking purposes.

**Response:** Interstate has charged all of the costs relating to the acquisition of the high speed ferry operations through the test year (which did not include any fast ferry operations) to Interstate's traditional service general ledger accounts. Because Interstate felt that it was unlikely that the purchase would ever go through, Interstate did not segregate the costs.

During the interim period (between the test year and the rate year) and for all future years Interstate intends to account for all direct costs relating to the fast ferry and all fast ferry revenues in separate fast ferry general ledger accounts, if the Commission approves Interstate's proposal to operate a separate fast ferry Division.

Prepared by WEE

TOWN-5

Please provide an explanation how Interstate proposes to account for revenues, capital costs and expenses associated with its high speed ferry operations during the rate year. Explain what steps, if any, will be taken to separate conventional and high speed operations for accounting and ratemaking purposes.

**Response:** As stated in the response to Town-4, Interstate proposes to treat the fast ferry operations as a separate division (profit center) with its own balance sheet, revenue and expense accounts.

Prepared by WEE

TOWN-6

Please provide a detailed itemization of all costs (including but not limited to legal and accounting costs) incurred by Interstate in connection with its multi-year efforts to acquire the RI assets of IHSF and to obtain financing for that acquisition, whether or not such costs were booked to test year results. Specify all such costs (a) incurred prior to the test year; (b) incurred during the test year; (c) incurred post test year and/or estimated to occur before the rate year; and (d) estimated to occur during the rate year. Specify the accounting entries made regarding such costs by year (e.g., the accounts charged). Provide supporting general ledger back-up where available.

**Response:** All legal and accounting costs regarding IHSF were billed to Interstate in general IHSF billings. They covered various matters regarding IHSF, including, but not limited to, Commission proceedings, Division proceedings, Superior Court litigation, Supreme Court litigation, and other matters. They were not segregated by topic, and therefore, the costs associated solely with the efforts to acquire IHSF cannot be readily identified. Any attempt to do so would be inordinately expensive and time consuming. It is also not possible to estimate any future costs at this time, especially since the status of the Division and Commission approvals is not yet known. All such legal and accounting bills were booked to professional services, Interstate's general ledger accounts #8300 Accounting and #8310 Legal and were included in this filing in the test year analysis.

Prepared by WEE

TOWN-7

Assuming approval of Interstate's proposal to treat its high-speed ferry operations as a separate Division that bears its own direct costs, would Interstate treat the cost of the IHSF asset purchase and related financing as direct costs chargeable to its high-speed ferry operations? Or would these costs be included in whole or in part in the cost of conventional ferry operations?

**Response:** Yes and no to both questions. Interstate believes that the purchase of the fast ferry operations from IHSF and the agreement by Interstate to apply all net profits (net of losses) from the fast ferry operation to the traditional (lifeline) service suggests that the acquisition costs should be born by the traditional ratepayers. After all, ratemaking philosophy encourages the matching theory of the ratepayers that get the benefit absorb the costs.

That said, since all of the net profits from the fast ferry will go for the good of the traditional (lifeline) service the point is meaningless. If Interstate charges the acquisition costs to the fast ferry service there will be less profit available to transfer to the traditional (lifeline) service. If, however, the traditional service pays the acquisition cost then the fast ferry service will provide a greater subsidy to the traditional service. This is a "pay me now or pay me later" issue. Either way the traditional service receives the benefit.

Prepared by WEE

TOWN-8

Please state whether Interstate would agree to apply any one-time net revenues from its first year of high speed operations to fund an Old Harbor dockside costs and improvements (e.g., restrooms, visitor center) reserve account required as a result of continued increased use of Old Harbor by ferry passengers. If not, please explain how Interstate proposes to treat such net revenues for ratemaking purposes.

**Response:** No. Interstate has proposed that the benefit of fast ferry profits go to the traditional (lifeline) service, not to subsidize the Town's taxpayers. Also, Interstate's ratepayers are already paying statutorily-mandated landing fees to the Town that total over \$100,000 per year and to date have submitted over \$1.5 million to the Town. Such payments, by law (RIGL 45-2-35.1), must be used by the Town "to promote the health, safety and welfare of all (ferry) passengers, including, but not limited to, emergency medical services, acquisition of property to support tourism related activities, to construct and maintain tourism support facilities, and to establish a fund to assist the town of New Shoreham in resolving problems which may arise due to growth in the tourism industry." Finally, Interstate Nav. has leased the property on which the Town maintains the visitor center for only \$1 to the Town.

Prepared by WEE

TOWN-9 Please provide all inputs, assumptions and workpapers which support Mr. Edge's Schedule WEE-1, his projection of high speed ferry net revenues during the first year after Interstate's proposed purchase of IHSF assets and issuance of related long term debt (see Interstate response to DIV 1-6). Please provide updated inputs, assumptions and workpapers as well if Mr. Edge submits an updated Schedule WEE-1.

**Response:** Unfortunately, there are a number of WEE-1 schedules in various dockets. The Schedule WEE-1 in this traditional rate filing however reflects no inputs, assumptions or workpapers relating to high speed ferry net revenues. As I stated in my response to Div 1-6 there are no fast ferry revenues or expenses reflected in my prefiled testimony therefore there are no fast ferry revenues or expenses in my Schedule WEE-1. Interstate will provide a new Schedule WEE-1 in rebuttal which is likely to have a net revenue allowance from the fast ferry operations to the life line service if the Division and Commission approve the current filings before them relating to Interstate's fast ferry acquisition of IHSF's RI assets.

Prepared by WEE

TOWN-10 Please explain how Interstate proposes to treat any rate year and post rate year net revenues or net losses from high-speed ferry operations for conventional ferry ratemaking purposes on a going forward basis.

**Response:** This issue has not yet been fully analyzed by the Division and Commission and I would expect that there could be some modification to the way the net revenues and net losses are treated in the traditional rate filing. However, Interstate has proposed in previous filings that the net profit (after any net losses) be credited to the benefit of the traditional service. Interstate believes that this could be accomplished in any number of ways.

Interstate is currently proposing that the net profit from the fast ferry service from the summer of 2006 be deposited into a restricted account that would be used as a "true-up" account to address variances in fast ferry profits and losses. Interstate would suggest that in this traditional docket an allowance be estimated for the future profit of the fast ferry operations and that amount be used to reduce the revenue requirement in this filing. For example the amount could be \$150,000. This would assure that no matter what happened in the fast ferry operations the traditional service would get the benefit in reduced rates by \$150,000 until Interstate refiled for traditional service rate relief.

If the fast ferry service generates a \$200,000 profit for the first year then Interstate would deposit \$50,000 ( $\$200,000 - \$150,000$ ) into the true-up account. On the other hand if the fast ferry operation were to only earn a profit of \$100,000 then Interstate would withdraw \$50,000 ( $\$150,000 - \$100,000$ ) from the true up account. If Interstate were to have a very bad summer and lose \$50,000 then Interstate would withdraw \$200,000 ( $\$150,000 + \$50,000$ ).

The true-up account would be reviewed annually by the Commission and the Division after Interstate files its annual report to determine if it was appropriate for Interstate to increase or decrease the allowance (subsidy) to the traditional service. Of course Interstate has agreed that if there is a loss in the first year of operation that Interstate will absorb that loss.

Prepared by WEE

TOWN-11 Please explain how Mr. Edge defines “direct costs” and “direct revenues” for Interstate’s high-speed operations, as described in his testimony in pending Division dockets.

**Response:** Revenues and costs that would not exist if there were no Interstate fast ferry operations.

Prepared by WEE

TOWN-12 Does Mr. Edge's definition of "direct costs" include any allocation of joint and common costs of Interstate's conventional/fast ferry operations to the high-speed operations?

**Response:** No.

Prepared by WEE

TOWN-13 If a fully allocated cost of service methodology were adopted by the Commission to determine the level of costs to be directly assigned and allocated to high-speed operations, does Mr. Edge agree that portions of rate year cost of service adjustments would be allocated to high-speed operations?

**Response:** Yes, but the idea makes no regulatory rate making sense at all.

Prepared by WEE

TOWN-14 Has Interstate made any commitment regarding the level of service it will provide during the rate year, comparable to its commitment in the Docket 3573 Stipulation (Edge at 3, lines 20-23)?

**Response:** Interstate remains committed to and bound by the Order in Docket 3573. Interstate has not asked for relief from that Order. The commitment is attached (see Section 4).

Prepared by WEE

The parties agree that the boat shall be depreciated over a life of 15 years for rate making purposes.

**Section 4:** The Company agrees to provide a level of service equal to the service level set forth in the Company's 2004 ferry schedule on file with the Commission, and the Company agrees that the *MV Anna C*, *MV Block Island*, and *MV Carol Jean* shall be the vessels in service for trips made between Point Judith and Block Island, except during situations beyond Interstate's control, such as major repairs, severe weather, acts of God, sinking, etc.

**Section 5:** The rate increase will be applied as follows: All rates except non-commuter cars (and related non-commuter vehicles such as SUVs, pick ups, and vans) will increase by approximately 11.5%. Non-commuter cars (and related non-commuter vehicles such as SUVs, pick ups, and vans) will increase by approximately 50%. The new rates and tariffs are set forth on Stip 6, Stip 8 and Stip 9 attached hereto and incorporated by reference into this Stipulation and Settlement. The eligibility requirements for discounted commuter rates are hereby changed so that only the holders of a Rhode Island driver's license with a Block Island address on the license are eligible for commuter rates, and to be eligible for the commuter car, SUV, van and pick up rates, the vehicle (1) must be driven by a driver with a Block Island license, and (2) must have a Block Island address on its registration.

**Section 6:** The Parties agree that the Company will be permitted to offer the following volume and group discounts: (1) an advance purchase of 10 non-commuter

MEHC  
BMR 5/12/04  
MAY  
5-12

TOWN-15 In the event that high-speed revenues were inadequate to cover debt service, capital and operating costs associated with Interstate's high-speed operations(e.g., business failure, damage to vessel causing loss of passenger revenues, extraordinary capital or maintenance costs) what steps would Interstate take to (a) ensure that the level and quality of conventional ferry service would not be adversely impacted and (b) insulate conventional ferry operations from increased revenue requirements and loss of use of internally generated funds?

**Response:** Interstate addressed this question in part in its own CPCN filing in Docket D-05-06. In that docket I testified as follows:

**“Q. What if Interstate losses money on the Fast Ferry operation, how would that impact the current customer base?”**

A. It would have no impact. Interstate would simply not file for a rate increase relating to the loss from the Fast Ferry operation and therefore the loss would not be passed on to the ratepayers. In other words Interstate is willing to take the business risk of the Fast Ferry not being profitable.

**Q. Mr. Edge, isn't it possible that a large loss from the Fast Ferry operation could result in a financial hardship for Interstate which in turn could adversely impact on Interstate's current ratepayers even if there is no increase in current rates?**

A. Based upon my analysis, I do not expect a large loss from the Fast Ferry operations.

**Q. Nevertheless, what if there is a large loss from the Fast Ferry operations, what will Interstate do?**

A. Interstate will determine why there was a loss. If it is decided that the Fast Ferry operation can not be profitable, then Interstate Navigation's management intends to sell or charter the new Fast Ferry. Our research has shown that the resale value of these fast ferry boats, due to the high demand for this quickly growing mode of transportation, is often greater than the original cost for a period of time. Therefore, Interstate is confident that even the worst case loss scenario will not adversely impact the current ratepayers.

**Q. Is Interstate prepared to take any other steps to protect the current rate payers?**

A. Yes. \*\*\*\*\*.

Also, although Interstate prefers to use the new Fast Ferry exclusively for its own operations, it is possible that the new Fast Ferry could be leased to other operators. Interstate has determined that these leases can be very profitable. The Commission's review of Hi-Speed's winter leases should support this claim."

In this docket, Interstate is confident that it can continue to make profits (as it has in the poor weather summer of 2006) in its fast ferry operations after the purchase of the IHSF assets in RI. Further, Interstate is prepared, if necessary, to make appropriate changes to the fast ferry operation in the areas of scheduling and staffing to eliminate any losses that may result. It must be remembered that Interstate has been running ferries back and forth from Block Island for well over fifty years and I believe that they have the knowledge and experience to make this fast ferry operation profitable.

If, after Interstate has exhausted all of the fast ferry cost cutting options, Interstate still has a loss, Interstate would then need to evaluate the fast ferry rates. For example, would it be better to increase rates and in turn increase revenue to restore profit or would it be better to decrease rates, which may increase ridership, and in turn increase revenue and profit? Interstate would evaluate these options and the option of leasing the *MV Athena* fully before Interstate would consider selling the *MV Athena*.

The only risk that is different in the sale of the *MV Athena* compared to Interstate's selling its own vessel built for its CPCN is the fact that the *MV Athena* is not worth the full amount of the borrowing needed to buy all the RI assets of IHSF. Therefore, if the fast ferry operation was not profitable, even after Interstate made all of the appropriate changes (including adjusting rates), then Interstate would have to either lease the vessel year round to cover the debt service, sell the *MV Athena* and reduce debt service payments or sell the entire fast ferry business for \$5.6 million dollars or more.

However, in a worse case scenario suggested by the data request, Interstate would have to sell the *MV Athena*. The proceeds from that sale would go to reduce the debt from \$5,600,000 to \$1,400,000 (\$5.6-\$4.2 million). Interstate would then negotiate a refinancing of the remaining balance of the debt and reduce the debt service payments from \$490,000 to about \$123,000. Interstate could then pay the reduced debt service amount by using its authorized return on rate base (nearly \$500,000) from its traditional service. The authorized return on rate base is the property of the owners, not the ratepayers, and the use of these funds would not adversely impact the traditional service.

One additional option would be for Interstate to return the *M/V Manitou* to the Newport to Block Island run and sell the *M/V Nelseco* (appraised value \$2.3 million). The proceeds from the sale of both the *M/V Athena* and the *M/V Nelseco* would be \$6.5 million (\$2.3 + \$4.2) which is greater than the total debt of this deal \$5.6 million.

It should be noted however that the risk of failure for the proposed fast ferry operation using the *MV Athena* is far less than the risk that Interstate would have faced with its own CPCN. With the purchase of the *MV Athena* and the other RI assets of the IHSF, Interstate eliminated significant competition and purchased an established fast ferry service with an established customer base. Also, Interstate's traditional service would have faced far more risk of increased traditional rates if Interstate continued to lose customers to IHSF.

Interstate expects that as its customers become familiar with the Interstate fast ferry operations to Old Harbor, and Interstate has the opportunity to refine its schedule to meet its customers' needs, as well as refine and expand its fast ferry marketing, ridership on the fast ferry will increase and the fast ferry service will be more profitable and will provide an increased subsidy for the traditional service. It should be noted that Interstate's marketing of its fast ferry in 2006 was limited by virtue of the fact that approval was not received until just before the season began.

Prepared by WEE

TOWN-16 Please provide the Homeland Security Reports for FY 2005 and FY 2006 as mentioned on page 17 of Mr. Edge's testimony, lines 3-8.

**Response:** Interstate has filed in this docket the revenues and expenses related to Homeland Security for FYE May 31<sup>st</sup> 2005 and FYE May 31<sup>st</sup> 2006 (See Schedule WEE-8). In addition, Interstate has now provided additional information to the Commission regarding the description of the personnel charged to the Homeland Security account and support for other charges to the Homeland Security account (see responses to Commission data request COM-16, COM-17 and COM-18).

Prepared by WEE

TOWN-17 Please refer to Interstate's response to DIV 1-17 and Schedules WEE-3 and WEE-8. Please: (a) explain why \$144,730 in future capital additions for Homeland Security are treated as a cost of service expense line item rather than added to plant in service; (b) provide a reference to the "federal guidelines" referred to in the DIV 1-17 response; (c) state whether Mr. Edge maintains that the Commission is required to permit these capital expenditures as expenses for ratemaking purposes; and (d) explain what is meant by a 'pay as you go account'.

**Response:** (a) The answer to this item is the same answer as was provided in the response to DIV 1-17 noted in the question above. (b) The federal guidelines were provided in their entirety in the last docket when the allowance was established. The Town was a party to that docket. Interstate will not do the Town's legal work. However, see Interstate's response to Town 23. (c) For all capital items unless and until the Commission changes its decision in the last Docket, I believe that the Commission is required to permit capital items in the Homeland Security account. The Commission has the authority to amend its previous decision prospectively but not retrospectively. (d) Pay as you go is a ratemaking term used frequently in dockets before the Commission. It means that instead of purchasing capital items using long term debt and capitalizing and depreciating the asset the Commission allows a utility to purchase capital items (usually with monies from a restricted account) and expense them in the year of acquisition.

Prepared by WEE

TOWN-18 Please state whether Interstate has considered a separate surcharge for Homeland Security costs.

**Response:** No.

Prepared by WEE

TOWN-19 Please state whether Interstate is prepared to consider a lower amount of fuel cost in bases rates, such as \$1.25, leaving a balance of fuel costs to be recovered through a fuel surcharge.

**Response:** Yes, Interstate is prepared to consider a lower amount of fuel in base rates.

Prepared by WEE

TOWN-20 Has Interstate considered a fuel cost reconciliation rate design to ensure that it neither under-collects nor over-collects its fuel costs?

**Response:** No. Interstate follows the fuel surcharge statute and the Division's related Regulations and Orders. Reconciliation is not part of the statute, regulations or Orders.

Prepared by WEE

TOWN-21      What accounting or other measures has Interstate implemented to ensure that conventional ferry rates are not recovering fuel costs associated with it high speed operations?

**Response:** Separate fuel surcharge calculations approved by the Division.

Prepared by WEE

TOWN-22      What, if any, accounting or other measures has Interstate taken to ensure that the post test year and rate year costs associated with Homeland Security requirements for high speed operations are being and will be recovered directly from high-speed operations?

**Response:** None, other than as suggested in the response to Town-5.

Prepared by WEE

TOWN-23 Please provide a citation to the Homeland Security Cost Guard regulations cited by Mr. Linda on page 5, line 24 of his testimony.

**Response:** These regulations were provided in their entirety in the last docket when the Homeland Security restricted allowance was established by the Commission. The Town was a party to that Docket. See also 33 CFR Navigation and Navigational Waters Chapter 1, Coast Guard, Department of Homeland Security, Subchapter H – Maritime Security, parts 101, 103, 104, 105 and 106, and Interstate’s response to Com 1-17.

Prepared by WEE

TOWN-24 Please identify test year and overall costs associated with Division Docket No. D-05-06 and explain how these costs have been treated for purposes of developing the proposed revenue requirement.

**Response:** D-05-06 was Interstate's CPCN docket. These costs are included in the test year professional services account in this Docket. However, there are no such costs in the proposed revenue requirement for the rate year.

Prepared by WEE

TOWN-25 Please identify the “direct competition for summer tourists” that Mr. Linda expects to occur during the 2007 rate year (see page 5, lines 26-27 of his testimony) and whether any shareholders, officer or employees of Interstate have any ownership, voting or other economic interest in any competitor identified by Mr. Linda.

**Response:** Mr. Linda is not an economist and was not using this term in the strict economic sense. He considered such competition to be from the Block Island Express ferry out of New London to Block Island; IHSF’s ferry out of Point Judith to Block Island (if the acquisition by Interstate is not approved); the fast ferry from Quonset Point to Martha’s Vineyard; the RI and CT gambling venues; the Newport mansions, etc.

Prepared by WEE assisted by JL

TOWN-26      Given Mr. Linda's testimony on page 6, lines 8-13, please explain why Interstate has not proposed to increase its fast ferry rates at a time when it has proposed a substantial increase in conventional ferry service rates.

**Response:** Interstate believes that the more ridership it gets on the fast ferry the better it will be for the traditional service. Increasing the fast ferry rates at this time would most likely reduce the fast ferry ridership.

Interstate does not agree with the statement above that the traditional service rate increase requested in this filing is "substantial". In fact if the roll-in of fuel were not part of the revenue requirement the rate request would be a modest 15% and given all of the improvements Interstate has made to its fleet in the past three years (Interstate's last increase was effective in 2004 and this increase will not be effective until 2007), I believe that the rate increase is modest, averaging only about 5% per year. The increase relating to the fuel roll-in is not a rate increase at all. The ratepayers are already paying the entire fuel cost in the fuel surcharge and the proposal in the docket is simply a reclassification as to how the revenue is collected.

Prepared by WEE

TOWN-27 Please provide Interstate's current long-term year capital and operating budgets, including its conventional and fast ferry operations.

**Response:** Interstate does not waste time or professional fees in preparing written budgets. Interstate has been run by the same management for over 50 years and Interstate's management has an excellent handle on its projected operating and capital needs. As a guide Interstate uses its previous year actual results for its operating budget. Capital needs are identified well in advance because Interstate has hands on knowledge of all of Interstate's capital assets. Management makes sure that the all capital needs are addressed and often completes capital improvements in house.

Prepared by WEE

TOWN-28 Please provide any fast ferry business plans provided by Interstate to its lenders.

**Response:** No business plan was provided.

Prepared by WEE

TOWN-29 Please provide Board of Directors meeting minutes for the test year and post test year period concerning (1) high speed ferry operations; (2) the effect of high speed ferry operations on conventional service revenue requirements; (3) the need for conventional service rate relief; (4) the issuance of shares; (5) the payment of dividends; and/or (6) the setting of management compensation levels.

**Response:** Attached are all meeting minutes for the test year and post test year.

Prepared by WEE

MINUTES OF SPECIAL MEETING  
OF  
INTERSTATE NAVIGATION COMPANY

A special meeting of Interstate Navigation Company (the "Company") was held on May 31, 2006 at 11:49 a.m. at the offices of the Company at Eugene O'Neill Drive, New London, Connecticut.

The following shareholders were present: Susan Linda, Joshua Linda and Raymond Linda. Also present were Michael R. McElroy, Esq. and Meredith E. Russell, Esq., both counsel to the Company; and Walter Edge, CPA. Mr. McElroy acted as moderator of the meeting and called the meeting to order.

The purpose of the meeting was to discuss the purchase of the IHSF's Rhode Island assets and fast ferry vessel M/V Athena for \$5,612,000. Susan Linda has signed a confidentiality agreement with IHSF not to disclose this purchase except to make application for a loan and for regulatory permits, and this confidentiality agreement is in effect until the closing of the Modern Continental transaction, which has not yet occurred.

The first order of business was to authorize the Company to purchase IHSF's Rhode Island assets and fast ferry vessel M/V Athena for a purchase price of \$5,612,000, with a closing to take place on or about November 1, 2006. A motion to that effect was approved unanimously.

The second order of business was to authorize the Company to borrow \$5.6 million dollars from Washington Trust Company to purchase IHSF's Rhode Island assets and fast ferry vessel M/V Athena, and in effect to ratify that borrowing process which had already been undertaken by the Company (a commitment letter has been issued). A motion to that effect was approved unanimously.

The next order of business was a motion to ratify the lease of the M/V Athena to IHSF for the winter of 2006-2007 for \$1,285 per day. That motion passed unanimously.

The final order of business was a discussion of current pending legislation which, if passed, could have a negative impact of the purchase of IHSF. The Company is opposing the bill or will try to get an exemption from this legislation if it looks like it might pass.

There being nothing further to come before the meeting, it adjourned at 12:00 p.m.

  
\_\_\_\_\_  
Susan E. Linda, Secretary

# AGENDA

## INTERSTATE - SPECIAL MEETING

1. ✓ Vote to authorize purchase of IHSF's RI assets and vessel for \$5,612,000 on or about 11/1/06.
2. ✓ Vote to authorize loan for \$5.6 M from Washington Trust Company to purchase IHSF.
3. ✓ Vote to authorize lease of M/V Athena to IHSF for winter of 2006-07.
4. ✓ Update on legislation (proposed R.I.G.L. § 39-3-25 changes).

MINUTES OF THE ANNUAL MEETING  
OF  
INTERSTATE NAVIGATION COMPANY

The Annual Meeting of Interstate Navigation Company (the "Company") was held on May 31, 2005 at 10:30 p.m. at the offices of the Company at Eugene O'Neill Drive, New London, Connecticut.

The following shareholders were present at the meeting: Susan Linda, Raymond Linda, Robert Tobin, Esq. (pursuant to a proxy for Jessica Wronowski), Adam Wronowski, Derek Tyrseck, and Bryon Hewitt.

Also present were Joshua Linda, Vice President and Director, Michael R. McElroy, Esq., and Meredith E. Russell, Esq., both counsel to the Company, Walter Edge, C.P.A., regulatory accountant for the Company, and Richard MacMurray.

Mr. McElroy acted as moderator of the meeting, and the meeting was called to order by the President of the Company, Susan Linda.

A Moment of Silence was observed in recognition of the passing of Anna C. Wronowski.

The minutes of the 2005 Annual Meeting were signed and approved.

The next order of business was the election of directors and then officers of the Company. Susan Linda nominated herself for Director, President, Treasurer, and Secretary; Joshua Linda as Director and Vice President, and Raymond Linda as Director. No other slate of directors or officers was proposed. The proposed slates of directors and officers were elected by unanimous votes.

The next item was such other business as may come before the meeting. Attorney McElroy presented an agenda of items to be reviewed at the meeting (attached hereto) and each item was discussed in detail.

Mr. Edge made a presentation concerning the financial activity and status of the company since the last annual meeting. A balance sheet and income statement as of November 30, 2005, prepared by John G. Kanabis, the Company's accountant, was distributed and is attached hereto.

Mr. Edge and Attorney McElroy reported on a rate increase filing that is being prepared for filing with the Rhode Island Public Utilities Commission:

- a. Some reasons for the need for a rate increase include the purchase of the "Anna C."; the renovations to the "Carol Jean"; high fuel prices; and other

increases in the cost of running the company largely as a result of payroll and insurance.

- b. The recommended rate increase is currently projected to be about 25% - 30%.
- c. A motion to approve the rate increase filing was passed unanimously.

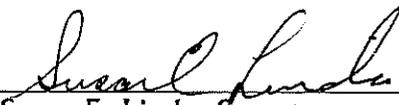
Mr. McElroy then made a presentation of the following matters which occurred since the last Annual Meeting.

1. The M/V Athena fast ferry has been leased from ISHF for the 2006 summer season ending October 11, 2006, at a rate of \$1,285 per day, plus captain and engineer, plus \$200 per day to train crews. The DPUC has approved the lease and the PUC has approved operating Interstate's fast ferry at the same rates as IHSF used to operate.
2. The IHSF CPCN is on hold for one year and has not been abandoned by IHSF, with the permission of the PUC. If our fast ferry the season is successful, the Company may decide to build its own fast ferry. Meanwhile, this lease is an easy way for the Company to get started in the fast ferry business, get training, and hopefully to make money. A motion to ratify the lease was approved unanimously.
3. As to stock swap/purchase negotiations, further information is required and is coming soon from Interstate Nav., Thames Towboat, and the other companies involved, according to Richard MacMurray.
4. The offer was extended to purchase treasury stock from current stockholders at approximately \$10,000 for each 1% of Company stock, or approximately \$1,033.06 per share. This is the same offer as last year as the Company is not in a position to increase its offer.
5. The Company anticipates continued competition from Block Island Express and the Quonsett Point to Martha's Vineyard fast ferry. The Company is not sure of the level of competition it will be facing from the fast ferry from Montauk to Block Island and New Bedford, especially since parking is an issue at the Montauk ferry terminal.
6. The Company is waiting for the issuance of a Certificate of Occupancy on the Point Judith passenger terminal. The new Point Judith freight operation is a success and there are no traffic issues; it appears to be working well. This project is paid for in part by Federal funds and in part by the Company's own cash.
7. As to the Filippi Marina, the Company has taken an appeal to the Superior Court regarding the CRMC issuance of the marina permit.

8. The Island Hi-Speed Ferry court case, in which the Company appealed the increase in capacity from 149 to 250 passengers, is on hold because of the lease by the Company of the vessel.
9. The Company was granted a CPCN for a fast ferry between Point Judith, Block Island, and Newport. A revision to the CPCN has put Newport on hold for this year only. The Company will operate the M/V Athena using this fast ferry CPCN.
10. The minority stockholders argued for distribution of dividends. However, Mr. Edge gave a report of the uses of the cash on hand, which is not sufficient to meet all needs. There is a possibility of a dredging project in Montville this fall. The Company is waiting for an okay on the disposal of the material. Funds are also needed for the terminal renovation, for lease of the fast ferry, for working capital needs, and for possible purchase of the a fast ferry. Therefore, any profits will have to be reinvested rather than distributed as dividends.
11. There are three asbestos cases which are being handled by an asbestos law firm and are inactive. The carrier is on notice.
12. The Company is generally settling small personal injury cases within the insurance deductible and putting the carriers on notice.
13. With respect to legislation and item 11 on the 2005 Minutes, it was reported that the increase in the fuel surcharge cap from 50¢ per ticket to \$3.00 per ticket has been approved and the law has been amended.

On each issue discussed, input from the minority shareholders was sought, all questions were answered, and the meeting did not end until there were no more questions posed.

There being no further business to come before the meeting, the meeting adjourned at 11:20 p.m.

  
\_\_\_\_\_  
Susan E. Linda, Secretary

# AGENDA

## INTERSTATE - ANNUAL MEETING

- ✓ Attendance sheet.
- ✓ Moment of Silence to Honor the passing of Anna C. Wronowski
- ✓ 1. ✓ Approval of 2005 minutes and signature of secretary.
- ✓ 2. ✓ Election of directors and officers.
- ✓ 3. Summary of financial results as of 11/30/05.
- ✓ 4. ✓ Vote to authorize rate increase filing at the RI PUC. *for 2007 calendar year.*
- ✓ 5. ✓ Vote to ratify lease of M/V Athena
- ✓ 6. ✓ Stock swap/purchase negotiations update.
- ✓ 7. ✓ Possibility of purchasing treasury stock from current stockholders at approximately \$10,000 per 1% of the company stock or approximately ~~\$516.53~~ per share (see Exhibit A).  
\$ 1033.06
- ✓ 8. ✓ Anticipated impact from continued competition from the high speed ferry from Quonset Point to Martha's Vineyard, the high speed ferry from New London to Block Island, and the high speed ferry from Montauk to Block Island and New Bedford.
- ✓ 9. ✓ Status of Point Judith terminal project.
- ✓ 10. ✓ Filippi Marina status.
- ✓ 11. ✓ Island Hi-Speed Ferry Superior Court case regarding 250 passengers (on hold).
- ✓ 12. ✓ Interstate granted a CPCN for a high speed ferry between Point Judith and Newport. Revision to CPCN for this year only to put Newport on hold.
- ✓ 13. ✓ Uses of cash and inability to distribute dividends.

- ✓ Cash needs for the dredging at Montville.
- ✓ Cash needs for the terminal renovation project.
- ✓ Cash needs for possible purchase of a high speed ferry.
- ✓ Cash needs for working capital and to cover costs in winter

14. ✓ Asbestos cases (3) – handled by asbestos law firm – (inactive).

15. ✓ Small personal injury cases covered by insurance.

16. ✓  $3^{rd}$  cap pressed for fuel survival  
(increased from 50¢).

Interstate Navigation Company, a Connecticut corporationShareholdings as of 12/31/04:

	<u>Class A</u> <u>Voting</u>	<u>Class B</u> <u>Non Voting</u>	
Susan Linda	96	0	= 96 x 1,033.06 = \$99,173.76
Anna C. Wronowski	0	412	= 412 x 1,033.06 = \$425,620.72
Raymond & Susan Linda	16	282	= 298 x 1,033.06 = \$307,851.88
Craig Hewitt	5-1/3	100-2/3	= 106 x \$1,033.06 = \$109,504.36
Mary Jo McInerney	5-1/3	100-2/3	= 106 x \$1,033.06 = \$109,504.36
Byron Hewitt	5-1/3	100-2/3	= 106 x \$1,033.06 = \$109,504.36
Derek S. Tyrseck	8	151	= 159 x \$1,033.06 = \$164,256.54
Thomas Tyrseck	8	151	= 159 x \$1,033.06 = \$164,256.54
Trust for Carol Jean Wronowski	16	160	= 176 x 1,033.06 = \$181,818.56
Adam Wronowski	16	231	= 247 x 1,033.06 = \$255,165.82
John Peter Wronowski, as Custodian for Jessica Wronowski	0	71	= 71 x 1,033.06 = \$73,347.26
TOTAL:	<u>176</u>	<u>1,760</u>	

Officers:

- Susan Linda, President, Secretary & Treasurer
- Joshua Linda, Vice President

Directors:

- Susan Linda
- Joshua Linda
- Raymond Linda

# John G. Kanabis

*Certified Public Accountant*  
326 State Street, Suite 204  
New London, Connecticut 06320

John A. Kanabis, CPA  
Lisa V. Peabody, CPA

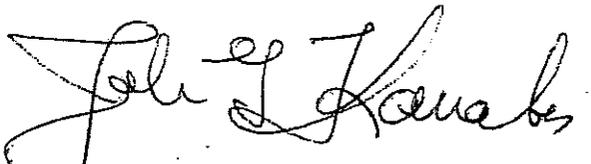
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Fax (860) 444-1699

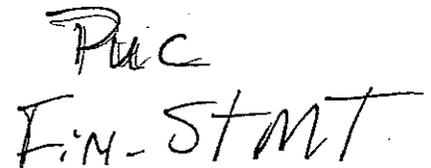
To the Board of Directors  
Interstate Navigation Co., Inc.  
New London, Connecticut

I have compiled the accompanying balance sheet of Interstate Navigation Co., Inc. as of November 30, 2005 and the related statement of income and retained earnings for the six-month period then ended, and the accompanying supplementary information contained in Schedule I, which is presented only for supplementary analysis purposes, in accordance with Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements and supplementary schedule information that is the representation of the management. I have not audited or reviewed the accompanying financial statements and supplementary schedule and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all the disclosures and the statement of cash flows required by generally accepted accounting principles. If the omitted disclosures and statements of cash flows were included in the financial statements, they might influence the user's conclusions about the Company's financial position, results of operations, and cash flows. Accordingly, these financial statements are not designed for those who are not informed about such matters.

  
February 28, 2006



INTERSTATE NAVIGATION CO., INC.

BALANCE SHEET

FOR THE SIX-MONTH PERIOD ENDED NOVEMBER 30, 2005

ASSETS

CURRENT ASSETS			
Cash		\$ 2,473,649	11/30/05
Accounts Receivable		218,128	3,898,3
Prepaid Taxes and Expenses		133,387	
Loans-Employees		59,980	
Deferred Income Taxes		93,315	
		<u>2,978,459</u>	
Total Current Assets			
PROPERTY, VESSELS AND EQUIPMENT		22,354,222	
Less: Accumulated Depreciation		(10,109,916)	
Net Depreciated Value		12,244,306	
Capital Additions in Progress		458,238	
		<u>12,702,544</u>	11,173,17
Total Property, Vessels and Equipment			
OTHER ASSETS			
Restricted Cash		494,450	
Deposits		1,000	
		<u>495,450</u>	
Total Other Assets			
TOTAL ASSETS		<u>\$ 16,176,453</u>	

See accompanying accountant's report.

INTERSTATE NAVIGATION CO., INC.

BALANCE SHEETS

NOVEMBER 30, 2005

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES:

Current Portion of Notes Payable	\$ 516,354
Accounts Payable	
Trade	229,534
Related Entities	31,554
Accrued Taxes and Expenses	465,478
Accrued Profit Sharing	55,600
Deferred Revenue	8,688
	<hr/>
Total Current Liabilities	1,307,208

*1/1/05*

LONG-TERM LIABILITIES:

Notes Payable	10,190,153
Advances Payable-Related Entity	17,500
	<hr/>
Total Long-Term Liabilities	10,207,653

TOTAL LIABILITIES

11,514,861

STOCKHOLDERS' EQUITY:

Capital Stock	
Common Voting, \$100 Par Value, Authorized 500 Shares Issued and Outstanding 176 Shares	17,600
Capital Surplus	382,951
Retained Earnings	4,261,041
	<hr/>
TOTAL STOCKHOLDERS' EQUITY	4,661,592

~~170,000~~

4,435,046

TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY

\$ 16,176,453

See accompanying accountant's report.

INTERSTATE NAVIGATION CO., INC.

STATEMENTS OF INCOME AND RETAINED EARNINGS

FOR THE SIX-MONTH PERIOD ENDED NOVEMBER 30, 2005

OPERATING REVENUES	\$ 6,554,970	<u>118,110</u> <u>6,049,14</u>
OPERATING EXPENSES		
Payroll	1,560,407	
Repairs and Maintenance	178,310	
Depreciation and Amortization	545,576	
Fuel and Lube	752,349	
Wharfage and Rent	182,110	
Supplies	171,297	
Utilities	52,832	
Terminal and Traffic Expenses	561,452	
General and Administrative	404,420	
Insurance and Casualties	300,850	
Payroll Taxes	167,753	
Other Taxes	103,898	
Other Vessel Expense	27,044	
Pension and Profit Sharing	<u>60,218</u>	
 Total Operating Expenses	 <u>5,068,516</u>	 <u>5,087,53</u>
OPERATING INCOME	<u>1,486,454</u>	
OTHER INCOME (EXPENSES)		
Interest Expense	(357,265)	(218,505)
Interest Income	<u>20,408</u>	
 Total Other Income (Expense)	 <u>(336,857)</u>	
INCOME BEFORE INCOME TAXES	1,149,597	
Provision for Federal Income Tax	<u>(390,875)</u>	
NET INCOME	758,722	<u>839,610</u>
	<u>80,000</u>	
RETAINED EARNINGS, BEGINNING OF PERIOD	<u>3,502,319</u>	
RETAINED EARNINGS, END OF PERIOD	<u>\$ 4,261,041</u>	

See accompanying accountant's report.

INTERSTATE NAVIGATION CO., INC.

SCHEDULE I - SALARIES OF OFFICERS AND GENERAL MANAGER

FOR THE SIX-MONTH PERIOD ENDED NOVEMBER 30, 2005

OFFICERS

Susan Linda, President and Secretary	\$ 59,400
Joshua Linda, Vice President	<u>45,770</u>
	<u>\$ 105,170</u>

GENERAL MANAGER

Raymond Linda	<u>\$ 56,430</u>
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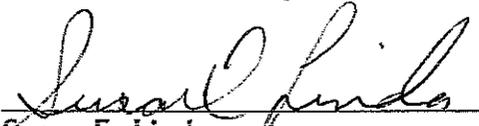
See accompanying accountant's report.

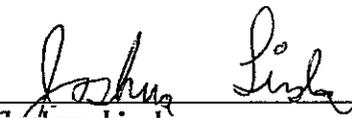
DIRECTORS' CONSENT TO ACTION WITHOUT A MEETING

The undersigned, being all of the Directors of The Interstate Navigation Co, Inc., a/k/a Interstate Navigation Co., Inc., hereby consent to the actions set forth herein which are to be taken by the corporation. This Consent is made and executed in accordance with Article III, Section 10 of the Bylaws of the Corporation and shall have the same force and effect as would our unanimous vote in favor of such action at a duly constituted meeting of the Board of Directors.

"BE IT RESOLVED, that the President of this Corporation, and Michael R. McElroy, legal counsel to the Corporation be, and they hereby, are authorized for and on behalf of said corporation (1) to execute a certain letter agreement dated November 16, 2005, for the purchase of all the assets of Island Hi-Speed Ferry LLC (IHSF) which consist primarily of the *M/V Athena* and a Certificate of Public Convenience and Necessity, as well as customer lists, non-compete agreement, good will, and berthing permit, and any other assets related to IHSF's Rhode Island ferry business for the sum of \$5,612,500, together with any subsequent purchase and sale agreement related thereto, (2) to execute a certain loan agreement, note, mortgage, and all other necessary or desirable documents needed to borrow up to \$5,612,500 from the Washington Trust Company, or any other lender, to purchase the aforesaid assets of IHSF, (3) to execute any and all documents necessary to obtain any and all necessary or desirable approvals for the aforesaid transaction, including but not limited to approvals from the Rhode Island Division of Public Utilities and Carriers and the Rhode Island Public Utilities Commission, and (4) to further execute all documents necessary and/or desirable in the opinion of those authorized as aforesaid in order to consummate the acquisition of the Rhode Island assets and ferry business of IHSF as in the judgment of said President or legal counsel may be deemed appropriate.

IN WITNESS WHEREOF we have hereunto affixed our names as Directors of said corporation on this 28 day of December, 2005.

  
\_\_\_\_\_  
Susan E. Linda

  
\_\_\_\_\_  
Joshua Linda

  
\_\_\_\_\_  
Raymond Linda

**MINUTES OF THE ANNUAL MEETING  
OF  
INTERSTATE NAVIGATION COMPANY**

The Annual Meeting of Interstate Navigation Company (the "Company") was held on May 31, 2005 at 2:00 p.m. at the offices of the Company at Eugene O'Neill Drive, New London, Connecticut.

The following shareholders were present at the meeting: Susan Linda, Raymond Linda, Attorney Robert Tobin (pursuant to a proxy for Jessica Wronowski), and Adam Wronowski.

Also present were Joshua Linda, Vice President and Director, Michael R. McElroy, Esq., and Mark E. Block, Esq., both counsel to the Company, Mr. Walter Edge, C.P.A., regulatory accountant for the Company, and Richard MacMurray.

Mr. Block acted as moderator of the meeting, and the meeting was called to order by the President of the Company, Susan Linda.

The first order of business was the election of officers and directors of the Company. Susan Linda nominated herself for President, Treasurer, Secretary and Director, Joshua Linda as Vice President and Director, and Raymond Linda as Director. No other slate of officers and directors was proposed. The proposed slate of officers and directors was elected by a majority vote.

The minutes of the 2004 Annual Meeting were approved.

The next item was such other business as may come before the meeting. Attorney McElroy presented an agenda of items to be reviewed at the meeting (attached hereto).

Mr. Edge made a presentation concerning the financial activity and status of the company since the last annual meeting. A balance sheet and income sheet as of November 30, 2004, prepared by John G. Kanabis, the Company's accountant was distributed and is attached hereto.

Mr. Edge and Attorney McElroy reported on the rate increase that was granted to the Company:

- a. The rate increase was in the amount of \$1,456,061 and was effective May 28, 2004.
- b. The Company assets increased by \$3,000,000 as a result of the purchase of the Anna C.
- c. The Company liabilities also increase by \$3,000,000 as a result of the debt incurred from the purchase of the Anna C.

- d. Operating revenue increased \$1,151,000 on an annualized basis, 80% of which was as a result of the rate increase, and mostly attributable to vehicle traffic.
- e. Revenue was up 24%.
- f. Operating expenses of \$668,000 are up 17%.
- g. Operating income is up \$482,000.
- h. Fuel cost is up \$200,000.
- i. Ridership is relatively flat.

Mr. McElroy then made a presentation of the following matters which occurred since the last Annual Meeting.

1. The Old Harbor lease expired on September 30, 2004. The lease was renewed on a month to month basis because Interstate Nav. would not sign a new long term lease. The PUC refused to approve the increased lease amounts requested in the rate filing because Interstate Nav. did not sign a new long term lease.
2. Negotiations for a stock swap/purchase with the other shareholders and the related companies are still ongoing.
3. The Company made an increased offer to purchase the stock owned by any shareholder based upon a price of \$1,033.06/1% of stock owned, which is twice the offer communicated at last years Annual Meeting (see attached Exhibit A).
4. The Company 's port security plans have been fully approved by the Coast Guard for vessels and facilities.
5. The impact from the increased competition from the Island Hi-Speed Ferry, the Quonset Point high-speed ferry, and the New London high speed ferry are expected to be felt more severely in passenger ridership this coming summer. However, the base summer Company income from cars and freight will not be impacted.
6. The docking in Old Harbor has been worked out through the cooperative efforts of Joshua Linda and Adam Wronowski, and it worked relatively well this past year.
7. The appeal of the assessment of the Old Harbor property was successful. The valuation was lowered from \$7.0 MM to \$3.5MM. Attorney Tobin's assistance in the appeal was noted.
8. The repairs to the Carol Jean have been completed and she is presently operating. The public reception to the renovations has been very positive.
9. The renovation project for the Point Judith terminal was discussed. The work has received partial federal funding. The initial bid for the work was \$1.2MM with funding

of \$500,000 available. The project was bid a second time and the low bid was \$800,000, and the project is proceeding.

10. Dredging at the Montville Dock is at a stand still. Clean capping material is need, and the Company will need to renew its permit.
11. Legislation:
  - A. Through the efforts of the Company's lobbyist, a law was passed which provides that if there is a finding by the PUC of public convenience and necessity for water carriers to have new equipment (i.e. a high speed ferry) then any stay pending appeal of the Division's decision would be ineffective. The Company has applied for approval for the operation of a high speed ferry between Point Judith, Newport, and Block Island.
  - B. The Company is trying to get approval of a bill to increase the fuel surcharge cap from a maximum 50 cents per ticket to a maximum of \$3.00 per ticket.
12. The Company plans to appeal any decision granting the pending application related to the Filippi Dock.
13. The appeal related to the Company's request to see the information submitted by Island Hi-Speed Ferry, which was kept secret by the PUC, is now moot.
14. Island Hi-Speed Ferry has proposed a new rate structure which will drop its rates for season passes and group discounts. This will result in a drop below the \$26 floor in the Company's rates. The Company has opposed this new rate structure, but the Company believes that Island Hi-Speed Ferry will get approval for their new rates.
15. The Superior Court case relating to the 250 passenger issue is presently on hold.
16. The Company's application to the Division for a high speed ferry certificate of public convenience and necessity is scheduled to begin hearings on June 13, 2005.
17. Attorney McElroy presented the following reasons that the Company cannot declare dividends:
  - a. Cash needs for the renovation of the Carol Jean. The Company's line of credit was exhausted, and will be repaid with excess cash.
  - b. Cash needs for the dredging at Montville.
  - c. Cash needs for the terminal renovation project.
  - d. Cash needs to cover possible decreases in revenue due to additional competition from the high speed ferries.
  - e. Cash to possibly purchase a high speed ferry.
  - f. Cash for possible purchase of the Southland, which is not PUC regulated.

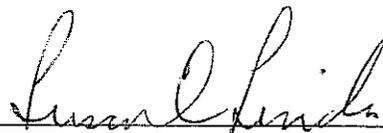
- g. Cash for possible purchase of Barnaby's Dock (formerly the Sunflower). This would give the Company control of the whole "Block," in Galilee and provide space to expand offices.

Mr. Tobin objected on behalf of the minority shareholders to the failure to distribute dividends.

- 18. The Company rejected a proposal by Island Hi-Speed Ferry to sell the Athena and its Certificate of Public Convenience and Necessity for \$7.9MM.
- 19. The Company will renew its 50¢ per adult passenger landing fee contract with the Town of New Shoreham. This is based upon Island Hi-Speed Ferry's promise to pay landing fees for 2004, and Block Island Express agreed to pay at least \$40,000 per year that it had previously refused to pay.
- 20. There are three (3) asbestos cases being handled by an outside law firm which are inactive cases.
- 21. The Company's line of credit with Washington Trust Company has been increased from \$400,000 to \$500,000. The extra \$100,000 is unsecured.
- 22. The Company paid \$70,000 from its restricted account to settle the Narragansett tax case involving \$85,000 in landing fees.
- 23. There are several small personal injury cases pending which are covered by insurance.

On each issue discussed, input from the minority shareholders was sought, and all questions were answered and the meeting did not end until there were no more questions posed.

There being no further business to come before the meeting, the meeting adjourned at 2:55 p.m.

  
\_\_\_\_\_  
Susan Linda, Secretary

Interstate Navigation Company, a Connecticut corporationShareholdings as of 12/31/04:

	<u>Class A</u> <u>Voting</u>	<u>Class B</u> <u>Non Voting</u>	
Susan Linda	96	0	= 96 x 1,033.06 = \$99,173.76
Anna C. Wronowski	0	412	= 412 x 1,033.06 = \$425,620.72
Raymond & Susan Linda	16	282	= 298 x 1,033.06 = \$307,851.88
Craig Hewitt	5-1/3	100-2/3	= 106 x \$1,033.06 = \$109,504.36
Mary Jo McInerney	5-1/3	100-2/3	= 106 x \$1,033.06 = \$109,504.36
Byron Hewitt	5-1/3	100-2/3	= 106 x \$1,033.06 = \$109,504.36
Derek S. Tyrseck	8	151	= 159 x \$1,033.06 = \$164,256.54
Thomas Tyrseck	8	151	= 159 x \$1,033.06 = \$164,256.54
Trust for Carol Jean Wronowski	16	160	= 176 x 1,033.06 = \$181,818.56
Adam Wronowski	16	231	= 247 x 1,033.06 = \$255,165.82
John Peter Wronowski, as Custodian for Jessica Wronowski	0	71	= 71 x 1,033.06 = \$73,347.26
TOTAL:	<u>176</u>	<u>1,760</u>	

Officers:

- Susan Linda, President, Secretary & Treasurer
- Joshua Linda, Vice President

Directors:

- Susan Linda
- Joshua Linda
- Raymond Linda

# John G. Kanabis

*Certified Public Accountant*  
326 State Street, Suite 204  
New London, Connecticut 06320

John A. Kanabis, CPA  
Lisa V. Peabody, CPA

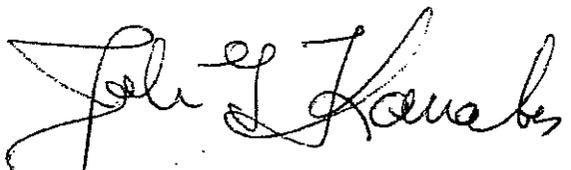
(860) 442-0475  
Fax (860) 444-1699

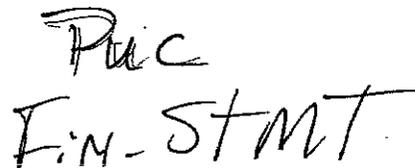
To the Board of Directors  
Interstate Navigation Co., Inc.  
New London, Connecticut

I have compiled the accompanying balance sheet of Interstate Navigation Co., Inc. as of November 30, 2005 and the related statement of income and retained earnings for the six-month period then ended, and the accompanying supplementary information contained in Schedule I, which is presented only for supplementary analysis purposes, in accordance with Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements and supplementary schedule information that is the representation of the management. I have not audited or reviewed the accompanying financial statements and supplementary schedule and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all the disclosures and the statement of cash flows required by generally accepted accounting principles. If the omitted disclosures and statements of cash flows were included in the financial statements, they might influence the user's conclusions about the Company's financial position, results of operations, and cash flows. Accordingly, these financial statements are not designed for those who are not informed about such matters.

  
February 28, 2006



INTERSTATE NAVIGATION CO., INC.

BALANCE SHEET

FOR THE SIX-MONTH PERIOD ENDED NOVEMBER 30, 2005

ASSETS

CURRENT ASSETS	
Cash	\$ 2,473,649
Accounts Receivable	218,128
Prepaid Taxes and Expenses	133,387
Loans-Employees	59,980
Deferred Income Taxes	93,315
Total Current Assets	<u>2,978,459</u>
PROPERTY, VESSELS AND EQUIPMENT	
Less: Accumulated Depreciation	22,354,222 <u>(10,109,916)</u>
Net Depreciated Value	12,244,306
Capital Additions in Progress	<u>458,238</u>
Total Property, Vessels and Equipment	<u>12,702,544</u>
OTHER ASSETS	
Restricted Cash	494,450
Deposits	<u>1,000</u>
Total Other Assets	<u>495,450</u>
TOTAL ASSETS	<u>\$ 16,176,453</u>

See accompanying accountant's report.

INTERSTATE NAVIGATION CO., INC.

BALANCE SHEETS

NOVEMBER 30, 2005

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES:	
Current Portion of Notes Payable	\$ 516,354
Accounts Payable	
Trade	229,534
Related Entities	31,554
Accrued Taxes and Expenses	465,478
Accrued Profit Sharing	55,600
Deferred Revenue	8,688
	<hr/>
Total Current Liabilities	1,307,208
LONG-TERM LIABILITIES:	
Notes Payable	10,190,153
Advances Payable-Related Entity	17,500
	<hr/>
Total Long-Term Liabilities	10,207,653
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TOTAL LIABILITIES	11,514,861
STOCKHOLDERS' EQUITY:	
Capital Stock	
Common Voting, \$100 Par Value,	
Authorized 500 Shares	
Issued and Outstanding 176 Shares	17,600
Capital Surplus	382,951
Retained Earnings	4,261,041
	<hr/>
TOTAL STOCKHOLDERS' EQUITY	4,661,592
	<hr/>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 16,176,453
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See accompanying accountant's report.

INTERSTATE NAVIGATION CO., INC.

STATEMENTS OF INCOME AND RETAINED EARNINGS

FOR THE SIX-MONTH PERIOD ENDED NOVEMBER 30, 2005

OPERATING REVENUES	<u>\$ 6,554,970</u>
OPERATING EXPENSES	
Payroll	1,560,407
Repairs and Maintenance	178,310
Depreciation and Amortization	545,576
Fuel and Lube	752,349
Wharfage and Rent	182,110
Supplies	171,297
Utilities	52,832
Terminal and Traffic Expenses	561,452
General and Administrative	404,420
Insurance and Casualties	300,850
Payroll Taxes	167,753
Other Taxes	103,898
Other Vessel Expense	27,044
Pension and Profit Sharing	<u>60,218</u>
Total Operating Expenses	<u>5,068,516</u>
OPERATING INCOME	<u>1,486,454</u>
OTHER INCOME (EXPENSES)	
Interest Expense	(357,265)
Interest Income	<u>20,408</u>
Total Other Income (Expense)	<u>(336,857)</u>
INCOME BEFORE INCOME TAXES	1,149,597
Provision for Federal Income Tax	<u>(390,875)</u>
NET INCOME	758,722
RETAINED EARNINGS, BEGINNING OF PERIOD	<u>3,502,319</u>
RETAINED EARNINGS, END OF PERIOD	<u><u>\$ 4,261,041</u></u>

See accompanying accountant's report.

INTERSTATE NAVIGATION CO., INC.

SCHEDULE I - SALARIES OF OFFICERS AND GENERAL MANAGER

FOR THE SIX-MONTH PERIOD ENDED NOVEMBER 30, 2005

OFFICERS

Susan Linda, President and Secretary	\$ 59,400
Joshua Linda, Vice President	<u>45,770</u>
	<u>\$ 105,170</u>

GENERAL MANAGER

Raymond Linda	<u>\$ 56,430</u>
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See accompanying accountant's report.

TOWN-30 Please state whether Interstate has ever applied for Homeland Security port security grants? If not, please explain.

**Response:** Yes.

Prepared by WEE

TOWN-31 Please provide the test year earned return on (a) common equity and (b) rate base. Provide supporting workpapers.

**Response:** See Schedule WEE-1 in this filing.

Prepared by WEE

TOWN-32 Does Interstate acknowledge that its existing fast ferry rate is not based upon a fully allocated cost of service study performed by Interstate with respect to its own fast ferry operations?

**Response:** Yes.

Prepared by WEE

TOWN-33 Please provide Interstate's most recent annual financial statement and its most recent annual report. Update this response as such reports become available for the most recent fiscal year.

**Response:** Interstate's most recent annual report (May 31<sup>st</sup> 2005) is on file at the Division and has been provided to the Town previously. Interstate's most recent financial statement (6 months ending 11/30/05) is attached to Interstate's 2006 annual meeting minutes provided in Town-29. Interstate does not provide its annual (year end May 31<sup>st</sup>) financial statements because they are unaudited and the information is the same as the PUC annual report. Interstate will provide the May 31<sup>st</sup> 2006 annual report as soon as it is ready.

Prepared by WEE