

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 MIKE GLEASON  
CHAIRMAN

3 WILLIAM A. MUNDELL  
COMMISSIONER

4 JEFF HATCH-MILLER  
COMMISSIONER

5 KRISTIN K. MAYES  
COMMISSIONER

6 GARY PIERCE  
COMMISSIONER

7  
8 IN THE MATTER OF THE APPLICATION OF  
9 ARIZONA-AMERICAN WATER COMPANY,  
10 INC., AN ARIZONA CORPORATION, FOR A  
11 DETERMINATION OF THE CURRENT FAIR  
12 VALUE OF ITS UTILITY PLANT AND  
13 PROPERTY AND FOR INCREASES IN ITS  
14 RATES AND CHARGES BASED THEREON  
15 FOR UTILITY SERVICE BY ITS PARADISE  
16 VALLEY WATER DISTRICT.

Docket No. W-01303A-05-0405

13 IN THE MATTER OF THE APPLICATION OF  
14 ARIZONA-AMERICAN WATER COMPANY  
15 FOR APPROVAL OF AN AGREEMENT  
16 WITH THE PARADISE VALLEY COUNTRY  
17 CLUB.

Docket No. W-01303A-05-0910

16 **RUCO'S CLOSING BRIEF**

17 **INTRODUCTION**

18 The Residential Utility Consumer Office ("RUCO") submits this Brief in opposition to  
19 the proposed Rate Design Agreement ("Agreement") submitted on behalf of the Town of  
20 Paradise Valley, the Camelback Inn, the Sanctuary on Camelback Mountain and the  
21 Renaissance Scottsdale Resort (collectively the "Signatories"). RUCO supports the Arizona  
22 Corporation Commission Staff's ("Staff") proposal to provide interim relief to the Paradise  
23 Valley District's residential and resort customers by reducing the High Usage Surcharge  
24 ("HUS") from the current \$2.15 per 1,000 gallons to \$1.00 per 1,000 gallons. RUCO also

1 supports Staff's recommendation to eliminate the Public Safety Surcharge ("PSS") until the  
2 Commission has the opportunity to examine the fire flow issue in the Company's next rate  
3 case proceeding. RUCO-2 at 2<sup>1</sup>.

4  
5 **THE COMMISSION SHOULD REJECT THE AGREEMENT PROPOSED BY THE**  
6 **SIGNATORIES.**

7 The Agreement, in relevant part, provides for the following:

8 1) A reduction of the existing HUS from \$2.15 to \$1.00 per 1,000 gallons of water  
9 sold effective March 1, 2008. The reduced HUS would recover all un-recovered fire flow  
10 improvement costs incurred up to the end of February 2008 and would continue to be booked  
11 by the Company as CIAC. T-1 at 3.

12 2) On March 1, 2008 the existing \$1.00 per 1,000 gallons PSS would be reset to  
13 \$0.00 and would subsequently be replaced with an Arsenic Cost Recovery Mechanism  
14 ("ACRM") like mechanism that would allow for regular step increases to recover the costs  
15 associated with new fire flow plant at the Commission approved 10.40 percent cost of equity.  
16 T-1 at 3.

17 3) The PSS would continue to apply only to the commodity portion of the rate, and  
18 the first step increase filing would likely occur in the later part of 2008 after Phase 3 of the fire  
19 flow project is completed. A charge of \$0.125 per 1,000 gallons of water is estimated for the  
20 first step increase under the proposed ACRM-like mechanism. T-1 at 3.

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22  
23 <sup>1</sup> For ease of reference, trial exhibits will be identified similar to their identification in the Transcript of  
24 Proceedings. The Transcript page number will identify references to the Transcript.

1           4)     For fire flow plant construction phases completed after March 1, 2008, the PSS  
2 would be designed to recover fifty percent of the investment in the improvements. The  
3 revised HUS would cover the remaining fifty percent, at least until a final order is issued by  
4 the ACC in Arizona-American's next rate case proceeding before the Commission. T-1 at 4.

5           5)     All other rate design features of the HUS and PSS and accounting deferrals  
6 would remain in their present form until a final order is issued by the ACC in Arizona-  
7 American's next rate case proceeding. T-1 at 4.

8           6)     During Arizona-American's next rate case proceeding, the Company will  
9 request that the proceeds from the HUS be no longer treated as CIAC, but instead be treated  
10 as an investment in plant in service that would provide the Company with a return on  
11 investment and be fully recoverable in rates. The other Signatories will join in the Company's  
12 request. T-1 at 4.

13          7)     The Rate Design Agreement provides a timetable for the completion of Phases  
14 3 through 7 of the fire flow improvements, but has no cost estimates for Phases 5 through 7.  
15 T-1 at 4.

16          RUCO opposes the Agreement for several reasons. First, the Agreement would  
17 terminate the current PSS, reset it to zero and then re-establish the PSS in ACRM-like step  
18 increase filings upon completion of each fire-flow construction phase. T-1 at 3. The ACRM-  
19 like mechanism will only consider cost increases in one category of expenses and will ignore  
20 changes in revenues, cost of capital, rate base and other expense categories. RUCO-1 at 3.  
21 Ratepayers will not enjoy the benefits of efficiencies or other potential off-sets to costs since  
22 the sole focus of the step reviews will be the incremental fire flow construction costs. This is  
23 "single-issue" ratemaking and is "fraught with potential abuse." See Scates v. Arizona  
24 Corporation Commission, 118 AZ. 531, 534, 578 P.2d 612, 615 (1978). To the extent the

1 Commission is willing to consider such mechanisms, it should only do so under the most dire  
2 and extreme circumstances. Approving a mechanism for the recovery of discretionary  
3 projects that are not in the purview of what the Commission regulates does not qualify for this  
4 extraordinary ratemaking device.

5 The ACRM was the result of a change in the federal law which did not provide water  
6 companies with an alternative. No one questioned that to comply with the new federal  
7 arsenic standard, numerous water utilities would have to expend large amounts of capital in a  
8 relatively short time to build the infrastructure. In addition, there would be operation and  
9 maintenance costs. RUCO, Staff and the water utilities all understood the unique situation  
10 confronting the water utilities because of the new law, and worked hard to come up with a  
11 cost recovery mechanism that was fair to ratepayers and allowed timely cost recovery.  
12 While the ACRM raises the same concerns addressed by the *Scates* decision, the  
13 mechanism became unavoidable given the federal mandate and its simultaneous impact on  
14 a large number of Arizona water systems.

15 Here, the Signatories are proposing a similar mechanism be applied to remedy biased  
16 rates that are currently being paid by certain classes of ratepayers (high-end users). These  
17 same ratepayers advocated for the fire flow construction in the underlying case. These  
18 ratepayers knew the estimated costs of the construction, and that the costs would be  
19 recovered through rates. The situation here is not the same as the case with the Arsenic  
20 Cost Recovery Mechanism, and the Commission should not disregard tried and proven  
21 ratemaking principles in an effort to provide a group of ratepayers short-term relief from  
22 something that they originally advocated for.

23 Second, the step increases will fund future rate hikes that have no definite cost at this  
24 time. RUCO-1 at 9. Paragraph III (G) of the Agreement sets forth the current construction

1 schedule for the fire flow projects. T-1 at 4. The estimated costs for Phases 5, 6, 7 are  
2 “TBD”. The entire project was estimated at \$16.1 million. Transcript at 315. The final  
3 estimate now is unknown but “it’s significantly higher” than the \$16.1 million estimate.  
4 Transcript at 96. The Commission’s approval of the Agreement with an ACRM-like  
5 mechanism that allows for an unspecified number of step-increases to recover an  
6 undetermined amount of costs could well be the same as handing a blank check to the  
7 Company. RUCO-1 at 10.

8 Third, the Agreement is ambiguous, and should not be approved. RUCO has stated  
9 clearly that all things being equal, it would consider a modification to the rate design that  
10 holds classes not otherwise adversely affected by the current rate design harmless (i.e.  
11 customers that are not high-end users). However, RUCO would oppose any modification of  
12 the current rate design that shifts the costs from the high-end users to the low-end users.  
13 The proposed ACRM-like mechanism will recover the fire flow construction costs through  
14 step-increases. The Agreement is silent on which ratepayers will be paying for the  
15 increases. In the past, where the Commission has approved an ACRM, the step-increases  
16 have always applied to all the ratepayers in the affected district. If the ACRM-like mechanism  
17 is allocated in this manner, it would shift the costs from the high-end users to the low-end  
18 users. However, the Agreement does not define how the ACRM-like mechanism would be  
19 allocated to end-users. At the hearing in this matter, the expert witness for the Resorts (the  
20 Camelback Inn, the Sanctuary on Camelback Mountain and the Renaissance Scottsdale  
21 Resort), John Thornton, testified that the modified PSS surcharge will be recovered only from  
22 “those blocks where the current PSS applies.” Transcript at 240. During cross-examination,  
23 Mr. Thornton explained that the signatories’ intention to apply the modified PSS to the same  
24

1 blocks that the current PSS applies, is memorialized in paragraph III (E) of the Agreement.  
2 Transcript at 240-242. Paragraph III (E) of the Agreement provides as follows:

3 E. All other rate design features of these two  
4 surcharge and accounting deferrals would remain  
5 as they presently exist until modified by a final  
6 order in Arizona-American's next rate case for the  
7 Paradise Valley Water District.

8 Regardless of the intent of the signatories, nowhere in the Agreement, including  
9 paragraph III (E) do the signatories specify which ratepayers will be paying the step-  
10 increases. It is subject to interpretation, and for this reason the Agreement is ambiguous and  
11 should be rejected.

12 Finally, it is not appropriate to treat the proceeds of the HUS as revenue, because  
13 they are ratepayer-supplied funds provided for the purpose of funding fire-flow plant. RUCO-  
14 1 at 12. Since these funds are not being provided by Arizona-American's investors, it would  
15 be unfair for the Company to earn a rate of return on them. Id. The Commission should  
16 reject the Agreement's proposal to allow the Company to earn a return on HUS proceeds  
17 after the next rate case.

## 18 **CONCLUSION**

19 The Commission should reject the Agreement. The Commission should approve  
20 Staff's recommendation to provide interim relief to the Paradise Valley District's residential  
21 and resort customers by reducing the HUS from the current \$2.15 per 1,000 gallons to \$1.00  
22 per 1,000 gallons, and to eliminate the PSS until the Commission has the opportunity to  
23 examine the fire flow issue in the Company's next rate case proceeding.  
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1 RESPECTFULLY SUBMITTED this 13<sup>th</sup> day of June 2008.

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3  
4  Daniel Pozefsky  
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5  
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8 of June 2008 with:

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