



BEFORE THE ARIZONA CORPORATION COMMISSION

DOCKETED

WILLIAM A. MUNDELL
CHAIRMAN
JIM IRVIN
COMMISSIONER
MARC SPITZER
COMMISSIONER

FEB 02 2001

DOCKETED BY [Signature]

IN THE MATTER OF THE APPLICATION OF
THE AGUA FRIA WATER DIVISION OF
CITIZENS COMMUNICATIONS COMPANY FOR
AN ACCOUNTING ORDER AUTHORIZING A
HOOK-UP FEE FOR RECOVERY OF DEFERRED
CENTRAL ARIZONA PROJECT EXPENSES AND
FOR RELATED ACCOUNTING TREATMENT.

DOCKET NO. W-01032B-00-0205

DECISION NO. 63334

ORDER

Open Meeting
January 30 & 31, 2001
Phoenix, Arizona

BY THE COMMISSION:

On March 29, 2000, the Agua Fria Water Division ("Agua Fria" or "Division") of Citizens Communications Company ("Citizens") submitted a tariff application to the Arizona Corporation Commission ("Commission") seeking approval of the implementation of a hook-up fee to be assessed on builders and developers for recovery of deferred Central Arizona Project ("CAP") capital costs. On October 12, 2000, the Commission's Utilities Division Staff ("Staff") field testimony indicating Staff supported Agua Fria's request for a hook-up fee and accounting order authorizing deferral of CAP expenses, but recommended a different hook-up fee and carrying cost than proposed by Agua Fria. On November 1, 2000, Agua Fria filed a Reply To Staff Testimony. On November 15, 2000, Staff filed a Response to Company's Reply To Staff Testimony. On November 22, 2000, Agua Fria filed a Reply To Staff's Response To Company's Reply To Staff's Testimony.

Background

Citizens entered into CAP water contracts in October 1985 for its Agua Fria, Sun City Water and Sun City West affiliates. As a result, Agua Fria has an annual CAP water allocation of 11,093 acre-feet. Since 1985, Citizens has been incurring and paying holding charges to the Central Arizona Water Conservation District ("CAWCD") to retain the right to use CAP water for current and future customers. In Decision No. 58750 (August 31, 1994), the Commission authorized deferral of the

1 CAP holding charges and allowed Citizens' Sun City and Agua Fria affiliates to request recovery of
2 such amounts at a later time. In 1995, Agua Fria, along with other Citizen affiliates, filed a joint
3 application for rate increases, which included a request for approval of the recovery of deferred and
4 on-going CAP water M&I charges by means of a customer surcharge. In Decision No. 60172 (May
5 7, 1997), the Commission found Citizens' decision to obtain CAP water allocations to have been
6 prudent, but denied the request for surcharge. The Commission believed that at that time, the CAP
7 water was not "used and useful" and that Citizens did not have a definite plan to use the CAP water.

8 In October 1998, Citizens' Sun City West and Sun City Water affiliates filed a joint
9 application with the Commission seeking approval of a "groundwater savings fee," a portion of
10 which was intended to enable the two companies to recover their respective deferred CAP M&I
11 charges. Included in that filing was a definitive plan for the use of CAP water. A key element of that
12 plan was for Citizens to begin delivering CAP water to the existing Maricopa Water District
13 ("MWD") Recharge Facility, which it began doing in March 2000. In Decision No. 62293 (February
14 1, 2000) the Commission found that the Groundwater Savings Project was completed, that the CAP
15 water allocation for the Sun Cities affiliates was used and useful and thus, recovery of the deferred
16 costs was appropriate.

17 On July 15, 1999, the Arizona Department of Water Resources ("ADWR") issued Agua Fria a
18 permit to allow the storage of up to 11,093 acre-feet of CAP water at the MWD Recharge Facility.
19 Under its agreement with MWD, Agua Fria has begun delivering 2,100 acre-feet of CAP water per
20 year into the MWD Recharge Facility. The agreement provides for the delivery to increase each year
21 by an additional 1,100 acre-feet until the full use of the allocation is achieved in 2008.

22 Proposed Hook-up Fees and Accounting Treatment

23 To date, Agua Fria has paid over \$2.45 million in CAP water M&I charges that are currently
24 recorded on its balance sheet as a deferred cost. Agua Fria has requested to be able to recover these
25 deferred CAP costs through a flat hook-up fee assessed on developers and builders of residential and
26 commercial subdivisions. Agua Fria proposed three different hook-up fees: 1) a \$150 fee for age-
27 restricted dwellings, 2) a \$257 fee for conventional residential housing units, and 3) a \$150
28 Equivalent Resident Unit ("ERU") fee for commercial buildings. Agua Fria determined the fees by

1 adding deferred and on-going CAP charges and dividing by the number of hook-ups documented in
2 the Agua Fria Master Plan. The fee differential reflects the distinctive water usage patterns for the
3 three customer categories and projected future annual number of hook-ups over the next 10 years.

4 Agua Fria proposed that amortization take place monthly so that, after deducting the
5 amortization expense from the actual hook-up fee revenues, the resulting after-tax operating income
6 equals the required return on the deferral balance based on the rate of return approved in Agua Fria's
7 last rate case (i.e. 8.73 percent approved in Decision No. 60172). According to Citizens, and not
8 disputed by Staff, this approach will ensure that Citizens neither over nor under recovers its deferred
9 costs. Any differences between the projected and actual numbers of hook-ups or costs would be
10 automatically offset by a change in the amortization amount computed. Based on current projections,
11 the deferred balance will be fully amortized in approximately 10 years.

12 Staff's Recommendations

13 In its testimony filed on October 12, 2000, Staff stated that it believed that Agua Fria's use of
14 CAP water is identical to the interim plan adopted by Sun City Water and Sun City West, which the
15 Commission had found to comply with the "used and useful" criteria in Decision No. 60172. Staff
16 further believed that MWD's boundaries are in close alignment with Agua Fria's certificated area and
17 thus, Agua Fria will receive a direct and immediate benefit from reduced groundwater pumping by
18 MWD. Staff believed that recovery of Agua Fria's deferred CAP costs is now appropriate. Staff
19 agreed with Agua Fria that the concept of a hook-up fee was appropriate in this case, as the Agua Fria
20 area is only approximately 15 percent built-out, leaving ample opportunity to recover the deferred
21 costs. Further, Staff stated that the use of hook-up fees at least initially, transfers cost responsibility
22 from ratepayers to builders and developers.

23 Staff did not agree with the Division's proposal for an 8.73 percent rate of return as a carrying
24 charge on deferred CAP charges. Staff recommended a 4.365 percent interest component, or 50
25 percent of the request. Staff's recommendation is consistent with the 4.365 percent approved in
26 Decision No. 62293 in the Sun Cities matter. Staff's recommendation reduces the hook-up fee for
27 age-restricted dwellings from \$150 to \$127, for conventional residential housing units from \$257 to
28 \$218, and for commercial buildings from \$150 to \$127.

1 Staff agreed with Agua Fria's proposal to continue to defer CAP costs for water not being
2 used or delivered for recharge. Staff explained that such treatment is consistent with Decision No.
3 59079 (May 5, 1995) regarding CAP charge recovery for Paradise Valley Water Co., where the
4 Commission allowed recovery of CAP M&I charges without CAP water actually being used where
5 Paradise Valley Water Co. showed that both existing and future customers benefited from its CAP
6 allocation.

7 Staff further recommended that: 1) Agua Fria submit an annual informational report to the
8 Director of the Utilities Division showing the amounts collected through deferred CAP hook-up fees,
9 the amounts amortized, and the outstanding balance of CAP deferrals; 2) when the deferred CAP
10 charges are recovered, the corresponding hook-up fees be terminated and that any over-collection be
11 applied to any on-going CAP costs; 3) within the amortization period in the event Agua Fria fails to
12 recharge its full CAP water allocation, the deferred CAP hook-up fee should terminate and Agua Fria
13 should forfeit recovery of the deferred CAP costs; and 4) Agua Fria file with the Commission for an
14 adjustment to the approved hook-up fees to reflect any price fluctuations in the recharge costs or
15 billing determinants, as soon as any fluctuation becomes known and measurable, but not less than
16 annually.

17 The Disputed Issues

18 Agua Fria accepted Staff's recommendations that it file an annual report of hook-up fee
19 revenues and an analysis of the deferral account, and that the collection of hook-up fees should cease
20 once all the deferred CAP costs are recovered. The Division disagreed that the appropriate carrying
21 charge should be only 50 percent of its authorized return. Staff's recommended rate of return is
22 based on the carrying charge approved in the Sun City West and Sun City Water case. Staff believed
23 the 4.365 percent rate of return was appropriate because Agua Fria will not use all the CAP water
24 throughout the amortization period. Agua Fria differentiates the Sun City case with the current
25 situation on the fact that the water recharged by Sun City Water and Sun City West would not
26 physically reach the taps of their customers and consequently there was found to be no "direct benefit
27 to customers." Because Agua Fria's wells are located throughout the area where its CAP water will
28 be discharged, Agua Fria argued the recharged water will reach the taps of its customers and there is

1 an immediate, direct benefit. The Division argued that the CAP allocation was determined based on
2 population projections and demand in the year 2035, and that although Agua Fria, has a large service
3 area and is experiencing rapid growth, it currently has a small developed base of customers, and thus,
4 it's unreasonable to expect it to utilize its full CAP allocation throughout the amortization period. In
5 addition, Citizens notes, the amortization period in the Sun Cities case was for five years, while the
6 period in the current situation is 10 years.

7 Agua Fria also disagreed with Staff that the hook-up fees should cease and the remaining cost
8 deferrals forfeited if Agua Fria fails to recharge its full CAP water allocation. The Division stated
9 that the recharge plan is only an interim measure and it will implement a water management strategy
10 that will ultimately include both direct treatment and recharge of CAP water. Agua Fria argued that
11 circumstances beyond the company's control, or the use of CAP water other than recharge, should
12 not automatically require a change to the hook-up fees or warrant the forfeiture of costs already
13 deemed to have been prudently incurred. Citizens proclaimed that it will inform the Commission of
14 any definitive change in the manner or quantity of the projected actual use of CAP water in its annual
15 informational report. Staff could determine at that time what, if any, actions should be taken.

16 Finally, Agua Fria disagreed with Staff's recommendation that the Division should file for an
17 adjustment to the hook-up fees to reflect any changes in the costs of recharge or billing determinants
18 from the projections in the application. The Division explained that the accounting model it
19 developed in its application uses two variable inputs, the actual balance in the deferral account and
20 the actual revenues generated by the hook-up fees. According to Citizens, to the extent that actual
21 deferred costs are lower than the estimates or the number of hook-ups are greater than projected, the
22 amortization rate is correspondingly increased such that the achieved return will not exceed what has
23 been authorized. Once the deferred costs are recovered the hook-up fees will cease. Agua Fria
24 argued that the administrative burden on itself and Staff to file an adjustment to the approved hook-
25 up fees is unwarranted because there is no risk of over-earning. Agua Fria believed that if the actual
26 costs and billing determinants differ sufficiently from projection to warrant a hook-up fee change,
27 Staff would be aware of this situation through Citizens annual information report.

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Analysis

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2 In Decision No. 62293, the Commission approved a carrying cost of 50 percent of Citizens
3 authorized rate of return for its Sun City affiliates, because in that case the recharge of CAP water did
4 not provide a "direct benefit to the customers of the Companies." In this case, Staff has recognized
5 that "[b]ecause of the alignment of service areas, Agua Fria will receive a direct and immediate
6 benefit from reduced groundwater pumping by MWD." Consequently, we believe that the current
7 situation is distinguishable from that of the Sun City affiliates where the Commission found there was
8 no direct benefit to their customers. On a going-forward basis, Agua Fria should receive its full
9 authorized rate of return on its deferred CAP costs.

10 Staff has recommended that if the Company fails to recharge its full CAP allocation, the
11 hook-up fees should cease and the remaining unrecovered deferred costs should be forfeited. We
12 believe that there may be many reasons why Agua Fria might not recharge its full CAP allocation and
13 that it is premature at this point to determine that for whatever reason the unrecovered deferred costs
14 should be forfeited. It does not seem unreasonable, given that full amortization of the deferred
15 balance is currently projected to be approximately ten years, and that Agua Fria's recharge agreement
16 with MWD allows delivery of the full CAP allocation in 2008, to require that Agua Fria achieve full
17 use of its CAP allocation either through recharge or direct treatment, or through a combination of
18 both treatment and recharge, within ten years. We will therefore order that if by December 31, 2010,
19 full recovery of the deferred CAP charges has not yet occurred, and if the Agua Fria Division of
20 Citizens has also as of that date failed to achieve full use of its CAP allocation either through direct
21 treatment or recharge, or through a combination of both treatment and recharge, the deferred CAP
22 hook-up fee shall terminate on that date, absent a showing of good cause.

23 Finally, Citizens disagreed with Staff's recommendation that Agua Fria should file for an
24 adjustment to the hook-up fees to reflect any changes in the costs of recharge or billing determinants
25 from the estimates used in the application. It seems likely that monthly costs or revenues from hook-
26 up fees will differ somewhat from projections, and that Staff's recommendation, literally interpreted
27 could be an unnecessary administrative burden. To address Staff's concerns that a year could pass
28 prior to Citizens informing the Commission that actual costs or billing determinants differ

1 significantly from projections, we will require Citizens to notify the Commission whenever it knows
2 with reasonable certainty that on a quarterly basis, actual costs and/or billing determinants have, or
3 are expected, to deviate from the projections in the application by more than 10 percent.

4 * * * * *

5 Having considered the entire record herein and being fully advised in the premises, the
6 Commission finds, concludes, and orders that:

7 **FINDINGS OF FACT**

8 1. Agua Fria provides water service to approximately 9,300 customers in Maricopa
9 County.

10 2. On March 29, 2000, Agua Fria submitted a tariff application to the Commission
11 seeking approval of the implementation of a hook-up fee to be assessed on builders and developers
12 for recovery of deferred CAP capital costs.

13 3. On June 16, 2000, Mr. Marvin Lustiger and the Arizona Utility Investors Association
14 ("AUIA") were granted intervention.

15 4. On October 12, 2000, Staff filed testimony.

16 5. On November 1, 2000, Agua Fria filed a Reply To Staff Testimony.

17 6. On November 15, 2000, Staff filed a Response To Company's Reply To Staff
18 Testimony.

19 7. On November 22, 2000, Agua Fria filed a Reply To Staff's Response To Company's
20 Reply To Staff Testimony.

21 8. To date, Agua Fria has paid over \$2.45 million in CAP water charges that are
22 currently recorded on its balance sheet.

23 9. Agua Fria has an annual CAP allocation of 11,093 acre feet.

24 10. In Decision No. 60172 (May 7, 1997), the Commission found Citizens' decision to
25 obtain CAP water allocations to have been prudent, but denied the pending request for a surcharge
26 because at that time the CAP water was not "used and useful" and Citizens did not have a definite
27 plan to use the CAP water.

28 11. Commencing in March 2000, Agua Fria began recharging a portion of its CAP

1 allocation at the MWD Recharge Facility. Pursuant to its contract with MWD, Agua Fria will deliver
2 2,200 acre feet of CAP water for recharge in the first year, which delivery will increase by 1,100
3 acre-feet per year, until the full allocation is used in 2008.

4 12. Agua Fria has requested to be able to recover these deferred CAP costs through a flat
5 hook-up fee assessed on developers and builders of residential and commercial subdivisions. Agua
6 Fria has proposed three different hook-up fees: 1) a \$150 fee for age-restricted dwellings, 2) a \$257
7 fee for conventional residential housing units, and 3) a \$150 Equivalent Resident Unit ("ERU") fee
8 for commercial buildings. Agua Fria requested a carrying charge of 8.74 percent be applied to
9 deferred CAP charges.

10 13. Staff recommended that:

11 (a) The Commission approve hook-up fees of \$127 for age-restricted dwellings, \$218
12 for conventional residential housing units, and \$127 per ERU for commercial buildings;

13 (b) The Commission allow the continued deferral of CAP charges until the full
14 allocation of water is either directly used and/or delivered to the recharge facility;

15 (c) The deferred CAP costs shall include a going forward carrying cost of 4.365
16 percent, or 50 percent of Citizens authorized rate of return of 8.73 percent;

17 (d) Agua Fria submit an annual informational report to the Director of the Utilities
18 Division showing the amounts collected through deferred CAP hook-up fees, the amounts amortized
19 and the outstanding balance of CAP deferrals;

20 (e) When the deferred CPA charges are recovered, the corresponding hook-up fees be
21 terminated and that any over-collection be applied to any on-going CAP costs;

22 (f) within the Amortization period in the event Agua Fria fails to recharge its full
23 CAP water allocation, the deferred CAP hook-up fee should terminate and the Division should forfeit
24 recovery of the deferred CAP costs; and

25 (g) Agua Fria file with the Commission for an adjustment to the approved hook-up
26 fees to reflect any price fluctuations in the recharge costs or billing determinants, as soon as any
27 fluctuation becomes known and measurable, but not less than annually.

28 14. MWD's boundaries are in close alignment with Agua Fria's certificated area and thus,

1 Agua Fria will receive a direct and immediate benefit from reduced groundwater pumping by MWD.
2 15. Because Agua Fria's agreement with MWD allows recharge of the Division's full
3 CAP allocation in 2008, and because Agua Fria intends to implement a water management strategy
4 that will ultimately include both direct treatment and recharge of CAP water, Agua Fria should
5 reasonably be able to achieve full use of its CAP allocation within approximately ten years.

6 **CONCLUSIONS OF LAW**

7 1. Citizens and Agua Fria are public service corporations pursuant to Article XV of the
8 Arizona Constitution and A.R.S. §§ 40-250 and 40-251.

9 2. The Commission has jurisdiction over Citizens and Agua Fria and of the subject
10 matter of the application.

11 3. Notice of the application was given in accordance with the law.

12 4. Citizens' decision to obtain CAP water allocations was a prudent planning decision.

13 5. Agua Fria will receive a direct and immediate benefit from the recharge of its CAP
14 water allocation.

15 6. It is in the public interest to limit the recovery period for the deferred CAP charges
16 that are the subject of this proceeding to a reasonable period of time.

17 7. Adoption of the proposed hook-up fees and Agua Fria's proposed accounting
18 treatment of deferred CAP costs as conditioned herein is in the public interest.

19 **ORDER**

20 IT IS THEREFORE ORDERED that the Agua Fria Water Division of Citizens
21 Communications Company shall file within 15 days from the effective date of this Decision, a tariff
22 setting forth the hook-up fees as approved herein.

23 IT IS FURHTER ORDERED that the amortization amount shall be computed monthly as
24 proposed by Citizens Communications Company and that the deferred CAP costs shall include a
25 going-forward carrying cost of 8.73 percent.

26 IT IS FURTHER ORDERED that the Agua Fria Water Division of Citizens Communications
27 Company shall notify the affected parties to existing Line Extension Agreements of the charges
28 authorized herein and the effective date of the same.

1 IT IS FURTHER ORDERED that the Agua Fria Water Division of Citizens Communications
2 Company shall file with the compliance section of the Utilities Division within 60 days from the
3 effective date of this Decision a copy of the notice it sends to the affected parties to existing Line
4 Extension Agreements.

5 IT IS FURTHER ORDERED that commencing January 31, 2002, the Agua Fria Water
6 Division of Citizens Communications Company shall submit an annual informational report to the
7 Director of the Utilities Division showing the amounts collected through deferred CAP hook-up fees,
8 the amounts amortized and the outstanding balance of CAP deferrals.

9 IT IS FURTHER ORDERED that when the deferred CAP charges are recovered, the
10 corresponding hook-up fees shall be terminated and that any over-collection be applied to any on-
11 going CAP costs.

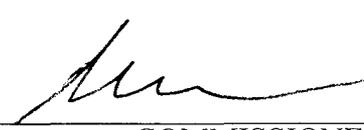
12 IT IS FURTHER ORDERED that the Agua Fria Water Division of Citizens Communications
13 Company notify the Director of the Utilities Division in writing whenever it knows with reasonable
14 certainty that on a quarterly basis, actual costs and/or billing determinants have, or are expected, to
15 deviate from the projections in the application by more than 10 percent.

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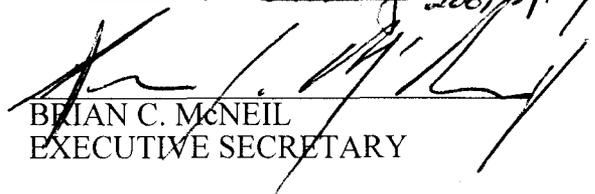
1 IT IS FURTHER ORDERED that if by December 31, 2010, full recovery of the deferred CAP
2 charges has not yet occurred, and the Agua Fria Division of Citizens Communications Company has
3 also by that date failed to achieve full use of its CAP allocation either through direct treatment or
4 recharge, or through a combination of both treatment and recharge, the deferred CAP hook-up fee
5 shall terminate on that date, absent a showing of good cause.

6 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

7 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

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11 CHAIRMAN COMMISSIONER COMMISSIONER
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13 IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive
14 Secretary of the Arizona Corporation Commission, have
15 hereunto set my hand and caused the official seal of the
16 Commission to be affixed at the Capitol, in the City of Phoenix,
17 this 2nd day of February, ~~2000~~ 2001.

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19 BRIAN C. McNEIL
20 EXECUTIVE SECRETARY

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29 DISSENT _____

1 SERVICE LIST FOR: THE AGUA FRIA DIVISION OF CITIZENS COMMUNICATIONS
2 COMPANY

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