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BEFORE THE ARIZONA CORPORATION COMMISSION

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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. E-01032B-00-0205

**COMPANY REPLY TO
STAFF'S RESPONSE TO COMPANY'S
REPLY TO STAFF TESTIMONY**

The Agua Fria Division ("Agua Fria") of Citizens Communications Company ("Citizens" or "Company") submits this Reply to the Staff's Response. Agua Fria requests that the Hearing Division issue a proposed order in this matter for Commission consideration on an expedited basis without a hearing. Citizens has discussed this procedure with Staff and it agrees the matter should be handled on this basis.

I. BACKGROUND

On March 29, 2000, Citizens submitted a tariff application to the Commission seeking approval for implementation of a hook-up fee to be assessed not to consumers but instead to builders and developers for recovery of deferred Central Arizona Project ("CAP") capital costs incurred by its Agua Fria Division. No further activity in this Docket occurred until the testimony of ACC Commission Staff Senior Rate Analyst Mr. Ronald E. Ludders was filed on October 12, 2000. On November 1, 2000 the Company filed a reply to Mr. Ludders testimony in which it accepted certain of Mr. Ludders' recommendations (Nos. 1, 3, 5 and 6), and set forth detailed explanations with respect to the remaining

1 recommendations (Nos. 2, 4, 7 and 8) which are not appropriate or are unwarranted in these
2 circumstances.

3 On November 15, 2000 the Staff responded and continued to press the four contested
4 recommendations. In this filing, the Company is presenting additional comments with respect to the
5 issues still in dispute.
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7 **II. REPLY TO STAFF RECOMMENDATIONS**

8 **A. Rate of Return on deferred CAP balances.**

9 The Staff continues to assert that a rate of return equal to only one-half of the current 8.73%
10 authorized in Commission Decision No. 60172 should be allowed on the balance of deferred CAP
11 payments. The principal basis for this recommendation is Commission Decision No. 62292 in which
12 customer surcharges in the form of a "groundwater saving fee" were allowed for the recovery of CAP
13 costs. However, Decision No. 60172 not only assigned full cost responsibility for both current and
14 deferred CAP costs to ratepayers, but also reflected a five-year amortization period for the deferred
15 balances in the resulting customer surcharge rates. By contrast, in this proceeding, the Company is
16 proposing that all deferred CAP costs be recovered only from builders and developers, not consumers
17 and over an amortization period twice as long--approximately ten years. Moreover, the portion of CAP
18 M&I costs and all delivery costs relating to CAP water taken and recharged are being accounted for as
19 an operating expense absorbed by current revenues. Ratepayers will not be asked to pay for any of
20 these costs until the conclusion of the next Agua Fria rate case, and then only on a prospective, as-
21 incurred basis.
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25 The test year used for establishing the revenue requirement underlying current service rates in
26 Decision No. 60172 was the twelve months ending March 31, 1995. Due to actions by the Federal
27 Reserve, and other factors, the costs of all forms of capital have clearly been rising since the issuance
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1 of Decision No. 60172. Citizens is not requesting a rate of return reflecting current market conditions;
2 only the rate of return it has been authorized.

3 The recognition by the Commission that there is a time value associated with the deferral of
4 CAP costs, from the point at which the affected utility remits funds until they are ultimately recovered,
5 was clearly established in Decision No. 58120 issued in 1992. In Decision No. 60172, Citizens'
6 procurement of CAP water was found to be prudent, and in Decision No. 62292, the recharge of CAP
7 water was found to meet the "used and useful" test. There is no reason for allowing anything less than
8 the full, authorized rate of return on an investment that has been determined not only to be prudent but
9 also to be providing a current benefit.
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11 In its response, the Staff offers a new argument that the full rate of return would be
12 inappropriate due to the fact that not all the CAP water will be used throughout the amortization
13 period. However, unlike the Sun Cities' area, Agua Fria is a large, rapidly growing certificated area
14 with currently a relatively small developed base of customers. CAP allotments were granted based
15 upon 2034 population and demand estimates. It is simply unreasonable to expect Agua Fria to use its
16 full CAP allotment at this time. For example, Agua Fria's 1999 total water use was 4,040.96 acre-feet,
17 only 36% of its CAP allocation. Agua Fria has adopted a reasonable CAP water use plan which
18 provides that by using 2,100 acre-feet of CAP water in 2001, 34% of its 2001 water use will be met
19 with CAP water. The percentage use of CAP water is projected to increase steadily as Agua Fria
20 phases-in its CAP water use by an additional 1,100 acre-feet per year, reaching a maximum of 75%
21 CAP water use in 2009. In comparison, the full CAP allotments of the Sun Cities amount to 29% of
22 the total water use by Sun City Water Company and Sun City West Utilities Company.
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1 **B. Cessation of Hook-up Fees and Forfeiture of Cost Deferrals (Staff Recommendation**
2 **No. 7).**

3 Staff believes that, should the Company fail to recharge its full CAP allocation, the hook-up
4 fees should cease and the remaining unrecovered deferred costs be forfeited. That recommendation
5 fails to recognize that (1) the Commission has already found these expenditures to be prudent, and (2)
6 there are other acceptable uses for the CAP water, such as direct delivery to customers, that would
7 continue to meet the "used and useful" requirement for cost recovery. There is no logical justification
8 for disallowing the recovery of a cost which has been deemed to have been prudently incurred and is
9 providing direct benefit.

10 **C. Adjustments to Hook-up Fees to Reflect Changes in Recharge Costs of Billing**
11 **Determinants.**

12 Staff would require the Company to file for a change in the hook-up fees every time there is
13 difference between the forecasted and actual CAP payments or the number of customer hook-ups.
14 There is no similar reporting requirement imposed by the Commission in Decision No. 62293 relating
15 to the customer surcharges allowed for recovery of CAP costs incurred by Sun City Water and Sun City
16 West Utilities.

17 This recommendation by Staff literally could require monthly filings with the Commission.
18 Undoubtedly, the actual hook-ups every month will differ from what is projected. The only logical
19 reason for such a recommendation is a concern that the Company could earn a return greater than its
20 authorized rate. The hook-up fees proposed by the Company essentially reflect a levelized revenue
21 requirement based on projected CAP costs, the current authorized rate of return and the number of
22 hook-ups projected for the period during which CAP water use is to be phased-in. The resulting fees
23 have been discussed with, and have been found to be acceptable by, representatives of the various
24 developers and home builders, the actual payers of such proposed fees. As previously explained, the
25 Company's application contains an accounting model that was developed to assure there was no
26 potential for over-earning. The rate at which the deferred balances of CAP costs are amortized is solely
27 dependent on two variable inputs--customer hook-ups and CAP payments. To the extent hook-ups are
28 greater than expected or CAP payments less than anticipated, the model will correspondingly increase
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1 the rate of amortization, thereby assuring no opportunity for over-earning.

2 The annual report to the Director of Utilities (Staff Recommendation No. 5), to which the
3 Company has already committed, will fully disclose all relevant financial data relating to CAP
4 payments, hook-up fee revenues, and amortization expense. These reports will be more than sufficient
5 for Staff oversight. Any more frequent reporting requirements or changes in the hook-up fees are
6 totally unnecessary.

7 **III. SUMMARY**

8 Citizens filed this tariff application nearly eight months ago. During the intervening eight
9 months, Agua Fria has purchased, recharged and used 1,000 acre-feet of CAP water, and Agua Fria has
10 ordered 2,100 acre-feet of CAP water for delivery in 2001. The Commission Staff has proposed eight
11 recommendations--four of which are acceptable and four of which are either unnecessary or
12 inappropriate in this matter. The Company is requesting a hook up fee that will produce a fair return of
13 and on an investment the Commission has already determined to be prudent and that is providing
14 significant direct benefits to customers.

15 Citizens respectfully requests that the application be promptly considered by the Hearing
16 Division and a proposed order be issued for the Commission's consideration on an expedited basis
17 without a hearing.

18 RESPECTFULLY SUBMITTED on November 22, 2000.

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20 

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25 Original and ten copies filed this
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