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BEFORE THE ARIZONA CORPORATION COMMISSION

1
2 **MARC SPITZER**
Chairman
3 **WILLIAM A. MUNDELL**
Commissioner
4 **JEFF HATCH-MILLER**
Commissioner
5 **MIKE GLEASON**
Commissioner
6 **KRISTIN K. MAYES**
Commissioner

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AZ CORP COMMISSION
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Arizona Corporation Commission

DOCKETED

JAN 30 2004

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9 **IN THE MATTER OF THE APPLICATION OF**
10 **PINE WATER COMPANY 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 AND FOR**
16 **APPROVAL TO INCUR LONG-TERM DEBT**

Docket No. W-03512A-03-0279

**STAFF'S RESPONSE TO PINE
WATER COMPANY'S MOTION TO
STRIKE SURREBUTTAL
TESTIMONY OF JOEL M. REIKER**

17 The Arizona Corporation Commission ("Commission") Utilities Division ("Staff") hereby
18 responds to Pine Water Company's ("Pine's") motion to strike. Mr. Reiker's cost of capital
19 surrebuttal testimony should not be stricken. The testimony responds to the rebuttal testimony of
20 Pine's witness, Mr. Bourassa. Pine should have reasonably expected Staff would file surrebuttal cost
21 of capital testimony. It will not be unduly burdensome for Pine to prepare rejoinder to Mr. Reiker's
22 cost of capital testimony. Pine should be capable of preparing its response to the testimony in the
23 time allowed under the current procedural schedule. Mr. Reiker's cost of capital testimony should
24 not be stricken and Pine should not be afforded additional time to respond to that testimony.

25 **I. Mr. Reiker's Cost of Capital Testimony is Filed in Response to Mr. Bourassa's Rebuttal**
26 **Cost of Capital Testimony.**

27 The content of the parties' direct and Pine's rebuttal testimony show that Mr. Reiker's cost of
28 capital surrebuttal testimony directly responds to Mr. Bourassa's rebuttal testimony. Staff witness,
Mr. Thornton, provided direct testimony indicating Staff was not filing rate of return analysis because
the Company's application showed negative equity of \$153,000. (Thornton Dt. at 4). Mr. Thornton

1 testified that “rate of return, or more specifically a return on equity, is not a helpful method to set
2 revenue requirement when a Company has negative equity.” (Id.) Staff witness, Mr. Fernandez,
3 provided direct testimony that a positive \$449,598 adjustment to Pine’s plant in service was
4 necessary to account for Project Magnolia’s original cost. (Fernandez Dt. At 6-7). Company
5 witness, Mr. Bourassa rebutted that if Staff’s adjustment to Pine’s plant in service is correct, a
6 corresponding adjustment to Pine’s “capital structure, either additional debt, equity, or both” must be
7 made. (Bourassa Rb. at 11-12). In surrebuttal, Mr. Reiker agrees the corresponding adjustment is
8 necessary. (Reiker Srb. at 3-4). Mr. Reiker recommends a corresponding adjustment to Pine’s
9 capital structure of \$299,619 to equity and \$149,979 to long-term debt. (Id.). The result is to place
10 Pine in a positive equity position.

11 Although this adjustment makes the cost of capital analysis somewhat more appropriate, Staff
12 still advocates using the operating margin method. (Reiker Srb. at 2). However, having made the
13 adjustments pointed out as necessary by Mr. Bourassa in his rebuttal, Staff is compelled to submit its
14 cost of capital analysis and recommendation to the Commission for consideration. Not doing so
15 would deny the Administrative Law Judge and the Commissioners an alternative to Pine’s flawed
16 cost of capital analysis should they determine such an analysis is appropriate.

17
18 **II. Staff’s Provision of the Cost of Capital Analysis does not Constitute Unfair Surprise to Pine.**

19 Pine should have reasonably expected that Staff would consider Mr. Bourassa’s rebuttal
20 testimony, and file cost of capital testimony in response to it. In fact, Mr. Bourassa testifies that Staff
21 should file cost of capital testimony. (Bourassa Rb. at 28-29). Staff was faced with two choices in
22 response to Mr. Bourassa’s testimony. It could either continue to argue cost of capital analysis and
23 testimony was unnecessary, or it could address cost of capital in its surrebuttal testimony. In short,
24 Mr. Reiker’s surrebuttal is a direct response to Mr. Bourassa, and is therefore entirely appropriate.

25 Unless Mr. Bourassa and Pine anticipated Staff would flatly reject Mr. Bourassa’s testimony
26 regarding the corresponding adjustments, it should have known the result would be Staff’s filing of a
27 cost of capital analysis in its surrebuttal. Because of the nature of the adjustments, it was
28 unreasonable for Pine to expect Staff to dismiss them. Pine cannot claim to have been unfairly

1 surprised when it should have reasonably expected Staff would file cost of capital testimony in its
2 surrebuttal. (*See Garcia v. Industrial Comm'n*, 20 Ariz.App. 243, 246, 511 P.2d 687, 690 (1973)
3 (holding unsubpoenaed appearance of hospital's chief surgeon was not unfair surprise where
4 worker's compensation plaintiff should reasonably expect that surgeon would appear). Like the
5 claimant in *Garcia*, Pine not unfairly surprised by Staff's response.

6
7 **III. It is Not Unduly Burdensome for Pine to Respond to Staff's Cost of Capital Testimony
in its Rejoinder Testimony and at Hearing.**

8 Staff's cost of capital methods mirror the methods used and testimony filed in past rate cases
9 in which Pine's expert, Mr. Bourassa participated. As it normally does, Staff has used the widely
10 accepted and common Capital Asset Pricing and Discounted Cash Flow models to determine its
11 recommended cost of capital. (Reiker Srb. at 19). Mr. Bourassa testifies that he is familiar with both
12 the CAPM and DCF models. (Bourassa Dt. at 15, 16, 30-33). Mr. Bourassa's familiarity with the
13 models and Staff's use of them makes his preparation of a response less burdensome. Pine is correct
14 in asserting that Mr. Reiker provided thirty-seven (37) pages of cost of capital testimony. (Pine
15 motion at 3). However, it is important to note that nineteen (19) pages of that testimony are devoted
16 to response to specific points in Mr. Bourassa's testimony. (See Reiker Srb. pp. 1-19). It certainly
17 should not be considered unduly burdensome for Mr. Bourassa to defend his own analysis.

18 Further, having already prepared his own cost of capital analysis Mr. Bourassa has necessarily
19 considered many (if not all) of the points raised by Mr. Reiker's analysis. (Bourassa Dt. at 13-30).
20 Mr. Bourassa is not now required to perform a full cost of capital analysis to respond to Mr. Reiker's
21 testimony. Mr. Bourassa performed that full analysis in preparation of his own cost of capital
22 testimony. Because Mr. Bourassa has already performed a thorough cost of capital analysis, his
23 response to Mr. Reiker's analysis is made less burdensome. It is not unduly burdensome for Pine to
24 prepare its response to Mr. Reiker's cost of capital testimony.

25 **IV. Pine's Reliance on Staff's Argument in a Prior Docket is Misplaced.**

26 Distinctions between Staff's 1992 argument and the argument presented by Pine in the present
27 case are apparent from the quotation provided by Pine in its Motion. The quotation tells us that the
28 Company involved in Docket No. U-2621-91-203, *et a* (the "1992" case), had two prior opportunities

1 to provide cost of capital testimony. (Pine Motion at 4). Here, Staff's Surrebuttal testimony is its
2 first opportunity to respond to Mr. Bourassa's rebuttal arguments concerning proper corresponding
3 adjustments to Staff's rate base treatment of Project Magnolia and his arguments concerning why
4 presentation of cost of capital was proper in the case.

5 Further, the quotation provided by Pine indicates that the Company involved in the 1992 case
6 was attempting to introduce cost of capital testimony "only six days before hearing." (Pine Motion at
7 4). Here, Pine has a full month before hearing and another round of testimony to file prior to the
8 hearing. Further, Staff's 1992 motion was never ruled on by the Administrative Law Judge, as the
9 case settled before a ruling was necessary. The factually different, decade-old statement has no value
10 here.

11 **V. Conclusion**

12 Staff's cost of capital testimony is appropriate because it responds to the rebuttal testimony of
13 Mr. Bourassa. It will not unduly burden Pine to respond to Staff's surrebuttal cost of capital
14 testimony in its rejoinder testimony. The testimony does not constitute unfair surprise to Pine, and
15 can be responded to in the amount of time allowed under the current procedural schedule. Pine's
16 reliance on Staff's 1992 argument is clearly distinguishable and is unpersuasive. Staff respectfully
17 requests Pine's Motion to Strike is denied.

18 RESPECTFULLY SUBMITTED this 30th day of January, 2004.

19 ARIZONA CORPORATION COMMISSION

20
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