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Arizona Corporation Commission
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JUN 1 0 2005

6 Attorneys for Coronado Utilities, Inc.

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BEFORE THE ARIZONA CORPORATION COMMISSION

9 IN THE MATTER OF THE APPLICATION
10 OF CORONADO UTILITIES, INC. FOR A
11 CERTIFICATE OF CONVENIENCE AND
12 NECESSITY TO PROVIDE WASTEWATER
13 SERVICE IN PINAL COUNTY, ARIZONA.

DOCKET NO. SW-04305A-05-0086

14 IN THE MATTER OF THE APPLICATION
15 OF CORONADO UTILITIES, INC., AN
16 ARIZONA CORPORATION, FOR
17 AUTHORITY TO ISSUE SHORT AND
18 LONG-TERM DEBT INSTRUMENTS IN
19 CONNECTION WITH FINANCING THE
20 ACQUISITION OF THE WASTEWATER
21 UTILITY PLANT OF BHP COPPER, INC.
22 AND CONSTRUCTING IMPROVEMENTS
23 THERETO.

DOCKET NO. SW-04305A-05-0087

**CORONADO UTILITIES' RESPONSE TO
STAFF REPORT**

(Consolidated)

24 Coronado Utilities, Inc. ("Coronado") hereby submits its response to the Staff Report
25 issued May 27, 2005 in this docket. Both Coronado and Staff reach the same conclusion – that it
26 is in the public interest for Coronado to own and operate a wastewater utility serving the
community of San Manuel, Arizona. Given that Coronado is a fit and property entity to fill a
clear and present need for service in the area, an area where BHP Copper, Inc. ("BHP") intends to
cease providing service, the Certificate of Convenience and Necessity ("CC&N") requested
herein should be granted.

Staff and Coronado disagree on one fundamental question – the extent to which Coronado
should take full advantage of low cost financing available through cooperation with the Pinal

1 County Industrial Development Authority. To begin with, there is no basis for Staff to conclude
2 that Coronado can meet the requirements of a capital structure with substantially more equity than
3 proposed. Moreover, Coronado believes the benefit of lower rates that will result from this type
4 of government-arranged financing outweighs the benefits Staff claims arise from a capital
5 structure with more equity. This is particularly true given the unavoidable rate increase
6 customers will experience under any scenario, having previously receiving subsidized wastewater
7 utility service from BHP over the last 50 years. In addition, Coronado disagrees with Staff's
8 failure to include revenue from effluent sales in total revenue and Staff's claim that Coronado is
9 seeking approval of debt to pay operating expenses. Except as noted herein, Coronado accepts
10 Staff's recommendations and associated conditions.

11 **I. BACKGROUND**

12 BHP has owned and operated a wastewater collection and treatment system in San
13 Manuel, Arizona for approximately 50 years. BHP used this system to provide wastewater
14 service to its mining operations, as well as residents living nearby in San Manuel. Because BHP
15 employed many of San Manuel's area residents, it subsidized nearly all the costs associated with
16 operating the existing wastewater system. However, in 1999 BHP announced that it was phasing
17 out its mining operations, leaving open the question of who would provide wastewater utility
18 service in the future.

19 On November 10, 2004, BHP entered into a Purchase Agreement ("Agreement") with
20 Coronado for the sale of approximately 84 acres of real property in and around San Manuel,
21 conditioned upon Coronado's commitment to construct desperately needed upgrades to the
22 existing wastewater collection and treatment system. The Agreement also requires Coronado to
23 obtain a CC&N to provide wastewater treatment service pursuant to rules and regulations
24 applicable to public service corporations, in addition to Commission authority to finance system
25 upgrades. Coronado intends to eventually take ownership of the existing wastewater treatment
26

1 plant, and make certain short-term improvements to the facility while it constructs a new, state-
2 of-the-art wastewater treatment facility.

3 In order to minimize the rate increase that must necessarily accompany the required
4 system upgrades, Coronado has secured the assistance of the Pinal County Industrial
5 Development Authority to obtain access to tax-exempt municipal bond loans. Issued by the
6 Municipal Leasing Credit Corporation ("MLCC"), these loans will earn between six (6%) and
7 seven (7%) percent interest, representing a lower cost of debt when compared to rates of return on
8 private capital. While Coronado's proposed initial capital structure will consist of more debt than
9 is traditionally afforded to public service corporations, the unique circumstances surrounding
10 Coronado's acquisition of BHP's wastewater system – coupled with the effort to minimize the
11 necessary rate increase – warrants special consideration by the Commission in order to regulate
12 the provision of safe and reliable wastewater service in San Manuel.

13 **II. BRIEF OVERVIEW OF RELIEF REQUESTED**

14 Coronado is requesting authority from the Commission to: 1) provide wastewater service
15 to residents living in the community of San Manuel, Arizona, under a CC&N issued by the
16 Commission where there presently exists a public need for safe and reliable service; 2) make
17 improvements to a half-century old wastewater collection system that currently cannot meet
18 Arizona Department of Environmental Quality regulations; 3) construct a new wastewater
19 treatment facility that will replace the old system and incorporate best available design control
20 technology; and 4) obtain low-cost financing through tax-exempt municipal bond loans. By
21 approving Coronado's consolidated applications, the Commission will not only authorize
22 collective efforts to immediately improve the health and safety of Arizona residents¹, but also
23 foster safe and orderly growth in Pinal County through continued wastewater utility regulation.

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26 ¹ Residents are currently served by a wastewater system that is at the end or has already exceeded its useful life.

1 **III. OBJECTIONS TO STAFF REPORT**

2 **A. Staff's Recommended Capital Structure is Less Favorable to Ratepayers**

3 Adoption of Staff's recommended capital structure would jeopardize Coronado's ability to
4 take over as the wastewater utility service provider in San Manuel and, if it did, saddle ratepayers
5 with even higher rates. In the past, residents of San Manuel have enjoyed subsidized service from
6 BHP. That subsidy is coming to an end and, under any scenario, customers in San Manuel are
7 going to experience a substantial increase in the rates they pay for wastewater utility service.
8 Before filing its application for a CC&N, Coronado explored low cost financing of the necessary
9 plant upgrades in order to minimize, to the greatest extent possible, rate increases to customers
10 will incur after the CC&N is granted. Coronado was successful and has secured a commitment
11 by MLCC to provide plant financing of up to \$3.3 million under arrangement with the Pinal
12 County Industrial Development Authority. Such financing will be provided at a rate between 6%
13 and 7%, a preferred rate Coronado was able to secure due to the cooperation of the County
14 bonding authority.

15 Staff rejects the level of proposed debt financing and recommends a capital structure with
16 nearly 30% more equity. To begin with, there is no evidence that Coronado can invest an
17 additional \$600,000 in an effort to replace BHP as the wastewater utility service provider in San
18 Manuel. If Staff's recommended capital structure is adopted and Coronado cannot make the
19 additional investment, then BHP and, more importantly, the ratepayers will be back to square one.
20 Additionally, even if Coronado could finance an additional 30% of the costs of building plant to
21 serve BHP's current customer base, customers will bear the burden of even higher rates. For
22 example, the net cost to the end-use customer of paying 6.5%-6.9% interest on a municipal bond
23 as compared to an approximately 10% return on equity is approximately \$4 per month, which
24 represents a significant savings (almost 10%) for these residential customers.

25 Staff has failed to justify the higher rates that result under its proposed capital structure.
26 For one thing, as shown in the Company's applications, Coronado will be able to cover the

1 anticipated debt service. It follows that Coronado disagrees with Staff's claim that revenue will
2 be inadequate to cover the debt. Moreover, given the unusual circumstances, it is not realistic to
3 expect Coronado to shoulder the level of risk that is typically expected of a new CC&N applicant.
4 Taking over plant that is more than five decades old and likely past its useful life, as well as a
5 customer base that is approximately half fixed-income retirees who have benefited from
6 subsidized utility service from BHP for that long is, at best, a risky proposition. Coronado should
7 not be forced to bear the burden of the additional risk and customers should not be required to pay
8 even higher rates.

9 **B. Other Issues in Dispute**

10 In the Staff Report, Staff indicates that effluent sales will occur at some unknown time in
11 the future when a golf course is built. Staff Report at 6, n. 1. The golf course exists today and
12 Coronado has included revenue from effluent sales in its pro forma financial information.

13 Staff also asserts that the Commission should reject Coronado's request to use loan
14 proceeds to pay for operating expenses. *Id.* at 13. However, Coronado has not requested
15 authorization to use loan proceeds to pay for operating expenses. Rather, as reflected in the Staff
16 Report, the proposed financing is to be used for utility plant. *Id.* at 4.

17 **IV. CONCLUSION**

18 Coronado believes that the community of San Manuel can have a bright future. The
19 community is located in close proximity to Tucson, and there is potential for large master-planned
20 developments to break-ground over the next five to ten years as significant parcels of land are
21 sold off by BHP. Once these new developments take hold, the costs of additional infrastructure
22 will be paid by new customers or even developers, and the overall rates could decrease as
23 operational costs per unit diminish with the increased number of customers paying monthly fees.
24 That is, however, the possible future. Today's reality is that BHP is leaving and someone must
25 step in to fill the void. Coronado is willing to do so – but first, those Staff recommendations that
26 burden Coronado with undue risk and ratepayers with higher rates must be rejected.

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DATED this 10th day of June, 2005.

FENNEMORE CRAIG, P.C.

By: 

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COPY sent via e-mail and U.S. Mail
this 15th day of June, 2005:

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