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BEFORE THE ARIZONA CORPORATION COMMISSION ^{Arizona Corporation Commission}
DOCKETED

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2 WILLIAM A. MUNDELL
CHAIRMAN
3 JIM IRVIN
COMMISSIONER
4 MARC SPITZER
COMMISSIONER
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DOCKETED BY

6 IN THE MATTER OF THE APPLICATION OF
FORTY NINER WATER COMPANY FOR AN
7 EMERGENCY RATE INCREASE.

DOCKET NO. W-01777A-02-0547

DECISION NO. 65352

OPINION AND ORDER

8
9 DATE OF HEARING: September 6, 2002
10 PLACE OF HEARING: Tucson, Arizona
11 ADMINISTRATIVE LAW JUDGE: Jane L. Rodda
12 APPEARANCES: Mr. Michael McNulty, BROWN & BAIN, P.C.,
13 on behalf of Forty Niner Water Company;
14 Mr. John Malamus, on behalf of Forty-Niner
Country Club Estates Homeowners Association;
15 and
16 Mr. David Ronald, Staff Attorney, Legal
Division, on behalf of the Utilities Division of
17 the Arizona Corporation Commission.

18 **BY THE COMMISSION:**

19 Forty Niner Water Company ("Forty Niner" or "Company") provides water utility service to
20 approximately 345 customers east of Tucson in Pima County. In addition to residential customers,
21 the Company provides water to a clubhouse and golf course. The water utility and the golf course
22 have the same parent company.

23 On July 19, 2002, Forty Niner filed an application with the Arizona Corporation Commission
24 ("Commission") for an emergency increase in rates.

25 By Procedural Order dated August 21, 2002, the matter was set for a hearing on September 6,
26 2002, at the Commission's offices in Tucson, Arizona.

27 Mr. John Malamus, representing the Forty-Niner Country Club Estates Homeowners
28 Association, was granted intervention.

1 A hearing convened on September 6, 2002, with Mr. Buck Lewis, President of Southwest
2 Utility Management, Inc., the management company for Forty Niner, testifying on behalf of the
3 Company; Mr. Malamus testifying for the Homeowners; and Mr. Darren Carlson, testifying on behalf
4 of Commission Staff.

5 Forty Niner filed its request for emergency rate relief because the persistent drought
6 conditions in the area and the lack of significant conservation by consumers caused the Company to
7 augment the production capacity of its wells with purchases of water from the City of Tucson. The
8 Company has had to purchase water from the City of Tucson at an average cost of \$3.59 per 1,000
9 gallons. The Company's current rates allow for a commodity charge of \$.56 per 1,000 gallons and
10 \$.61 per 1,000 gallons for usage over 14,000 gallons.

11 Through July 19, 2002, when the Company filed its application, it had incurred bills of
12 approximately \$57,000 from the City of Tucson. The amount had increased to approximately
13 \$78,170 as of the date of the hearing. Subsequent to the hearing, Forty Niner submitted a water bill
14 from the City of Tucson, which indicated additional charges for the 33 days ended September 16,
15 2002, of \$20,293. Consequently, to date, the Company has incurred a total cost of purchasing water
16 from the City of Tucson of approximately \$98,463.

17 In the summer of 2000, the Company had incurred a similar water shortage, which caused it
18 to construct an interconnection with the City of Tucson. The Company applied for emergency rate
19 relief to recover expenses of \$65,200 associated with hooking up to the City of Tucson and
20 purchasing water. The Commission did not issue a Decision on that emergency rate application, but
21 subsequently, as part of a permanent rate case, in Decision No. 63870 (July 25, 2001), allowed the
22 Company to collect the full \$65,200 from its customers by means of a \$.41 surcharge on all of its
23 customers.¹

24 The Company did not have to use the interconnection with the City of Tucson during the
25 summer of 2001.

26 In Decision No. 63870, in addition to approving the surcharge, the Commission authorized a
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28 ¹ The Company has fully recovered this cost.

1 permanent rate increase that would have increased the Company's revenue by \$43,656, from
2 \$192,802 to \$236,458. The increase would have increased operating income from \$23,126 to
3 \$49,661, for an 11.88 percent rate of return on fair value rate base.² The Commission conditioned the
4 rate increase on Forty Niner filing proof that it meets the quality standards of the Safe Drinking
5 Water Act, as tests had indicated that the Company exceeded household lead and copper action
6 levels.

7 Although the Company has been able to rectify the lead problem, it has not corrected the
8 copper levels. The Company had been trying to lower the copper levels by increasing the pH level of
9 its water through aeration which releases carbon dioxide into the water. Because its storage levels
10 have not been sufficient to permit effective aeration, and because the Company has not resorted to
11 chemical additives, the copper level continues to exceed the permissible maximums, and the
12 Company has not been able to implement the rates authorized in Decision No. 63870.³

13 At the hearing, the Company claimed that alternative methods of correcting the copper
14 problem, which included chemical additives and building additional storage would be very
15 expensive. The Company did not provide reliable estimates of the cost of rectifying the copper
16 problem. City of Tucson water does not appear to cause the same problem with copper. There is a
17 sale of the Company to the City of Tucson currently pending before the Commission (Docket No. W-
18 01777A-02-0175). It is not clear whether the cost of solving the copper problem has prevented its
19 resolution or whether the Company was anticipating the sale of the Company to the City of Tucson as
20 a solution. The sale of the Company has been delayed do to legal issues associated with irrigating the
21 golf course. A hearing on the application to sell the Company's assets has been postponed until
22 February 4, 2003. At this point, it is uncertain whether the Company will be able to consummate the
23 sale to the City.

24 The Company proposes to collect the extraordinary expenses associated with the purchase of
25 water from the City by means of \$.41 per 1,000 gallons surcharge on all residential customers until
26 the full amount is recovered. The Company did not propose collecting the surcharge from the golf

27 ² In the test year ended February 28, 2000, the Company experienced operating income of \$23,126, a 5.53 percent rate of
return.

28 ³ No party to the emergency proceeding was aware of any quality problems with the City of Tucson water.

1 course because the City prohibits using its water for golf course irrigation. In addition, the Company
2 indicates the golf course has reduced its water usage during the drought while the residential
3 customers have not.

4 It appears that the Company decided to request a \$.41 per 1,000 gallons surcharge based on
5 the previously approved surcharge. In Decision No. 63870, the Commission approved the \$.41
6 surcharge on the assumption that the Company would collect the \$65,200 of extraordinary charges in
7 a seven month period. The current costs associated with the purchase of water from the City of
8 Tucson to-date are approximately 50 percent higher than in 2000.

9 The intervenor homeowners support the \$.41 per 1,000 gallon surcharge but argue that it
10 should be applied on both residential users and the golf course users, because all users are responsible
11 for the demand on the aquifer.

12 Staff expressed the opinion that the Company's current request constitutes an emergency and
13 interim emergency rates should be approved. The drought caused a sudden change in operating
14 conditions that has in turn caused a financial hardship. Staff reviewed the Company's financial
15 statements and had conversations with representatives of the Company's parent company. The
16 Company's financial statements indicate that it does not have the resources to pay the additional
17 charges. Forty Niner's parent company, or an affiliate of the parent company, has been lending the
18 Company the funds to pay the City of Tucson. The loans from the parent company have allowed
19 Forty Niner to keep current on its bills to the City of Tucson.

20 Staff recommends that the Company be authorized an interim \$.41 per 1,000 gallons
21 temporary surcharge for all domestic and golf course water usage. Staff recommends that the
22 temporary surcharge remain in effect until Forty Niner recovers the costs of purchasing the City of
23 Tucson water incurred during the calendar year 2002.⁴ Staff further recommends that Forty Niner be
24 ordered to offset any recovery of these costs by \$.17 per 1,000 gallons purchased to reflect Forty
25 Niner's cost savings from reduced purchased pumping power requirements. Staff explained that the
26 offset would not reduce the \$.41 per 1,000 gallons collected from users, but would offset the total
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28 ⁴ Any purchases required in 2003 would be addressed as part of the permanent rate case.

1 amount that could be collected from ratepayers.

2 Staff further recommends that Forty Niner be ordered to file monthly reports with the Director
3 of the Utilities Division within 15 days of the end of each month, documenting amounts collected
4 pursuant to the interim surcharge, and that the surcharge should terminate without further action of
5 the Commission upon Forty Niner's recovery of the calendar year 2002 purchased water costs net of
6 purchased pumping power savings. Staff further recommends that Forty Niner be ordered to provide
7 the Commission with a bond equivalent to the total amount expected to be collected through the
8 interim surcharge, within 30 days of the date of the Commission's Decision in this matter. Staff
9 recommends that the reasonable costs of obtaining the bond be included in Forty Niner's recovery
10 through the surcharge.

11 Staff recommends that Forty Niner be ordered to file a permanent rate increase request within
12 three months of the effective date of a Commission Decision in this proceeding, and that as part of its
13 filing it include potential solutions to the water supply problems that have caused its emergency rate
14 applications. Staff also recommends that in the event Forty Niner effects the sale of the system to
15 the City of Tucson, or any other entity, that it provide the Commission with a full and final
16 reconciliation of the interim surcharge.

17 Staff's recommendations are reasonable. In less than six months, the Company has incurred
18 unanticipated, but necessary, expenses of almost \$100,000. In approving the Company's last rate
19 case, a little over a year ago, the Commission approved operating expenses of \$169,676. Thus, the
20 drought-caused emergency has increased the operating expenses of the Company by almost 60
21 percent, before adjusting for the savings in purchased power costs. The Company has had to borrow
22 from affiliates to pay the City of Tucson, and without that financial support would have been unable
23 to make payments to the City. "The severity of the current drought, and the need to supplement the
24 Company's water supply, was not anticipated in the previous rate case, which approved an increase in
25 the monthly minimum of \$1.50, from \$7.00 to \$8.50, and a commodity increase of \$.04, from \$.56
26 per 1,000 gallons to \$.60 per 1,000 gallons, for usage up to 20,000 gallons.

27 The Company has not implemented the rates approved in the last permanent rate case because
28 it has not reduced copper levels below the acceptable maximum. However, even if it had

1 implemented the new rates, those rates would not have been sufficient to prevent the current
2 emergency situation, as the Company purchases water from the City for \$3.59 per 1,000 gallons.

3 The record does not contain sufficient information to determine why the Company has not
4 corrected the copper problem. Although we are cognizant of the financial burden associated with
5 rectifying the problem on the Company as well as on ratepayers, we cannot allow a water company to
6 ignore water quality regulations. If the sale of the Company cannot be finalized prior to the time it
7 would take the Commission to process a permanent rate case, we believe the water quality problem,
8 as well as a permanent solution to the water supply problem, are best addressed in the context of a
9 comprehensive permanent rate case.

10 We authorize the Company to implement an interim \$.41 per 1,000 gallon surcharge on all
11 customers until the Company has collected the total amount it expended in the calendar year 2002 for
12 the purchase of water from the City of Tucson. Within 30 days of the end of the year, Forty Niner
13 shall file a report with the Commission detailing the total gallons purchased from the City of Tucson,
14 as well as the total costs. The amount to be recovered from the surcharge shall be reduced by \$.17
15 per 1,000 gallons purchased to adjust for the estimated amount the Company saved pumping power
16 costs.

17 If in a permanent rate case, to be filed within 90 days of the date of this Decision, the
18 Company cannot justify the amount to be collected from the interim surcharge, the amounts collected
19 shall be refunded to the ratepayers. Staff has recommended that the Company secure a bond as
20 security for a potential refund and that the costs of such a bond be added to the amounts recovered
21 from ratepayers. The Arizona Court of Appeals held in RUCO vs. Ariz Corp. Comm'n and Rio
22 Verde Utilities, Inc., 199 Ariz. 588, 20 P.3d 1169 (Ct. App. 2001), that when the Commission
23 approves interim rates without "a finding of fair value, all three of the following elements must be
24 present: 1) an emergency; 2) the posting of a bond; and 3) a subsequent full rate case. Thus, we order
25 the Company to secure a bond, and authorize that the reasonable costs thereof may be collected as
26 part of the surcharge.

27 While it may appear that the amount of the surcharge should be higher than \$.41 per 1,000
28 gallons so that the Company can recover its emergency expenses prior to next summer and the

1 potential need to make additional purchases, we are mindful that in the last rate case the surcharge
2 increased the average residential bill by \$10.18. We believe such charge is significant but also
3 reasonable under these circumstances. Depending on when the Company is able to file its permanent
4 rate case, we may be able to resolve that request before the amounts associated from the current
5 emergency are fully recovered. We reserve the right to adjust or eliminate the surcharge by future
6 order.

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

9 **FINDINGS OF FACT**

10 1. Forty Niner provides water utility service to approximately 345 residential customers
11 and a golf course in the subdivision known as Forty Niner Country Club Estates, located east of
12 Tucson in Pima County, Arizona.

13 2. On July 19, 2002, Forty Niner filed an application with the Commission for an
14 emergency increase in rates.

15 3. By Procedural Order dated August 21, 2002, the matter was set for a hearing on
16 September 6, 2002, at the Commission's offices in Tucson, Arizona.

17 4. Mr. John Malamus, representing the Forty-Niner Country Club Estates Homeowners
18 Association, was granted intervention.

19 5. A hearing convened on September 6, 2002. Mr. Buck Lewis, President of Southwest
20 Utility Management, Inc., the management company for Forty Niner, testified on behalf of the
21 Company. Mr. Malamus testified for the Homeowners and Mr. Darren Carlson testified on behalf of
22 Staff.

23 6. In the late Spring of 2002, drought conditions caused the Company to notify its
24 customers that its water usage was exceeding its pumping and storage capacity, and was causing the
25 Company to have to purchase water from the City of Tucson.

26 7. From May 2002 through September 16, 2002, the Company purchased water from the
27 City of Tucson for a total cost of \$98,463.

28 8. Forty Niner did not, and does not, have the financial resources to pay the City of

1 Tucson. The Company's parent company has lent the Company money to keep its bills with the City
2 of Tucson current.

3 9. Forty Niner requested a surcharge of \$.41 per 1,000 gallons be applied to residential
4 customers to recover the amounts expended to purchase water from the City of Tucson.

5 10. Staff recommends the following:

6 (a) the Company be authorized an interim \$.41 per 1,000 gallons temporary surcharge
7 for all domestic and golf course water usage;

8 (b) the temporary surcharge remain in effect until Forty Niner recovers the costs of
9 purchasing the City of Tucson water during the calendar year 2002, and that the Company be ordered
10 to offset any recovery of these costs by \$.17 per 1,000 gallons purchased to reflect its cost savings
11 from reduced purchased pumping power requirements;

12 (c) Forty Niner be ordered to file monthly reports with the Director of the Utilities
13 Division within 15 days of the end of each month, documenting amounts collected pursuant to the
14 interim surcharge, and the surcharge shall terminate without further action of the Commission upon
15 Forty Niner's recovery of the calendar year 2002 purchased water costs net of purchased pumping
16 power savings;

17 (d) Forty Niner be ordered to provide the Commission with a bond equivalent to the
18 total amount expected to be collected through the interim surcharge, within 30 days of the date of the
19 Commission's decision in this matter, and that the reasonable costs of obtaining the bond be included
20 in the amount to be recovered through the surcharge;

21 (e) Forty Niner be ordered to file a permanent rate increase request within three
22 months of the effective date of a Commission Decision in this proceeding, and that it include
23 potential solutions to the water supply problems that have caused its emergency rate applications as
24 part of the permanent rate increase;

25 (f) in the event Forty Niner effects the sale of the system to the City of Tucson, or any
26 other entity, it will provide the Commission with a full and final reconciliation of the interim
27 surcharge.

28 11. Staff believes that Forty Niner meets the requirements for emergency rate relief

1 consistent with Attorney General Opinion No. 71-17 because drought conditions caused a sudden
2 change in operations and financial hardship from having to purchase water from the City of Tucson at
3 a cost many times greater than the rates it is able to charge its users.⁵

4 12. The Company has borrowed money from its parent to purchase domestic use water
5 from the City of Tucson.

6 13. The homeowners, through their intervenor representative, supported the \$.41 per 1,000
7 surcharge, but believed that the surcharge should apply to the golf course as well as the residential
8 users.

9 14. The drought conditions and the Company's inability to pay for water purchased from
10 the City of Tucson without borrowing constitute an emergency under Attorney General Opinion 71-
11 17.

12 15. The Company is not in compliance with ADEQ regulations because the water it
13 delivers from its own wells exceeds the maximum contaminant levels for copper.

14 16. The Company had been trying to increase the pH of its water by aerating its tanks,
15 and thereby ameliorating copper levels, however, usage that has exceeded the ability to pump and
16 store water has made aeration ineffective in reducing copper levels.

17 17. The Company states it could address the copper problem either by adding storage or
18 by chemical additives, but either solution would be costly.

19 18. There is no evidence that the water the Company purchases from the City of Tucson
20 does not meet quality standards of the Safe Drinking Water Act.

21 19. The Company's water quality and long-term water supply issues are best addressed in
22 connection with a permanent rate case.

23 20. All users contribute to the demand on the aquifer and should bear responsibility for the
24 emergency expense of augmenting the water supply.

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27 ⁵ According to Attorney General Opinion No. 71-17, interim or emergency rates are proper when either all or any
28 of the following conditions occur: when sudden change brings hardship to a Company; when the Company is insolvent;
or when the condition of the Company is such that its ability to maintain service pending a formal rate determination is in
serious doubt.

CONCLUSIONS OF LAW

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2 1. Forty Niner is a public service corporation within the meaning of Article XV of the
3 Arizona Constitution and A.R.S. §§ 40-250, 40-251, 40-252.

4 2. The Commission has jurisdiction over Forty Niner and of the subject matter of the
5 application.

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

7 4. Forty Niner is facing an "emergency" within the definition set forth in Attorney
8 General Opinion No. 71-17.

9 5. Staff's recommendations for an interim emergency surcharge for \$0.41 per thousand
10 gallons is just and reasonable and should be approved.

11 6. The surcharge should be collected by means of adding a charge of \$0.41 per 1,000
12 gallons usage to each customer's monthly bill until the net costs of purchasing the water from the
13 City of Tucson are recovered.

14 7. Staff's recommendations set forth in Findings of Fact No. 10 are reasonable.

ORDER

15
16 IT IS THEREFORE ORDERED that Forty Niner Water Company shall recover its
17 emergency expenses as discussed hereinabove by means of a surcharge of \$0.41 per thousand gallons
18 per month per customer.

19 IT IS FURTHER ORDERED that the surcharge approved herein shall be interim and subject
20 to refund pending the Commission's review of Forty Niner Water Company's permanent rate
21 application.

22 IT IS FURTHER ORDERED that within 30 days of the date of this Decision, Forty Niner
23 Water Company shall provide the Commission with proof of a bond equivalent to the total amount to
24 be collected through the interim surcharge.

25 IT IS FURTHER ORDERED that Forty Niner Water Company may add the reasonable costs
26 of the bond to the amount to be recovered by means of the surcharge.

27 IT IS FURTHER ORDERED that Forty Niner Water Company shall file a report with the
28 Director of the Utilities Division by January 31, 2003, that details the total gallons purchased, and the

1 cost thereof, from the City of Tucson in calendar year 2002. Forty Niner Water Company shall
2 reduce the amount to be recovered from ratepayers under the surcharge by \$.17 per 1,000 gallons
3 purchased to account for the savings in purchased pumping power and by the amount of additional
4 revenue it would have collected pursuant to Decision No. 63870 had it corrected the copper problem.
5 The report shall include the total amount of water purchased and the calculation of the amount of the
6 adjustment for the purchased power savings, as well as the cost of the bond.

7 IT IS FURTHER ORDERED that Forty Niner Water Company shall file monthly reports with
8 the Director of the Utilities Division within 15 days of the end of each month, documenting amounts
9 collected pursuant to the interim surcharge, and the surcharge shall terminate without further action
10 of the Commission upon Forty Niner Water Company's recovery of the calendar year 2002
11 purchased water costs net of purchased pumping power savings.

12 IT IS FURTHER ORDERED that Forty Niner Water Company shall file a permanent rate
13 increase request within three months of the effective date of this Decision, and shall include as part of
14 its filing, potential solutions to its water quality and water supply problems that have caused its
15 emergency rate applications.

16 IT IS FURTHER ORDERED that in the event Forty Niner Water Company effects the sale of
17 the system to the City of Tucson, or any other entity, it will provide the Commission with a full and
18 final reconciliation of the interim surcharge.

19 IT IS FURTHER ORDERED that Forty Niner Water Company shall file on or before October
20 31, 2002, a tariff authorizing it to collect the temporary \$0.41 per thousand gallons emergency
21 surcharge.

22 IT IS FURTHER ORDERED that the surcharge authorized hereinabove shall be effective for
23 all service provided on and after November 1, 2002.

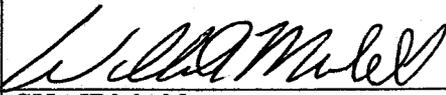
24 IT IS FURTHER ORDERED that Forty Niner Water Company shall notify its customers of
25 the emergency surcharge authorized herein and the effective date of same by mailing notice to its
26 customers within five days of the effective date of this Decision.

27 ...
28 ...

1 IT IS FURTHER ORDERED that Forty Niner Water Company shall file with the Director of
2 the Utilities Division, within ten days of the effective date of this Decision, a copy of the Notice
3 mailed to its customers.

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

5 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

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7   
8 CHAIRMAN COMMISSIONER COMMISSIONER

9 IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive
10 Secretary of the Arizona Corporation Commission, have
11 hereunto set my hand and caused the official seal of the
12 Commission to be affixed at the Capitol, in the City of Phoenix,
13 this 1st day of November, 2002.

14 
15 BRIAN C. McNEIL
16 EXECUTIVE SECRETARY
17 DISSENT _____

18 JR:mlj
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1 SERVICE LIST FOR:

FORTY NINER WATER COMPANY

2 DOCKET NO.

W-01777A-02-0547

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