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BEFORE THE ARIZONA CORPORATION COMMISSION

DOCKETED

SEP 23 2002

WILLIAM A. MUNDELL
CHAIRMAN
JIM IRVIN
COMMISSIONER
MARC SPITZER
COMMISSIONER

DOCKETED BY *clp*

IN THE MATTER OF THE FINANCING
APPLICATION FOR RIDGEVIEW UTILITY
COMPANY, AND THE APPLICATION BY
RIDGEVIEW UTILITY COMPANY AND LAGO
DEL ORO WATER COMPANY TO ENTER INTO
A WATER FACILITY SHARING AGREEMENT.

DOCKET NO. W-03861A-01-0167
DOCKET NO. W-01944A-01-0167

DECISION NO. 65216

ORDER

Open Meeting
September 17 and 18, 2002
Phoenix, Arizona

BY THE COMMISSION:

On November 25, 1998, the Arizona Corporation Commission ("Commission") issued Decision No. 62861 which granted Ridgeview Utility Company ("Ridgeview", "Applicant" or "Company") a Certificate of Convenience and Necessity ("Certificate") to provide water utility service to the public in Pima County, Arizona, near the city of Tucson. Ridgeview's service area includes a proposed 800-acre, age-restricted master planned community known as Saddlebrook Ranch that will have approximately 600 homes at build out.

On February 26, 2001, Ridgeview filed a financing application requesting that the Commission authorize Ridgeview to enter into certain specified financial transactions approving the issuance of up to \$2,400,000 of new common stock. The application also requested authority to enter into a water facility sharing agreement with Lago Del Oro Water Company ("Lago").

On February 24, 2001, Ridgeview published notice of its application in The Arizona Daily Star in Pima County.

On March 30, 2001, the Residential Utility Consumer Office ("RUCO") filed an application to intervene.

On April 11, 2001, the Commission granted RUCO intervention.

On March 1, 2002, Staff filed a Staff Report regarding Ridgeview's application. In that

1 report, Staff recommended that Ridgeview be authorized to issue up to \$1,800,000 in stock equity.
2 That amount represents Ridgeview's requested financing authorization of \$2,400,000 less \$600,000
3 related to the initial distribution system. The Staff Report recommended that Ridgeview should
4 construct the distribution system with Advances-in-Aid of Construction ("AIACs"), which Staff
5 refers to as a zero-cost source of capital. The Staff Report recommends the Commission take no
6 action on the water facility sharing agreement between Ridgeview and Lago as Staff believes that
7 Commission approval is not necessary.

8 On March 8, 2002, RUCO filed comments concurring with the Staff Report.

9 On May 23, 2002, Ridgeview filed objections to the Staff Report. The Company objected to
10 the use of AIACs.

11 Discussion

12 The sole issue in dispute in this matter is whether or not to use AIACs to finance the water
13 distribution system. Applicant argues that it should be allowed to fund the distribution system with
14 equity. Staff and RUCO recommended that, as a condition of granting the financing application, the
15 Applicant should be required to use AIACs to fund the distribution system.

16 **A. Ridgeview's Arguments**

17 In the objections filed to the Staff Report, Applicant objected to Staff's recommendation to
18 use AIACs. Applicant argued that shareholders should provide the funds for the initial facilities.

19 Applicant argued that there is no provision in rates that provide the funds required to refund
20 the obligations under the AIACs. Therefore, Applicant argued, the Applicant might not generate the
21 funds required to pay for the AIACs.

22 Applicant cited to the cash flow problems that affected Pima Utility Company ("Pima") when
23 it used AIACs previously. Applicant stated that Pima financed all of the water and sewer line
24 extensions in the community of Sun Lakes with AIACs. The Applicant then noted that, from 1987 to
25 1992, Pima had to file three rate cases. According to the Applicant, the reason for these rate cases
26 was that Pima was so far in arrears due to the refund requirement of the AIACs that it simply did
27 not have the cash flow to operate properly.

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1 The Company argued that the use of AIACs would eventually require an order from the
2 Commission authorizing a rate increase and/or the issuance of equity to repay the obligations. The
3 Company cites Decision No. 57645 (November 2, 1991) which not only authorized Pima to increase
4 rates, but also approved over \$2,000,000 in equity, most of which was used to pay the AIAC
5 obligations that were in arrears.

6 Applicant stated that, in more recent applications, similarly situated utilities have been
7 allowed to finance their infrastructure using 100 percent equity. Applicant argued that a benefit to its
8 proposal is that the enormous cost of applying for and litigating an additional rate case and/or
9 financing applications, which are passed on to the ratepayers, can be avoided if the Company's
10 proposal to finance the initial systems with equity is adopted.

11 Applicant argued that the particular situations where AIACs should be utilized do not exist in
12 these matters. Applicant states they will be providing service to residential lots that are similarly
13 situated, sized uniformly and are constructed sequentially in the development. The lines are neither
14 exclusive to one service area, nor are the costs disproportionate to any one customer, which obviates
15 the need for AIACs. Additionally, the Applicant pointed out that A.A.C. R14-2-406(D) does not
16 mandate the use of AIACs to finance line extensions.

17 Applicant argued that Staff and RUCO's fear of the Applicant expanding the utility too
18 quickly and, therefore, burdening the ratepayers was unwarranted. Applicant argued that if the
19 utilities proceeded down that path, then the Commission would make determinations as to what plant
20 was used and useful and, thereby, restrict the utility's to earn a return on anything not deemed used
21 and useful.

22 Applicant also argued that Staff and RUCO's concern regarding the possibility that
23 Applicant's customers will pay line extension costs twice is unfounded in these applications. RUCO
24 asserted that when the developer is an affiliate of the utility, as is in the case of Ridgeview, line
25 extensions should be treated as having been funded by AIACs in setting initial rates. RUCO
26 advocated this policy to ensure that ratepayers do not pay the cost of line extensions twice, first in the
27 price of their homes and again in their utility rates. Robson Communities is the developer of
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1 Saddlebrook Ranch, and is an affiliate of the Applicant. Applicant argued that there was no evidence
2 that proved Robson Communities would charge a water utility development fee to homeowners.

3 **B. Staff and RUCO's Arguments.**

4 RUCO and Staff recommend that the distribution system be financed with AIACs. Staff and
5 RUCO contended that the use of AIACs is appropriate in this case. Staff stated that AIACs benefit
6 ratepayers because they are a cost free source of capital compared to equity. Staff further argued that,
7 when AIACs are used, there is a reduction in rate base, which in turn reduces required operating
8 income. According to Staff, the use of AIACs results in a reduced revenue requirement for the
9 Company, which ultimately results in lower rates for customers.

10 Staff and RUCO also argued that the AIACs in this case can be distinguished from the AIACs
11 used in the Pima Utility Company case. Staff and RUCO noted that in the Pima case, Pima was
12 unable to make the refunds that were required under its advances because during that time period, 70
13 percent of the total plant funded was attributable to AIACs, and that the period of time for calculating
14 the refund amounts was based on a either 10-year or 15-year recovery period. In contrast, in this
15 matter, Staff is recommending that AIACs fund only 19 to 21 percent of the entire new plant.

16 Finally, RUCO and Staff argued that these are new developments and that, although the
17 developer has a track record for successful communities, there are no guarantees in the future as to
18 the success of the communities that these utilities are proposed to serve. In light of the fact that the
19 Company would not commit to making a non-used and useful adjustment in the forthcoming rate
20 case, RUCO argued that AIACs are the only possible way to add some certainty to the future. RUCO
21 argued that the Applicant should be required to finance the line extensions through AIACs, as that
22 would add some certainty that the ratepayers would not be subject to the risk in the event that the
23 development is not successful." Staff and RUCO also argued that there is a possibility that customers
24 will pay line extension costs twice, both in the price of the home and in the utility rates.

25 **C. Analysis**

26 We find Staff and RUCO's arguments compelling in this matter. However, we do not agree
27 that AIACs are a 'cost free source of capital' merely because their costs are not included in Rate
28 Base. A.A.C. R14-2-406.D requires companies to refund "a minimum amount equal to 10% of the

1 total gross annual revenue from water sales” for a period of not less than ten years. Revenues
2 refunded or deferred have the same effect as a cost to the entity and increase the likelihood of
3 financial instability thus necessitating the more frequent filing of rate cases.

4 Given that the development in question is an age-restricted master planned community; we
5 recognize that the difficulty of implementing rate increases over the objections of ratepayers will add
6 to the cost and complexity of rate cases and will increase the likelihood that the utility will under-earn
7 in violation of the Commission’s obligation to ensure just and reasonable rates. This Commission
8 must balance the interests of ratepayers in having low rates with the long-term interests of ratepayers
9 and utilities in ensuring that utilities are financially sound and able to meet both anticipated operating
10 and maintenance costs and unanticipated operating and maintenance costs.

11 Therefore, we find in this case, the use of 100% equity financing is in the long-term interest of
12 ratepayers and the utilities.

13 * * * * *

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

16 **FINDINGS OF FACT**

17 1. On November 25, 1998, the Commission issued Decision No. 62861 which granted
18 Ridgeview a Certificate to provide water utility service to the public in Pima County, Arizona, near
19 the city of Tucson.

20 2. On February 26, 2001, Ridgeview filed a financing application requesting that the
21 Commission authorize Ridgeview to enter into certain specified financial transactions approving the
22 issuance of up to \$2,400,000 of new common stock. The application also requested authority to enter
23 into a water facility sharing agreement with Lago Del Oro Water Company.

24 3. On February 24, 2001, Ridgeview published notice regarding its application in The
25 Arizona Daily Star in Pima County.

26 4. Ridgeview’s service area includes a proposed 800-acre, age-restricted master planned
27 community known as SaddleBrook Ranch.

28 5. Ridgeview does not serve any customers. However, it is anticipated that Ridgeview

1 will provide water services to approximately 600 homes in Saddlebrook Ranch at build-out.

2 6. The funds provided by the proposed \$2,400,000 stock issuance will be used to pay for
3 the design and construction of Ridgeview's initial water infrastructure.

4 7. On March 1, 2002, Staff filed a Staff Report regarding Ridgeview's application for
5 approval for financing. In that report, Staff recommended that Ridgeview be authorized to issue up
6 to \$1,800,000 in stock equity. That amount represents Ridgeview's requested financing authorization
7 of \$2,400,000 less \$600,000 related to the initial distribution system. The Staff Report recommended
8 that Ridgeview should construct the distribution system with Advances-in-Aid of Construction
9 ("AIACs"), which Staff refers to as a zero-cost source of capital.

10 8. The Staff Report recommends the Commission take no action on the water facility
11 sharing agreement between Ridgeview and Lago as Staff believes that Commission approval is not
12 necessary.

13 9. Staff Engineering has reviewed Ridgeview's application and considers the proposed
14 design construction cost to be reasonable and appropriate.

15 10. AIACs are contracts between a developer and the utility that provide for the developer
16 to finance the initial cost of a line extension. If the development is successful and the utility
17 generates revenues from the customers on the line extension, then the utility refunds a percentage of
18 those revenues to the developer over time.

19 11. On March 8, 2002, RUCO filed comments regarding Ridgeview's application, which
20 concurred with Staff's recommendations.

21 12. On May 23, 2002, Ridgeview filed objections to the Staff Report.

22 13. Applicant filed affidavits of publication that comply with the notice requirement as
23 prescribed by law.

24 14. The use of reasonable amounts of AIACs will reduce the risk to ratepayers if a
25 proposed development is not successful.

26 15. When a developer is an affiliate of a utility, stricter scrutiny must be applied when
27 reviewing rate and financing applications.

28 16. The Commission has analyzed the issues and evidence as presented by the parties and

1 has resolved the issues as stated in the Discussion above.

2 17. The Commission hereby adopts and incorporates the Discussion and the
3 Commission's resolution of the issues therein.

4 18. The Applicant has agreed to provide financial information from the affiliated
5 developer(s) for Commission Staff to review pursuant to a confidential/proprietary agreement in
6 order to ascertain whether homeowners are being charged for utility plant or expenses in the costs of
7 their homes.

8 19. Further, the Applicant has agreed to not file a rate case application for at least 60
9 months after the date it provides permanent service to its first customer.

10 **CONCLUSIONS OF LAW**

11 1. Ridgeview Utility Company is a public service corporation within the meaning of
12 Article XV of the Arizona Constitution and A.R.S. §§ 40-301 and 40-302.

13 2. The Commission has jurisdiction over Ridgeview Utility Company and the subject
14 matter of the applications.

15 3. Staff's recommendation that Commission action is unnecessary regarding the water
16 facility sharing agreement between Ridgeview and Lago is reasonable and should be adopted.

17 4. A.A.C. R14-2-406(D) does not mandate the use of the AIACs.

18 5. Notice of the application was given in accordance with the law.

19 6. The financing approved herein is for lawful purposes within Ridgeview Utility
20 Company's corporate powers, is compatible with the public interest, with sound financial practices,
21 and with the proper performance by Ridgeview Utility Company of service as public service
22 corporations, and will not impair Ridgeview Utility Company's ability to perform that service.

23 7. The financing approved herein is for the purposes stated in the applications and is
24 reasonably necessary for those purposes, and such purposes are not, wholly or in part, reasonably
25 chargeable to operating expenses or to income.

26 **ORDER**

27 IT IS THEREFORE ORDERED that Ridgeview Utility Company is authorized to issue up to
28 \$2,400,000 in stock equity.

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1 IT IS FURTHER ORDERED that Ridgeview Utility Company shall provide the financial
2 information from the affiliated developer(s) for Staff of the Arizona Corporation Commission to
3 review pursuant to a confidential/proprietary agreement in order to ascertain whether homeowners
4 are being charged for utility plant or expenses in the costs of their homes.

5 IT IS FURTHER ORDERED that Ridgeview Utility Company shall provide the financial
6 information from the affiliated developer(s) to the Staff of the Arizona Corporation Commission
7 within a reasonable time period, not to exceed 30 days after such request.

8 IT IS FURTHER ORDERED that Ridgeview Utility Company shall not file a rate case
9 application for at least 60 months after the date it provides permanent service to their first customer.

10 IT IS FURTHER ORDERED that Ridgeview Utility Company is hereby authorized to engage
11 in any transactions and to execute any documents necessary to effectuate the authorization granted
12 herein.

13 IT IS FURTHER ORDERED that such authority is expressly contingent Ridgeview Utility
14 Company's use of the proceeds for the purposes set forth in its application.

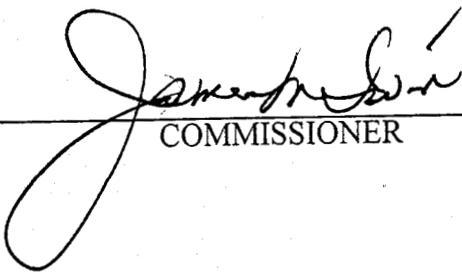
15 IT IS FURTHER ORDERED that approval of the financing set forth herein does not
16 constitute or imply approval or disapproval by the Commission of any particular expenditure of the
17 proceeds derived thereby for purposes of establishing just and reasonable rates.

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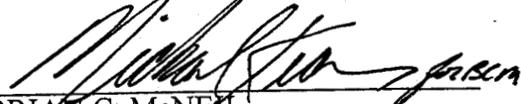
1 IT IS FURTHER ORDERED that Ridgeview Utility Company shall file with the Commission
2 copies of all executed financing documents setting forth the terms of the financing within 30 days of
3 obtaining such financing.

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

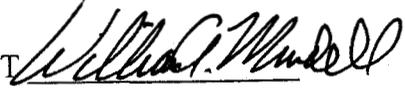
5 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

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8 CHAIRMAN  COMMISSIONER  COMMISSIONER

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10 IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive
11 Secretary of the Arizona Corporation Commission, have
12 hereunto set my hand and caused the official seal of the
13 Commission to be affixed at the Capitol, in the City of Phoenix,
14 this 23rd day of SEPT., 2002.

15 
16 BRIAN C. McNEIL
17 EXECUTIVE SECRETARY

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DISSENT 

PD:mlj

1 SERVICE LIST FOR:

RIDGEVIEW UTILITY COMPANY

2 DOCKET NOS.

W-03861A-01-0167 and W-011944A-01-0167

3 James Poulos
4 Ridgeview Utility Company
5 Lago del Oro Water Company
6 9532 East Riggs Road
7 Sun Lakes, AZ 85248

8 Scott Wakefield, Chief Counsel
9 RUCO
10 2828 N. Central Avenue, Ste. 1200
11 Phoenix, AZ 85004

12 Ernest Johnson, Director
13 Utilities Division
14 ARIZONA CORPORATION
15 1200 West Washington Street
16 Phoenix, AZ 85007

17 Chris Kempley, Chief Counsel
18 Legal Division
19 ARIZONA CORPORATION COMMISSION
20 1200 W. Washington Street
21 Phoenix, AZ 85007

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DISSENTING OPINION
of
CHAIRMAN WILLIAM A. MUNDELL

COMPANY: Ridgeview Utility Company
Application for Financing and the
Application by Ridgeview Utility
Company and Lago Del Oro Water
Company to Enter into a Water
Facility Sharing Agreement

OPEN MEETING DATE: 9-17-02

DOCKET NO. W-03861A-01-0167
W-01944A-01-0167

AGENDA ITEM: U-22

I respectfully dissent from the majority opinion and the Analysis, Findings of Fact, and the Conclusions of Law in this decision. In particular, I do not agree with the policy conclusions and the analysis behind it. I prefer a policy that treats a utility who is an affiliate of the developer, as is the situation in this case, as a separate and unique entity.

When a developer desires to have water or sewer services provided to a subdivision and approaches the appropriate holder of the certificate of convenience and necessity ("CC&N"), it is common for the holder of the CC&N to require Advances in Aid of Construction ("AIACs") to cover the cost of distribution or collection lines necessary for the extension of service. The rationale is that the developer accepts some risk for the success of the subdivision in exchange for being able to connect to a certificated provider's system. Application of the arm's length transaction mechanism between the developer and the certificated provider would, in my opinion, have been appropriate in this case.

CHAIRMAN WILLIAM A. MUNDELL
DISSENTING OPINION
SEPTEMBER 17, 2002
DOCKET NO. W-03861A-01-0167 ET.AL.

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I also respectfully disagree with the analysis in the Order. The AIACs are a cost-free source of capital to the certificated provider. There should be no debate on this point. The fact that in this case an affiliated relationship exists between the developer and the utility does not change the basic rate-making principles of how AIACs are factored into rates. I also disagree that revenues refunded or deferred have the same effect as a cost to the utility. AIAC refunds are not included as a cost of service unlike other costs. Therefore, they do not increase the utility's revenue requirement like other costs. I am not persuaded that AIACs when used in appropriate proportion to the utility's plant, increase the likelihood of the utility's financial instability or contribute to the need to have more frequent rate cases.

I was pleased that my colleagues reiterated the position that each financing application is determined separately on its merits and the facts specific to that case. We seem to be in accord that there should be no precedent presumed from the majority's decision in this case. I appreciate my colleagues encouraging me to express my opinion on these matters.



William A. Mundell
Chairman

Decision No. 65216