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MEMORANDUM

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2001 JUL 20 P 4: 52

FROM: Deborah R. Scott
for Director
Utilities Division

AZ CORP COMMISSION
DOCUMENT CONTROL

DATE: July 20, 2001

RE: AMENDED STAFF REPORT FOR THE APPLICATION OF DIVERSIFIED WATER UTILITIES, INC., AN ARIZONA CORPORATION, FOR AUTHORITY TO ISSUE DEBT (DOCKET NO. W-02859A-00-0964)

Attached is the amended Staff Report for the application of Diversified Water Utilities, Inc. for approval to issue long-term debt. Since the original Staff Report was filed, Diversified completed a project for which financing was requested. Because the project was completed below budget, the amount of debt required was reduced. Staff recommends approval of the reduced amount of debt without a hearing.

DRS:LAJ:bsl

Originator: Linda A. Jaress

Attachment: Original and eleven copies

Arizona Corporation Commission

DOCKETED

JUL 20 2001

DOCKETED BY	<i>SD</i>
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AMENDED
STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION

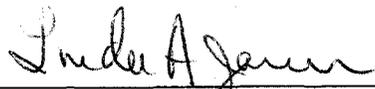
DIVERSIFIED WATER UTILITIES, INC.
DOCKET NO. W-02859A-00-0964

APPLICATION
FOR AUTHORITY TO ISSUE LONG-TERM DEBT

July, 2001

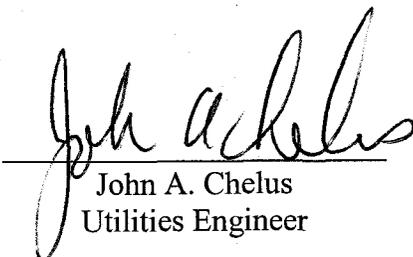
STAFF ACKNOWLEDGMENT

The financial analysis contained in the Staff Report for Diversified Water Utilities, Inc., Docket No. W-02859A-00-0964, was prepared by Linda A. Jaress.



Linda A. Jaress
Executive Consultant 111

The engineering analysis contained in the Staff Report was prepared by John A. Chelus, Utilities Engineer.



John A. Chelus
Utilities Engineer

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ATTACHMENTS

Exhibit 1

On November 22, 2000, Diversified Water Utilities, Inc., ("Diversified" or "the Company"), filed an application for approval to issue debt in the amount of \$58,428.30 to Skyline Vista Ranch, L.L.C., ("Skyline" or "the Developer") and \$378,900 to the Water Infrastructure Financing Authority ("WIFA"). On April 20, 2001, Staff filed its Staff Report recommending approval.

One of the purposes of the proposed WIFA debt was to purchase and install a 250,000-gallon storage tank. During the week of June 10th, Staff was informed that Diversified had completed the installation of a 200,000-gallon storage tank, which cost \$25,000 less than the planned 250,000-gallon tank. Engineering Staff believes that the smaller tank will be sufficient and that the cost is reasonable.

Through conversations with the Diversified's owner and manager, Diversified will amend its application to WIFA to reduce the requested debt from \$378,900 to \$353,900. The Skyline debt is unchanged.

The Ability of Diversified to Service the Proposed Debt

Attached is a Revised Exhibit 1 that represents the original Exhibit 1 adjusted for the lower amount of debt requested from WIFA. The abbreviated financial statements and debt service analysis shown on Revised Exhibit 1 still results in debt service requirements exceeding cash flow, although by a lower amount. The deficiency fell from \$33,182 to \$24,882. Besides the lower amount of WIFA principal, the Prime Rate upon which the WIFA interest rate is based has fallen further reducing the deficiency.

The Company contends that the funds generated by its hook-up fee will be sufficient to make up the difference between cash uses and cash sources. As previously mentioned in the original Staff Report, the Company has provided Staff with a copy of a written request for service sent by a representative of Skyline to Diversified, Salt River Project, Qwest, the City of Mesa, and Cox for planning purposes. Skyline expects to build three phases of a subdivision "as soon as they obtain all of the required approvals." Diversified expects that within one year, it will receive \$91,800 in hook-up fees from the three phases of the Skyline subdivision. If the customers materialize, Diversified will also experience increased revenues.

Staff believes there is some risk, as is common in the real estate industry, that some or all of the planned subdivision will not materialize and that current customers, under current rates, may not generate sufficient revenues to adequately cover debt service related to the proposed debt. However, due to the Company's continued reluctance to raise rates, Staff still recommends the same alternative solution as in the original Staff Report.

Staff recommends that the Company file a cash flow statement for the most recent 12 month period in the docket on July 31, 2002, for Staff's review. Staff also recommends that the Commission approve the total amount of debt requested by the Company with the additional condition that if Diversified does not generate positive cash flow by June 30, 2002, that the

Company file for a rate increase by September 30, 2002. These conditions should reduce the risk of financial harm that the Company would experience if the additional customers do not materialize.

Conclusions and Recommendations

Staff recommends approval of Diversified's application for approval to issue debt in the amount of up to \$58,428.30 to Skyline Vista Ranch, L.L.C., and up to \$353,900 to the Water Infrastructure Financing Authority.

The terms of the Skyline loan will be five years at 8.0 percent interest. The WIFA terms will be determined at the time the loan is drawn.

Staff believes the debt is for utility purposes, and the projects and their estimated costs are reasonable.

Staff recommends that the Company file a cash flow statement for the most recent 12 month period in the docket on July 31, 2002, for Staff's review.

Staff further recommends that if Diversified does not generate positive cash flow, including principal and interest payments on the proposed debt by June 30, 2002, then the Company shall file for a rate increase by September 30, 2002.

Under these conditions, Staff believes that the proposed debt is in the public interest, is compatible with sound financial practices, and should be approved.

DIVERSIFIED WATER UTILITIES, INC.
Years Ending December 31, 1999 and 2000

Abbreviated Income Statement

	<u>1999</u>	<u>2000</u>
Revenue	\$ 93,988	\$ 102,606
Depreciation	\$ 7,908	\$ 20,154
Op. Expenses	<u>\$ 82,431</u>	<u>\$ 67,207</u>
Total Op. Expenses	\$ 90,339	\$ 83,157
Op. Income	<u>\$ 3,649</u>	<u>\$ 19,449</u>
Interest Exp. Net	\$ 5,360	\$ 4,130
Net Income	<u>\$ (1,711)</u>	<u>\$ 15,319</u>

Abbreviated Balance Sheet

Assets:		
Net Plant	\$ 167,636	\$ 574,317
Current assets	\$ 15,911	\$ 24,978
Liabilities:		
Current Liabilities	\$ 136,737	\$ 61,437
Meter deposits	\$ 68,542	\$ 92,229
Advances-in-aid	-	290,439
Contributions	-	19,373
Long term debt	45,922	25,039
Equity	<u>\$ (21,731)</u>	<u>\$ 32,747</u>
Total Capital	<u>\$ 24,191</u>	<u>\$ 459,827</u>

Cash Available for Debt Service on Proposed Debt

Depreciation	\$ 20,154
Net Income	<u>\$ 15,319</u>
Subtotal	<u>\$ 35,473</u>
less;	
Principal/Harris Trust note	\$ 5,424
Meter Deposit Refunds	\$ 7,853
Total Cash available for debt service on new debt	<u>\$ 22,196</u>
Debt Service for proposed debt of \$412,328.	<u>\$ 47,078</u>
Difference between Debt Service and Cash Flow	<u>\$ (24,882)</u>