

OPEN MEETING ITEM



0000034969

COMMISSIONERS
JEFF HATCH-MILLER - Chairman
WILLIAM A. MUNDELL
MARC SPITZER
MIKE GLEASON
KRISTIN K. MAYES

ORIGINAL



ARIZONA CORPORATION COMMISSION

2005 OCT 25 P 3:31

AZ CORP COMMISSION
DOCUMENT CONTROL

DATE: October 25, 2005
DOCKET NO: W-01412A-04-0736 et al.
W-01412A-04-0849
TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Teena Wolfe. The recommendation has been filed in the form of an Opinion and Order on:

VALLEY UTILITIES WATER COMPANY, INC.
(RATES/FINANCING)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and thirteen (13) copies of the exceptions with the Commission's Docket Control at the address listed below by 4:00 p.m. on or before:

NOVEMBER 3, 2005

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Open Meeting to be held on:

NOVEMBER 8 AND 9, 2005

For more information, you may contact Docket Control at (602)542-3477 or the Hearing Division at (602)542-4250. For information about the Open Meeting, contact the Executive Director's Office at (602) 542-3931.


BRIAN C. McNEIL
EXECUTIVE DIRECTOR

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 COMMISSIONERS

3 JEFF HATCH-MILLER, Chairman
4 WILLIAM A. MUNDELL
5 MARC SPITZER
6 MIKE GLEASON
7 KRISTIN K. MAYES

8 IN THE MATTER OF THE APPLICATION OF
9 VALLEY UTILITIES WATER COMPANY, INC.
10 FOR AN INCREASE IN ITS WATER RATES FOR
11 CUSTOMERS WITHIN MARICOPA COUNTY,
12 ARIZONA.

DOCKET NO. W-01412A-04-0736

9 IN THE MATTER OF THE APPLICATION OF
10 VALLEY UTILITIES WATER COMPANY, INC.
11 FOR AUTHORITY TO ISSUE PROMISSORY
12 NOTE(S) AND OTHER EVIDENCES OF
INDEBTEDNESS PAYABLE AT PERIODS OF
MORE THAN TWELVE MONTHS AFTER THE
DATE OF ISSUANCE.

DOCKET NO. W-01412A-04-0849

DECISION NO. _____

OPINION AND ORDER

13 DATE OF PRE-HEARING CONFERENCE: July 11, 2005
14 DATE OF HEARING: July 14, 2005
15 PLACE OF HEARING: Phoenix, Arizona
16 ADMINISTRATIVE LAW JUDGE: Teena Wolfe
17 APPEARANCES: Richard L. Sallquist, SALLQUIST,
18 DRUMMOND & O'CONNOR, on behalf of
19 Valley Utilities Water Company, Inc.; and
20 David Ronald, Staff Attorney, Legal Division,
21 on behalf of the Utilities Division of the Arizona
22 Corporation Commission.

22 **BY THE COMMISSION:**

23 On October 7, 2004, Valley Utilities Water Company, Inc. ("Valley", "Applicant" or
24 "Company") filed an application with the Arizona Corporation Commission ("Commission") for an
25 increase in its water rates for customers within Maricopa County, Arizona.

26 On November 5, 2005, the Commission's Utilities Division Staff ("Staff") issued a Letter of
27 Deficiency indicating that Valley's application had not met the sufficiency requirements.

28 On November 12, 2004, Staff filed a Letter of Sufficiency indicating that Valley's application

1 met the sufficiency requirements outlined in A.A.C. R14-2-103.

2 On November 26, 2004, Valley filed an application for approval for the issuance of
3 promissory note(s) and other evidences of indebtedness in the original amount of up to \$1,926,100.

4 On December 7, 2004, by Procedural Order, a hearing was set in the rate case for July 14,
5 2005.

6 Valley caused notice of its financing application to be published in the *Record Reporter* on
7 December 20, 2005.

8 By Procedural Order issued March 23, 2005, the rate application and financing application
9 matters were consolidated in accordance with the Company's request filed on March 17, 2005.

10 On April 1, 2005, an Affidavit of Mailing was filed indicating notice of the hearing was
11 provided to all customers by first class mail as ordered in the Commission's Procedural Order dated
12 December 7, 2004.

13 Intervention was granted to K. Robert Janis, TC Crownover, and James Shade.

14 A hearing was held as scheduled before a duly authorized Administrative Law Judge of the
15 Commission on July 14, 2005. Public comment was taken at the commencement of the hearing. The
16 Company and Staff appeared and presented evidence. Following the hearing, the parties filed closing
17 briefs and the consolidated matters were taken under advisement pending the submission of a
18 Recommended Opinion and Order to the Commission.

19 DISCUSSION

20 Valley is a Class C water utility that provided public utility water service to approximately
21 1,210 customers during the test year ended December 31, 2003.¹ The Company's current rates were
22 set by the Commission in Decision No. 62908 (September 18, 2000), using a test year ending
23 December 31, 1998. In the rate application, the Company proposed a two step rate increase and a 10
24 percent operating margin for each step. According to Valley, the Company has negative equity, so a
25 meaningful cost of capital cannot be determined. Under Step 1, a 10 percent operating margin would
26 require an increase of approximately 12.2 percent over the adjusted test year and annualized

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28 ¹ If the Company's requested surcharge mechanism to service proposed debt is approved, Valley would become a Class B utility (Tr. at 115).

1 revenues, or \$101,800. Step 2 would also include a 10 percent operating margin (\$403,000 increase),
 2 and an adjuster mechanism for recovery of arsenic treatment operating costs.² According to the
 3 application, during the Test Year ended December 31, 2003 ("TY"), the Company had an adjusted
 4 operating income of \$13,138 (Exhibit A-1, Schedule C-1 Step 1).

5 Rate Base

6 The Company's TY rate base as filed was (\$540,689) (Exhibit A-1, Application Schedule A-1
 7 Step 1). The Company requested a waiver of the reconstruction cost new less depreciation
 8 ("RCND") schedule filing requirement and requested that its original cost rate base ("OCRB") be
 9 used as its fair value rate base ("FVRB").

10 Staff made two adjustments to rate base, resulting in a net increase of \$885, for a FVRB of
 11 (\$539,804). The first adjustment reflects capitalization of an erroneously recorded expense and the
 12 second adjustment increased Cash Working Capital. (Exhibit S-2, Rogers Direct, p 9). The Company
 13 accepted Staff's proposed adjustments, but calculated a different Cash Working Capital amount,
 14 resulting in a slightly different rate base of (\$543,488) (Exhibit A-4, Bourassa Rejoinder p 5).

15 We agree with the adjustments made by Staff to the Company's rate base, and find that the
 16 Company's OCRB is (\$539,804). Because the Company did not file RCND schedules, its FVRB is
 17 the same as its OCRB.

18 Revenue and Operating Expense

19 Staff and the Company agree that TY revenues were \$827,565. The Company proposed TY
 20 expenses of \$814,427. Staff made a number of adjustments to TY expense, including: a reduction in
 21 lawn service costs to reflect only that portion attributable to the Company's offices, which are located
 22 within the shareholder's domicile; an increase in water testing expenses to reflect a normalized
 23 amount; a reduction in transportation expense to remove a non-arm's length transaction involving a
 24 vehicle leased from the shareholder and the inclusion of two years' registration fees; a reduction in
 25 miscellaneous expense to remove a non-recurring recruitment expense; a reduction in directors' fees
 26 to remove "catch up" and advances in fees; a reduction in miscellaneous expense to remove long

27 _____
 28 ² In its rebuttal testimony, the Company dropped its request for a two step increase, and instead proposed a surcharge
 mechanism for recovery of the arsenic treatment operating and maintenance costs (Exhibit A-3, Bourassa Rebuttal p 2).

1 distance personal telephone calls,³ costs to acquire a new sign, the cost of which Staff added to rate
2 base, gym membership expenses, and sponsorship in a high school fundraiser; and an increase in
3 depreciation expense, property tax expense, and income tax expense (Exhibit S-2, Rogers Direct, pp
4 11-18, and Schedule DRR-7).

5 The Company accepted all of Staff's expense adjustments (Exhibit A-3, Bourassa Rebuttal, p
6 6). Staff's adjusted TY operating expense is \$814,662, for a TY operating income of \$12,903. In its
7 rebuttal testimony, the Company dropped its request for a two step increase, and instead proposed a
8 surcharge mechanism for recovery of the arsenic treatment operating and maintenance costs (Exhibit
9 A-3, Bourassa Rebuttal, p 2).

10 Because the Company's adjusted FVRB is negative \$539,804, a rate of return calculation is
11 not meaningful. Staff recommended that the Commission authorize a 10 percent operating margin, or
12 \$957,511. This represents a \$129,946, or 15.70 percent, revenue increase from \$827,565 to
13 \$957,511. We agree that because the Company's FVRB is negative, it is appropriate to use an
14 operating margin to set fair and reasonable rates. We are, however, concerned that this Company
15 continues to operate the utility in such a way that although equity is not being invested, ratepayers are
16 required to generate cash sufficient to show an operating income.⁴ We agree with Staff's
17 recommendation, discussed below, to require the Company to implement a plan to improve its equity
18 position.

19 Rate Design

20 The Company's current rate design consists of customer charges that vary by meter size, with
21 no gallons included. All but the 3 inch meters for commercial construction have a two tier structure,
22 with a commodity rate of \$1.80 per 1,000 gallons up to 25,000 gallons, and \$2.20 per 1,000 gallons
23 greater than 25,000.

24 The Company's proposed rate design applies a uniform percentage increase to all monthly
25 minimums and changes from a two tier commodity rate to a three tier rate for all customer classes

26 _____
27 ³ The Company requested rate recovery of these personal telecommunications expenses in its application despite the fact
28 that the Commission specifically disallowed similar expenses in the Company's prior rate proceeding (*see* Decision No.
62908 p 5).

⁴ The Company's FVRB in its last rate case was negative \$292,898 (*see* Decision No. 62908 p 11).

1 with the exception of construction water, to assist in conservation. The breakover points graduate by
2 meter size, with the first tier rate of \$1.98, the second tier at \$2.42, and the third tier at \$2.662 per
3 1,000 gallons. According to the Company, customers using larger quantities of water will experience
4 a higher increase due to the three tier rate design.

5 Staff proposed an inverted tier rate structure that includes three tiers for residential 5/8 x 3/4-
6 inch meters and residential 3/4-inch meters, and two tiers for all others. With the residential meters,
7 the first tier breakover point is 3,000 gallons and the second tier breakover point is 10,000 gallons.
8 Other breakover points vary by meter size. The Company objected to Staff's recommendation,
9 stating that the residential first tier is a "lifeline or low income" rate and that, according to the
10 American Water Works Association ("AWWA") should only be offered to residential customers who
11 meet certain eligibility requirements; "should not be considered unless the local cost of water service
12 is high compared to other similar water utilities or where a significant percentage of residential
13 customers are believed to be unable to afford water service" and should not be used in areas where
14 there are water shortages (Exhibit A-2, Kozoman Rebuttal, pp 4-5). The Company speculates that
15 Staff's recommended rate design may lead existing 1-inch meter customers to demand a downsizing
16 of meter sizes, which the Company believes would cause revenue and O&M impacts, in addition to
17 destabilization of cash flows, and which the Company believes would require monitoring to prevent
18 what it terms "over-revving" of the smaller meters (Exhibit A-3 Prince Rebuttal, p 2). The Company
19 acknowledged that it has not performed a cost of service study and that it is not facing water supply
20 shortages, although it is in the Phoenix Active Management Area ("AMA").

21 Staff points out that the concerns asserted by Mr. Prince are also present with the Company's
22 proposed rate design (Exhibit S-3, Rogers Surrebuttal, p 4). Staff asserts that its recommended rate
23 design acknowledges water use patterns by meter size and in total to encourage efficient
24 consumption, and that the Commission has recently issued decisions that adopted Staff's
25 recommended rate design consisting of an inverted three tier rate design for residential 5/8-inch and
26 3/4-inch meter customers and an inverted two tier structure for all other meter sizes and customers.

27 We agree that Staff's recommended rate design will promote conservation by sending
28 appropriate price signals to all customers, and find that it also addresses the goals of efficient water

1 use, affordability, fairness, simplicity, and revenue stability. We will therefore adopt it.

2 Arsenic Removal/Financing Request

3 The U.S. Environmental Protection Agency ("EPA") has reduced the arsenic maximum
4 contaminant level ("MCL") in drinking water from 50 parts per billion ("ppb") to 10 ppb, with a
5 compliance date of January 23, 2006. The Company's six wells have arsenic concentrations between
6 7 and 13 ppb. The Company is seeking a loan from the Water Infrastructure Finance Authority of
7 Arizona ("WIFA") to purchase and construct water treatment facilities for arsenic removal. In
8 Decision No. 67669 (March 9, 2005), the Commission approved an Arsenic Impact Fee Tariff for the
9 Company to help pay for debt service and/or principal on the requested WIFA loan, with the hook-up
10 fees⁵ to be treated as contributions in aid of construction ("CIAC"), and to be refunded if they are not
11 used to pay for arsenic treatment facilities. The Company hired a consulting firm to conduct an
12 arsenic treatment study using the treatment model methods presented in the Arizona Department of
13 Environmental Quality's ("ADEQ") Arsenic Master Plan guidelines. A pilot study was conducted at
14 three of the Company's wells and a final study report was completed in May 2004. The study
15 recommended using absorption media treatment with a total treatment system cost of \$1,926,100 for
16 treatment of five of Valley's six wells. According to Staff's testimony, the Company evaluated other
17 options such as blending and drilling new wells or deepening existing wells, but due to the high
18 arsenic concentration and its fluctuation in the area, the Company concluded that treating the water
19 source was the only available solution. Staff concluded that the arsenic treatment facilities are
20 appropriate and the estimated capital costs and O&M costs are reasonable for purposes of the
21 financing request (Exhibit S-1, Scott Direct, p *ii*).

22 The terms of the proposed \$1,926,100 WIFA loan is 20 years, with a maximum interest rate
23 of prime plus 200 basis points and a debt service coverage ("DSC") of at least 1.2. Payment of the
24 loan begins six months after WIFA provides the monies to the Company, and monthly payments on
25 the loan include both principal and interest. Staff analyzed the requested financing and testified that
26 the Company's capital structure is composed of 100 percent negative equity, and if the financing is

27 _____
28 ⁵ The approved hook-up fee is \$1,100 for all new 5/8 x 3/4-inch service connections, graduated for larger meter sizes.

1 approved, the capital structure would be 6.3 percent short-term debt, 121.1 percent long-term debt,
2 and 27.3 percent negative equity. According to Staff, the pro forma effect on the Company's
3 financial ratios of obtaining the \$1,926,100 WIFA loan at an interest rate of 5.0 percent and
4 implementation of Staff's recommended rates is a Times Interest Earned Ratio ("TIER") of 1.58 and
5 a DSC of 1.86. Staff determined that an annual surcharge of approximately \$185,247 would be
6 necessary for the Company to maintain its pre-loan cash flow. Staff testified that the proposed loan
7 "exacerbates the Company's negative equity with a debt burden, an undesirable event" (Exhibit S-2,
8 Rogers Direct, p 26). However, Staff concluded that there are no other known options to finance the
9 purchase/construction of the arsenic removal equipment required to comply with the EPA MCL.
10 Staff believes that a mitigating factor is that the pro forma DSC and TIER indicate that the Company
11 would have adequate earnings and cash flow to meet all obligations. Staff concluded that the
12 purchase and/or construction of the arsenic removal equipment is necessary for the Company to
13 comply with the federal rule; and that its recommended rates, which are intended to provide an
14 operating margin that will allow the Company to attain a positive equity position, are insufficient to
15 meet additional debt service obligations of the proposed WIFA debt.

16 In regard to the Company's financing request, Staff recommended:

- 17 • that the loan be approved on the terms and conditions described in the application,
18 with the understanding that the Commission will subsequently consider an arsenic
19 removal surcharge to enable the Company to meet its principal and interest obligations
20 on the WIFA loan, and the incremental income taxes on the surcharge;
- 21 • that the Company be authorized to execute any documents necessary to effectuate the
22 authorization granted;
- 23 • that the Company be ordered to provide to the Utilities Division Compliance Section
24 copies of all executed financing documents within 60 days after the loan agreement is
25 signed; and
- 26 • that the Company be ordered not to use any portion of the loan to pay for incurred
27 operating or other expenses.

28 In relation to its recommendation regarding future Commission consideration of an arsenic

1 removal surcharge, Staff recommended that the Company be required to:

- 2 • file in Docket Control an arsenic removal surcharge tariff application that will allow
3 the Company to meet its principal and interest obligations on the proposed WIFA
4 loan and income taxes on the surcharge;
- 5 • follow the same methodology set forth in Table A to the Staff testimony, to calculate
6 the incremental revenue needed to meet the interest, principal and incremental income
7 tax obligations on the WIFA loan, using actual loan amounts and use the result to
8 develop its arsenic removal surcharge tariff application, which would also include the
9 required increase in revenue calculation; and
- 10 • file with Docket Control copies of its calculation of revenue requirement for principal
11 and interest obligations on the WIFA loan and incremental income taxes on the
12 surcharge, within 60 days after the loan agreement is signed by both WIFA and the
13 Company.

14 These Staff recommendations are reasonable and will be adopted.

15 Funds Set Aside Pursuant to Decision No. 62908

16 Decision No. 62908 set rates for the Company and approved a WIFA loan in the amount of
17 \$452,080. It also ordered the Company to “set aside the amount of funds equivalent to the annual
18 debt service requirements of the WIFA loan and set aside one-twelfth on a monthly basis when the
19 amount of the debt service requirement becomes known to the Company. Until such time as that
20 amount is known, the Company shall set aside \$6.35 per bill per month in a separate, interest bearing
21 account to be used solely for the purpose of servicing the WIFA financing.” It further ordered the
22 Company to “submit information detailing the amount of debt service requirement on the WIFA loan
23 to the Utilities Division Director within 60 days of a Decision in this matter (Decision No. 62908, p
24 15). The Company complied with the filing requirement on January 30, 2003, after several
25 extensions had been granted by the Commission, but never filed copies of executed documents
26 indicating that the Company ever obtained the approved financing. According to a compliance filing
27 in that docket, the Company has been setting aside the required monthly amount in a segregated,
28 interest-bearing account to be used solely for the purpose of servicing the WIFA financing (Letter

1 from counsel for Valley to Patrick Williams dated January 4, 2002). The Company has not incurred
2 the WIFA debt approved in Decision No. 62908, but has collected funds intended to pay that debt.
3 The existing balance of the collected debt-service funds must either be refunded or applied to WIFA
4 debt. Because the Company is again requesting WIFA financing, and is requesting imposition of a
5 surcharge to pay the debt service, it would be reasonable and efficient to apply the existing balance of
6 the collected funds to service the new WIFA debt. Under the circumstances, it is reasonable to cancel
7 the prior WIFA financing authority, and require the Company to use the collected fund balance to
8 service the arsenic remediation-related long-term debt authorized herein. We will therefore require
9 the Company to file, in addition to the arsenic removal surcharge tariff application recommended by
10 Staff, a report detailing the balance of the funds collected for debt service as authorized by Decision
11 No. 62908, and the extent to which the application of the collected funds to debt service will offset
12 the amount of, or the need for, an arsenic removal surcharge.

13 AOMRSM Request

14 The Company proposed an Arsenic Operating and Maintenance Recovery Surcharge
15 Mechanism ("AOMRSM"). The Company estimates that the arsenic treatment costs will total
16 \$216,600 for the first full year of operation. Under the Company's proposal, the cost per 1,000
17 gallons would be determined by dividing the actual arsenic O&M costs for the year by the annual
18 gallons sold, and a balancing account would be maintained. Each year, the Company would provide
19 Staff a detailed calculation of the surcharge as well as provide an accounting of the amount collected
20 during the year. According to the Company's estimations, the AOMSM charge per 1,000 gallons
21 would be \$0.84, and the impact on an average 5/8-inch customer bill would be \$7.77, for a combined
22 estimated increase of 42.94 percent over present rates. The Company estimates that the total impact
23 of the ARSM and the AOMRSM on such a customer's monthly bill would be \$14.23, for a combined
24 increase of 67.55 percent (Exhibit A-3, Bourassa Rebuttal, p 14). Based on its estimates, the
25 Company claims that if both surcharges are not adopted, it will experience net losses (*see* Exhibit A-
26 4, Bourassa Rejoinder, Exhibit 3).

27 Staff recommended that the Company's proposed AOMRSM be disallowed and that the
28 Company file a rate case application after a period of time, so that actual operation and maintenance

1 costs can be determined and the appropriate rates established. Staff testified that while the costs
2 proposed by the Company may be a reasonable estimate, they are projected costs, and to authorize
3 estimated costs to be recovered at some future time, before they are known and measurable, would
4 not allow Staff the opportunity to ascertain with any degree of confidence, the reasonableness of the
5 charges and whether they are accounted for correctly (Exhibit S-3, Rogers Surrebuttal, p 6). Staff
6 further testified that the Commission has consistently found that operation and maintenance costs
7 associated with arsenic removal should be segregated and tracked for a period of time, and that a rate
8 case should be filed once the actual costs become known and measurable.

9 We agree with Staff for several reasons. First, it would not be reasonable to require the
10 Company's customers to pay a surcharge for O&M costs when the costs have only been estimated,
11 and have not been subject to audit in order to determine their reasonableness and whether they are
12 accounted for correctly. This problem is exemplified by the fact that the calculations presented in the
13 Company's testimony overstate the effect of the Company's own estimates due to an apparent
14 computation error involving the double-counting of interest expense. Valley presented calculations
15 estimating net losses it will incur if its requested surcharges are not granted. The estimation
16 calculations subtracted interest expense twice, which resulted in an understatement of cash flows to
17 the tune of \$94,988 (*see* Exhibit A-4, Bourassa Rejoinder, Exhibit 3). Correcting this error on the
18 Company's exhibit would result in estimated positive cash flows of \$55,150, instead of the
19 Company's negative \$39,838 estimated net operating loss.

20 Second, Decision No. 67669 has already approved a \$1,100 Arsenic Impact Fee Tariff for the
21 Company to help pay for debt service and/or principal on the requested WIFA loan.

22 Third, this Decision approves the concept of a surcharge to pay the debt service on the arsenic
23 remediation-related WIFA loan once the amount of the debt service is determined and orders the
24 Company to file an application for that surcharge. Approval of the AOMRSM in addition to the
25 WIFA debt-service surcharge would therefore result in the Company's existing customers paying two
26 surcharges, with new customers paying a hook-up fee in addition to the two surcharges.⁶

27 _____
28 ⁶ As an alternative to Staff's recommendation to deny the AOMRSM, Staff stated that if the Company were to fund the
needed arsenic remediation plant with equity contributions instead of debt, Staff could agree in concept to permitting a

1 Fourth, we are approving rates herein that are based on an operating margin instead of a return
2 on equity, in order to prevent operating losses, as discussed at page 4 above, due to the Company's
3 ongoing negative equity position. As discussed below, we are requiring the Company to develop,
4 submit and implement a plan to increase its equity position, because the Company has been operated
5 in such a way that its negative equity position has continued to deteriorate, despite the fact that over a
6 period of years, this Commission has authorized returns that provided the Company with an
7 opportunity to increase its equity position (*see* Tr. p 112).

8 For these reasons, we will not approve the Company's proposed AOMRSM, but will instead
9 consider actual operation and maintenance costs in a future rate filing, where rates can be established
10 based on known and measurable actual costs.

11 Shareholder/Company Transactions

12 Staff recommended that the Company be ordered to make all reasonable efforts to institute
13 operating policies that would remove any and all transactions between the Company and its owners
14 that are not arm's length transactions. Based on the evidence presented in this proceeding, this is a
15 reasonable recommendation, and it will be adopted. We will expect Staff to carefully scrutinize the
16 Company's books in the Company's next rate case, and bring to the Commission's attention any
17 instances of transactions between the Company and its shareholder that are not arm's length,
18 including but not limited to the payment of personal expenses from water utility revenues, along with
19 recommendations for appropriate Commission action.

20 Equity Position

21 Staff recommended that the Company be required to institute a plan that would produce a
22 positive equity position by December 31, 2010, such plan to be filed with Docket Control within 90
23 days from the date of the Commission's Decision. The Company's FVRB in its last rate case was
24 negative \$292,898 (*see* Decision No. 62908, p 11), and in this case, has deteriorated further, to
25 negative \$539,804. As stated at page 4 above, we are concerned that this Company continues to
26 operate the utility in such a way that although equity is not being invested, ratepayers are required to

27
28 surcharge to collect the Company's first year of arsenic-related O&M costs (Tr. at 91). However, the Company made no
indication at the hearing that it planned to make such an equity infusion.

1 generate cash sufficient to show an operating income. Staff's concerns are legitimate, and its
 2 recommendation provides a reasonable means of ameliorating the problem. We will therefore adopt
 3 Staff's recommendation. We will also direct Staff to bring to the attention of the Commission in the
 4 Company's next rate case all evidence of any inappropriate lease arrangements between the
 5 shareholder and the Company, or any other inappropriate practices that contribute to the deterioration
 6 rather than to the building of the Company's equity. The Company should be on notice that
 7 questionable expenses will be subject to disallowance in future rate proceedings.

8 Additional Staff Recommendations

9 Staff also recommended that the Company's proposed service line and meter installation
 10 charges be adopted, and that the Company use the depreciation rates in Exhibit MSJ-A, Table I-1,
 11 found in Hearing Exhibit S-1. Staff also recommended that the Company be required to file a
 12 curtailment tariff conforming to the sample tariff in Exhibit MSJ-A, Attachment K-1, found in
 13 Hearing Exhibit S-1, within 45 days after the effective date of this Decision with Docket Control, as a
 14 compliance item for Staff review and certification. These recommendations are reasonable and will
 15 be adopted.

16 * * * * *

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

19 FINDINGS OF FACT

20 1. Valley is an Arizona Corporation that was granted a Certificate of Convenience and
 21 Necessity in Decision No. 54274, dated December 20, 1984, to provide service to an area located
 22 approximately five miles west of Glendale, Arizona in Maricopa County. Valley provides water
 23 utility service to approximately 1,210 customers in Maricopa County, Arizona.

24 2. On October 7, 2004, Valley Utilities filed an application for a rate increase for its
 25 water customers comprised of a two-step phase-in rate increase based on a test year ("TY") ending
 26 December 31, 2003. The rate application requested an operating margin of 10 percent in order to
 27 have adequate debt service coverages for a loan from WIFA to fund improvements related to arsenic
 28 removal capital improvements.

1 3. On November 5, 2004, Staff filed a letter informing the Company that its application
2 had not met the sufficiency requirements outlined in A.A.C. R14-2-103.

3 4. Also on November 5, 2005, Valley filed a compliance status report from ADEQ.

4 5. On November 12, 2004, Staff filed a Letter of Sufficiency.

5 6. On November 26, 2004, Valley Utilities filed an application for authority to issue
6 promissory notes and evidences of indebtedness of up to \$1,926,100 to finance the purchase or
7 construction of a plant and the equipment necessary to treat and remove arsenic from its water
8 supply.

9 7. On December 7, 2004, by Procedural Order, a hearing was scheduled on Valley's rate
10 application.

11 8. On January 4, 2005, Valley docketed an Affidavit of Publication certifying that it
12 caused notice of its financing application to be published in the *Record Reporter* on December 20,
13 2005.

14 9. On March 17, 2005, the Company filed a Motion to Consolidate the financing
15 application with the rate application for purposes of hearing, which was granted by Procedural Order
16 issued March 23, 2005.

17 10. On April 1, 2005, pursuant to the Commission's Procedural Order of December 7,
18 2004, the Company filed an Affidavit of Mailing indicating that notice of the rate application and
19 hearing was mailed to all customers of record in the Company's February billings.

20 11. Public comment was filed on April 12, 2005 and July 14, 2005, objecting to the
21 Company's proposed rate increase.

22 12. On May 2, 2005, TC Crownover, James Shade and K. Robert Janis filed requests to
23 intervene.

24 13. On May 2, 2005, William Clark, on behalf of Litchfield Vista View III Homeowners
25 Association, filed a request to intervene.

26 14. On May 10, 2005, by Procedural Order, K. Robert Janis, TC Crownover, James Shade
27 and William Clark were granted intervention.

28 15. On May 11, 2005, Staff filed its Direct Testimony.

1 16. On May 13, 2005, Valley filed Objections to the Procedural Order Regarding
2 Intervention. Valley did not object to the intervention of K. Robert Janis, but stated that the
3 intervention requests of TC Crownover, James Shade and William Clark were untimely. Valley
4 further objected to Mr. Clark's intervention on the grounds that he is not a customer of Valley and
5 therefore has no interest in these proceedings. Mr. Clark did not appear at the hearing to respond to
6 the Company's objections. The May 10, 2005 Procedural Order was therefore amended at the
7 hearing to state that Mr. Clark's intervention request is denied due to his failure to show that he
8 would be directly and substantially affected by the outcome of this proceeding.

9 17. The Company and Staff docketed pre-filed testimony in accordance with the
10 requirements of the rate case Procedural Order.

11 18. The hearing was held as scheduled on July 14, 2005. Mr. Charles Prokow, Ms.
12 Almira Martinez, and Mr. Michael Fent appeared and provided public comment for the record in
13 opposition to the level of rate increase requested by the Company. The Company and Staff appeared
14 and presented testimony and cross-examined witnesses. Intervenor Ms. TC Crownover appeared on
15 her own behalf and provided public comment, and also filed written public comment in the docket on
16 the date of the hearing.⁷

17 19. On August 25, 2005, the Company and Staff filed Closing Briefs, and the consolidated
18 matters were taken under advisement.

19 20. The rates and charges for Valley at present, as proposed in the rate application, and as
20 recommended by Staff are as follows:

21 ...

22 ...

23 ...

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26 ...

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28 ⁷ It became known at the hearing that Ms. Crownover herself is not a customer of the Company.

	<u>Present</u> <u>Rates</u>	<u>Co.</u> <u>Phase One</u>	<u>Co.</u> <u>Phase Two</u>	<u>Staff</u>	
1					
2					
3	<u>MONTHLY USAGE CHARGE:*</u>				
4	5/8" x 3/4" Meter	\$ 9.60	\$ 10.37	\$ 14.16	\$ 11.24
5	3/4" Meter	14.50	15.66	21.38	16.87
6	1" Meter	24.00	25.92	35.38	28.10
7	1 1/2" Meter	48.00	51.85	70.78	56.21
8	2" Meter	77.00	83.18	113.54	89.94
9	3" Meter	144.00	155.55	212.33	179.87
10	4" Meter	240.00	259.25	353.88	281.05
11	6" Meter	480.00	518.50	707.75	562.10
12	Construction Water	144.00		212.33	179.87
13	<u>COMMODITY CHARGES:*</u>				
14	<u>All Meters</u>				
15	1,000 to 25,000 Gallons	\$ 1.80			
16	25,001 gallons and over	2.20			
17	<u>Construction Water</u>	2.60	2.86	4.25	\$ 3.02
18	<u>5/8" Meter</u>				
19	1 - 8,000 gallons		1.98	2.94	
20	8,001 - 12,000 gallons		2.42	3.60	
21	12,001 gallons and over		2.662	3.9580	
22	<u>3/4" Meter</u>				
23	1 - 12,000 gallons		1.98	2.94	
24	12,001 to 18,000 gallons		2.42	3.60	
25	18,001 gallons and over		2.662	3.9580	
26	<u>1" Meter</u>				
27	1 to 20,000 gallons		1.98	2.94	
28	20,001 to 30,000 gallons		2.42	3.60	
29	30,001 gallons and over		2.662	3.9580	
30	<u>1 1/2" Meter</u>				
31	1 - 40,000 gallons		1.98	2.94	
32	40,001 to 60,800 gallons		2.42	3.60	
33	60,801 gallons and over		2.662	3.9580	
34	<u>2" Meter</u>				
35	1 - 64,000 gallons		1.98	2.94	
36	64,001 to 96,000 gallons		2.42	3.60	
37	96,001 gallons and over		2.662	3.9580	

1	<u>3" Meter</u>		
2	1 to 128,000 gallons	\$ 1.98	\$ 2.94
	128,001 to 192,000 gallons	2.42	3.60
3	192,001 gallons and over	2.662	3.9580
4	<u>4" Meter</u>		
5	1 to 200,000 gallons	1.98	2.94
6	200,001 to 300,000 gallons	2.42	3.60
	300,001 gallons and over	2.662	3.9580
7	<u>6" Meter</u>		
8	1 to 400,000 gallons	1.98	2.94
9	400,001 to 600,000 gallons	2.42	3.60
	600,001 gallons and over	2.662	3.9580
10	<u>5/8" x 3/4" Meter - Residential</u>		
	1 to 3,000 gallons		\$ 1.50
11	3,001 to 10,000 gallons		2.31
12	10,001 gallons and over		2.53
13	<u>5/8" x 3/4" Meter - Commercial</u>		
	1 to 18,000 gallons		2.31
14	18,001 gallons and over		2.58
15	<u>3/4" Meter - Residential</u>		
	1 to 3,000 gallons		1.50
16	3,001 to 10,000 gallons		2.31
17	10,001 gallons and over		2.53
18	<u>3/4" Meter - Commercial</u>		
	1 to 18,000 gallons		2.31
19	18,001 gallons and over		2.58
20	<u>1" Meter</u>		
	1 to 50,359 gallons		2.31
21	50,360 gallons and over		2.53
22	<u>1 1/2" Meter</u>		
23	1 to 126,054 gallons		2.31
24	126,055 gallons and over		2.53
25	<u>2" Meter</u>		
	1 to 151,256 gallons		2.31
26	151,257 gallons and over		2.53
27	...		
28	...		

3" Meter

1 to 403,274 gallons	\$ 2.31
403,275 gallons and over	2.53

4" Meter

1 to 453,722 gallons	2.31
453,723 gallons and over	2.53

6" Meter

1 to 1,260,313 gallons	2.31
1,260,314 gallons and over	2.53

*In addition to the collection of regular rates, the utility will collect from its customers a proportionate share of any privilege, sales, use and franchise tax per Commission Rule R14-2-409.D.5.

SERVICE LINE AND METER INSTALLATION CHARGES:**
(Refundable pursuant to A.A.C. R14-2-405)

	Present Meter and Service Line Installation Charge	Proposed Service Line Inst. Charge Co.	Proposed Meter Inst. Charge Co.	Total Proposed Charge Co.	Total Proposed Inst. Charge Staff
5/8 x 3/4 Inch	\$ 455.00	\$385.00	135.00	\$ 520.00	\$ 520.00
3/4 Inch	515.00	385.00	215.00	600.00	600.00
1 Inch	590.00	435.00	255.00	690.00	690.00
1 1/2 Inch	820.00	470.00	465.00	935.00	935.00
2 Inch/Turbine	1,380.00	630.00	965.00	1,595.00	1,595.00
2 Inch/Compound	2,010.00	630.00	1,690.00	2,320.00	2,320.00
3 Inch/Turbine	1,935.00	805.00	1,470.00	2,275.00	2,275.00
3 Inch/Compound	2,650.00	845.00	2,265.00	3,520.00	3,520.00
4 Inch/Turbine	3,030.00	1,170.00	2,350.00	3,520.00	3,520.00
4 Inch/Compound	3,835.00	1,230.00	3,245.00	4,475.00	4,475.00
6 Inch/Turbine	3,535.00	1,730.00	4,545.00	6,275.00	6,275.00
6 Inch/Compound	7,130.00	1,770.00	6,280.00	8,050.00	8,050.00
8 Inch	At Cost	At Cost	At Cost	At Cost	At Cost
10 Inch	At Cost	At Cost	At Cost	At Cost	At Cost
12 Inch	At Cost	At Cost	At Cost	At Cost	At Cost

** All advances and/or contributions are to include labor, materials, overheads, and applicable taxes, including gross-up taxes for income taxes, if applicable. As meters and service lines are now taxable income for income purposes, the Company shall collect income taxes on the meter and service line charges. Any tax collected will be refunded each year that the meter deposit is refunded.

...
...
...

<u>SERVICE CHARGES:</u>	<u>Present Rates</u>	<u>Proposed Rates Company</u>	<u>Staff</u>
Establishment	\$ 30.00	\$ 30.00	\$ 30.00
Establishment (After Hours)	45.00	45.00	45.00
Reconnection (Delinquent) (b)	40.00	40.00	40.00
Reconnection (Delinquent and After Hours) (b)	\$ 40.00	\$ 40.00	\$ 40.00
Meter Test	30.00	30.00	30.00
Deposit Requirement	(a)	(a)	(a)
Deposit Interest	6%	6%	6%
Reestablishment (Within 12 Months)	(b)	(b)	(b)
Reestablishment (After Hours)	(b)	(b)	(b)
NSF Check (per Rule R14-2-409.F)	25.00	25.00	25.00
Deferred Payment, Per Month	1.50%	1.50%	1.50%
Meter Reread (per Rule R14-2-408.C)	10.00	10.00	10.00
Charge of Moving Customer Meter – Customer Requested	Cost	Cost	Cost
After hours service charge	25.00	25.00	25.00

(a) Residential – two times the average bill. Non-Residential – two and one-half times the average bill.

(b) Per Rule R14-2-403.D.

21. Valley's present rates and charges produced adjusted TY operating revenues of \$827,565 and adjusted TY operating expenses of \$814,662, for a TY operating income of \$12,903.

22. The Company's OCRB is (\$539,804). The Company did not file RCND schedules. The Company's FVRB is therefore determined to be (\$539,804).

23. Because the Company's adjusted FVRB is negative \$539,804, a rate of return calculation is not meaningful. Based on the unique circumstances of this case, it is appropriate to use an operating margin to set fair and reasonable rates, and to allow a 10 percent operating margin, for revenues of \$957,511. This represents a \$129,946, or 15.70 percent, revenue increase from \$827,565 to \$957,511. In the Company's next rate filing, if the Company again requests use of an operating margin in lieu of a rate of return calculation, consideration will be given to the strength of the Company's efforts to improve its equity position.

24. Average and median usage during the TY for the Company's 593 3/4-inch meter

1 residential customers were 10,134 and 7,500 gallons per month, respectively; and average and
2 median usage during the TY for the Company's 256 5/8 x 3/4-inch meter residential customers were
3 9,251 and 6,500 gallons per month, respectively.

4 25. The rate schedule adopted herein will increase the average residential 5/8 x 3/4-inch
5 meter customer's monthly bill by \$3.93, from \$30.18 to \$34.11, or 14.97 percent, and the median 5/8
6 x 3/4-inch meter customer's monthly bill by \$2.53, from \$23.83 to \$26.36, or 11.86 percent. The
7 average residential 3/4-inch meter customer's monthly bill will increase by \$5.14, from \$37.88 to
8 \$43.02, or 15.69 percent, and the median residential 3/4-inch meter customer's monthly bill will
9 increase by \$3.76, from \$31.76 to \$35.52, or 13.45 percent.

10 26. The Company proposes three-tier rates for all customer classes with the exception of
11 construction water, and disagrees with Staff's rate design, which provides three-tiers only for
12 residential customers and two tiers for all other customers. The Company believes that Staff's
13 proposed first-tier rates are equivalent to a "lifeline" rate, which it asserts should only be offered to
14 residential customers who meet certain eligibility requirements. The Company speculates that Staff's
15 recommended rate design may lead existing 1-inch meter customers to demand a downsizing of
16 meter sizes, leading to revenue and O&M impacts and destabilization of cash flows. However, no
17 cost of service study was performed, and Staff testified that the Company's concerns regarding
18 possible meter downsizing may also exist with the Company's recommendation.

19 27. Staff's recommended rate design acknowledges water use patterns by meter size and
20 in total to encourage efficient consumption. The inverted three tier rate design for residential 5/8-
21 inch and 3/4-inch meter customers and an inverted two tier structure for all other meter sizes and
22 customers as proposed by Staff is reasonable and will be adopted because it will promote
23 conservation by sending appropriate price signals to all customers; and because it addresses the goals
24 of efficient water use, affordability, fairness, simplicity, and revenue stability.

25 28. Valley's system consists of six wells, five storage tanks, four booster stations, and a
26 distribution system, with a source capacity of 1,060 gallons per minute ("GPM") and storage capacity
27 of 1,060,000 gallons. According to Staff, the existing system has adequate production and storage
28 capacity to serve the present customer base and reasonable growth.

1 29. Staff reviewed the arsenic treatment facilities Valley proposed in the financing
2 application. Based on its analysis, Staff's engineering section concluded that the proposed arsenic
3 treatment facilities to be financed are appropriate, and recommended that the Company's estimated
4 capital costs and O&M costs be used for purposes of processing the financing request.

5 30. Under the circumstances of this case, it is reasonable to approve the Company's
6 financing request on the terms and conditions described in the application, with the proceeds to be
7 used solely for capital expenditures, and not operating or other expenses, and to require the Company
8 to file, as recommended by Staff, an arsenic removal surcharge tariff application for subsequent
9 approval of a surcharge that will allow Valley to meet its principal and interest obligations on the
10 amount of the WIFA loan and income taxes on the surcharges.

11 31. For the reasons described herein, it is not in the public interest to approve in this
12 Decision the Company's request for a surcharge to service the financing for which authority is
13 requested in this proceeding.

14 32. The debt authority granted in Decision No. 62908 was never utilized and should be
15 cancelled. It is reasonable to require that the funds the Company has collected for the sole purpose of
16 servicing the WIFA debt approved in Decision No. 62908 be applied to service the WIFA debt for
17 which authority is requested in this proceeding.

18 33. The Company should be required to file with Docket Control, within 30 days, a report
19 that provides detailed information regarding the balance of the funds the Company has collected for
20 the sole purpose of servicing the WIFA debt approved in Decision No. 62908, which debt was never
21 issued. The report should also include an analysis of the extent to which the application of the
22 collected funds to service the debt approved in this proceeding will offset the amount of, or the need
23 for, a surcharge to service the WIFA loan for arsenic removal capital projects.

24 34. In relation to the WIFA financing approved herein, it is reasonable to require the
25 Company to follow the methodology set forth in Table A-DRR attached to Hearing Exhibit S-2, to
26 calculate the incremental revenue needed to meet the interest, principal and incremental income tax
27 obligations on the WIFA loan, using actual loan amounts and use the result to develop its arsenic
28 removal surcharge tariff application, which would also include the required increase in revenue

1 calculation. The Company shall also include in its revenue increase calculation the offsets provided
2 by the application of the previously-collected funds pursuant to Decision No. 62908 to service the
3 debt, and the offsets provided by hook-up fees collected pursuant to Decision No. 67669 (March 9,
4 2005), which approved an Arsenic Impact Fee Tariff for the Company to help pay for debt service
5 and/or principal on the requested WIFA loan; and shall file copies of its calculation of revenue
6 requirement for principal and interest obligations on the WIFA loan and incremental income taxes on
7 the surcharge, within 60 days after the loan agreement is signed by both WIFA and the Company.

8 35. Based on the evidence in this proceeding, it is reasonable to require the Company to
9 make all reasonable efforts to institute operating policies to remove any and all transactions between
10 the Company and its owners that are not arm's length transactions. It is also reasonable to require
11 Staff to carefully scrutinize the Company's books in the Company's next rate case, and bring to the
12 Commission's attention any instances of transactions between the Company and its shareholder that
13 are not arm's length, including but not limited to improper lease arrangements and payment of
14 personal expenses, along with recommendations for appropriate Commission action.

15 36. It is reasonable to require the Company to develop and institute a plan that would
16 produce a positive equity position by December 31, 2010, and to file a copy of the plan as a
17 compliance item in this docket within 90 days. It is also reasonable to require Staff to bring to the
18 attention of the Commission in the Company's next rate case all evidence of any inappropriate lease
19 arrangements between the shareholder and the Company, or any other inappropriate practices, that
20 contribute to the deterioration rather than to the building of the Company's equity.

21 37. It is not in the public interest to grant the Company's proposed AOMRSM.

22 38. It is reasonable to require the Company to file a curtailment tariff as recommended by
23 Staff within 45 days with Docket Control, as a compliance item for Staff review and certification.

24 39. The Company's proposed service line and meter installation charges are reasonable
25 and should be adopted.

26 40. Staff testified that the Company has no outstanding compliance issues with the
27 Commission.

28 41. Staff testified that Valley's TY water loss is 1.96 percent, within acceptable limits.

ORDER

IT IS THEREFORE ORDERED that Valley Utilities Water Company Inc. shall file with the Commission's Docket Control Center, on or before November 30, 2005, the following schedule of rates and charges:

MONTHLY USAGE CHARGE:

5/8" x 3/4" Meter	\$ 11.24
3/4" Meter	16.87
1" Meter	28.10
1 1/2" Meter	56.21
2" Meter	89.94
3" Meter	179.87
4" Meter	281.05
6" Meter	562.10
Construction Water	179.87

COMMODITY CHARGES:*

<u>Construction Water</u>	3.02
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5/8" x 3/4" Residential Meter

1 to 3,000 gallons	1.50
3,001 to 10,000 gallons	2.31
10,001 gallons and over	2.53

5/8" x 3/4" Meter - Commercial

1 to 18,000 gallons	2.31
18,001 gallons and over	2.58

3/4" Meter - Residential

1 to 3,000 gallons	1.50
3,001 to 10,000 gallons	2.31
10,001 gallons and over	2.53

3/4" Meter - Commercial

1 to 18,000 gallons	2.31
18,001 gallons and over	2.58

1" Meter

1 to 50,359 gallons	2.31
50,360 gallons and over	2.53

1 1/2" Meter

1 to 126,054 gallons	2.31
126,055 gallons and over	2.53

1	<u>2" Meter</u>	
2	1 to 151,256 gallons	\$ 2.31
	151,257 gallons and over	2.53
3		
	<u>3" Meter</u>	
4	1 to 403,274 gallons	2.31
5	403,275 gallons and over	2.53
6		
	<u>4" Meter</u>	
7	1 to 453,722 gallons	2.31
	453,723 gallons and over	2.53
8		
	<u>6" Meter</u>	
9	1 to 1,260,313 gallons	2.31
	1,260,314 gallons and over	2.53

10 *In addition to the collection of regular rates, the utility will collect from its customers a
 11 proportionate share of any privilege, sales, use and franchise tax per Commission Rule R14-2-
 12 409.D.5.

13 SERVICE LINE AND METER INSTALLATION CHARGES: **
 14 (Refundable pursuant to A.A.C. R14-2-405)

	Service Line Inst. <u>Charge</u>	Meter Inst. <u>Charge</u>	Total Inst. <u>Charge</u>
15	5/8 x 3/4 Inch	\$ 385.00	\$ 520.00
16	3/4 Inch	385.00	600.00
17	1 Inch	435.00	690.00
	1 1/2 Inch	470.00	935.00
18	2 Inch/Turbine	630.00	1,595.00
	2 Inch/Compound	630.00	2,320.00
19	3 Inch/Turbine	805.00	2,275.00
	3 Inch/Compound	845.00	3,520.00
20	4 Inch/Turbine	1,170.00	3,520.00
	4 Inch/Compound	1,230.00	4,475.00
21	6 Inch/Turbine	1,730.00	6,275.00
22	6 Inch/Compound	1,770.00	8,050.00
	8 Inch	At Cost	At Cost
23	10 Inch	At Cost	At Cost
24	12 Inch	At Cost	At Cost

25 ** All advances and/or contributions are to include labor, materials, overheads, and applicable taxes,
 26 including gross-up taxes for income taxes, if applicable. As meters and service lines are now taxable
 27 income for income purposes, the Company shall collect income taxes on the meter and service line
 28 charges. Any tax collected will be refunded each year that the meter deposit is refunded.

SERVICE CHARGES:

Establishment	\$ 30.00
Establishment (After Hours)	45.00
Reconnection (Delinquent) (b)	40.00
Reconnection (Delinquent and After Hours) (b)	40.00
Meter Test (If Correct)	30.00
Deposit Requirement	(a)
Deposit Interest	6%
Reestablishment (Within 12 Months)	(b)
Reestablishment (After Hours)	(b)
NSF Check (per Rule R14-2-409.F)	25.00
Deferred Payment, Per Month	1.50%
Meter Reread (per Rule R14-2-408.C)	10.00
Charge of Moving Customer Meter – Customer Requested	Cost
After hours service charge	25.00

- (a) Residential – two times the average bill.
Non-Residential - two and one-half times the average bill.
- (b) Per Rule R14-2-403.D.

Monthly Service Charge for Fire Sprinkler: ***

*** 1% of Monthly Minimum for a Comparable Size Meter Connection, but no less than \$5.00 per month. The Service Charge for Fire Sprinklers is only applicable for service lines separate and distinct for the primary water service line.

IT IS FURTHER ORDERED that the above rates and charges shall be effective for all service provided on and after December 1, 2005.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall notify its customers of the revised rates and charges authorized herein, and their effective date, in a form acceptable to the Commission's Utilities Division Staff, by means of an insert in its next regularly scheduled billing.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file with the Commission's Docket Control a copy of the notice it sends to its customers within 60 days of the effective date of this Decision.

1 IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc.'s request for
2 approval of the WIFA loan in the amount of \$1,926,100 is hereby approved.

3 IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. is hereby authorized
4 to engage in any transactions and to execute any documents necessary to effectuate the authorization
5 granted hereinabove.

6 IT IS FURTHER ORDERED that such authority is expressly contingent upon Valley Utilities
7 Water Company, Inc.'s use of the proceeds for the purposes set forth in its application.

8
9 IT IS FURTHER ORDERED that approval of the financing set forth hereinabove does not
10 constitute or imply approval or disapproval by the Commission of any particular expenditure of the
11 proceeds derived thereby for purposes of establishing just and reasonable rates.

12 IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file copies of all
13 executed financing documents setting forth the terms of the financing, within 30 days of the obtaining
14 such financing.

15 IT IS FURTHER ORDERED that the financing authority granted to Valley Utilities Water
16 Company, Inc. in Decision No. 62908 but which was never utilized, is hereby cancelled.

17 IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. file with Docket
18 Control, within 30 days of this Decision, a report that provides detailed information regarding the
19 balance of the funds the Company has collected for the sole purpose of servicing the WIFA debt
20 approved in Decision No. 62908, which debt was never issued. The report shall also include an
21 analysis of the extent to which application of the collected funds to service the debt approved in this
22 proceeding will offset the amount of, or the need for, a surcharge to service the financing approved
23 herein.

24 IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file with Docket
25 Control an application for approval of an arsenic removal surcharge tariff if a surcharge is necessary
26 to allow Valley Utilities Water Company, Inc. to meet its principal and interest obligations on the
27 amount of the WIFA loan and income taxes on the surcharges.

28 IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file with Docket

1 WIFA loan and incremental income taxes on the surcharge, within 60 days after the loan agreement is
2 signed by both WIFA and the Company. The revenue calculation shall include the effects of 1) the
3 application of the previously-collected funds referenced in the previous Ordering Paragraph to
4 service the debt authorized herein, and 2) hook-up fees collected pursuant to Decision No. 67669
5 (March 9, 2005), which approved an Arsenic Impact Fee Tariff for the Company to help pay for debt
6 service and/or principal on the requested WIFA loan.

7 IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall institute
8 operating policies to remove any and all transactions between the Company and its owners that are
9 not arm's length transactions.

10 IT IS FURTHER ORDERED that the Commission's Utilities Division Staff shall carefully
11 scrutinize Valley Utilities Water Company, Inc.'s books in its next rate case, and bring to the
12 Commission's attention any instances of transactions between the Valley Utilities Water Company,
13 Inc. and its shareholder that are not arm's length, including but not limited to improper lease
14 arrangements and payment of personal expenses, along with recommendations for appropriate
15 Commission action.

16 IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall develop and
17 institute a plan to produce a positive equity position by December 31, 2010, and shall file a copy of
18 the plan as a compliance item in this docket within 90 days.

19 IT IS FURTHER ORDERED that in Valley Utilities Water Company, Inc.'s next rate
20 proceeding, the Commission's Utilities Division Staff shall bring to the attention of the Commission
21 all evidence of any inappropriate practices that contribute to the deterioration of, rather than to the
22 building of, equity.

23 IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc.'s request for an
24 Arsenic Operating and Maintenance Recovery Surcharge Mechanism is hereby denied.

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IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall annually file as part of its annual report, an affidavit with the Utilities Division attesting that the Company is current in paying its property taxes in Arizona.

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

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN

COMMISSIONER

COMMISSIONER

COMMISSIONER

COMMISSIONER

IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive Director of the Arizona Corporation Commission, have hereunto set my hand and caused the official seal of the Commission to be affixed at the Capitol, in the City of Phoenix, this ____ day of _____, 2005.

BRIAN C. McNEIL
EXECUTIVE DIRECTOR

DISSENT _____

DISSENT _____

1 SERVICE LIST FOR: VALLEY UTILITIES WATER COMPANY, INC.

2
3 DOCKET NO.: W-01412A-04-0736 and W-01412A-04-0849

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