

**NEW APPLICATION
ORIGINAL**



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**UTILITIES DIVISION
REVIEW OF STAFF REPORT/TESTIMONY 2006 JAN -6 P 1:15
CHECKLIST**

AZ CORP COMMISSION
DOCUMENT CONTROL

COMPANY NAME:	McClain Water Systems		
DOCKET NO.	W-01646A-05-	W-01646A-06-0010	W-01868A-06-0010
ORIGINATING STAFF:	James J. Dorf	W-02235A-06-0010	W-02316A-06-0010
DOCKET DUE DATE & TIME:		W-02230A-06-0010	W-01629A-06-0010
		W-02240A-06-0010	

- **Final** review by Supervisor/Manager: _____ (Due) Date: _____ Time: _____

- **Final** review by Chief: _____ (N/A) Date: _____ Time: _____

- Received by Admin Staff: _____ Date: _____ Time: _____

- Review by Compliance: _____ (Due) Date: _____ Time: _____

- Received by Admin Staff: _____ Date: _____ Time: _____

- Review by Legal Division: _____ (Due) Date: _____ Time: _____

- Received by Admin Staff: _____ Date: _____ Time: _____

- **Received by Executive Assistant**

- Review by Director's Office: _____ (Due) Date: _____ Time: _____

• **DUE TO:**

Docket 4:00PM Date: _____ Time: _____

NOTE: THIS CHECKLIST MUST TRAVEL WITH THE DOCUMENT THROUGH ALL REVIEWS. PLEASE DO NOT DETACH FROM THE DOCUMENT. THE CHECKLIST WILL BE FILED IN THE DIRECTOR'S OFFICE AFTER DOCKETING.

BEFORE THE ARIZONA CORPORATION COMMISSION

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Commissioner
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Commissioner
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Commissioner
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Commissioner

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IN THE MATTER OF THE APPLICATION FOR)	DOCKET NOS. W-01646A-05-
EMERGENCY INTERIM RATE RELIEF FOR)	W-01868A-05-
MIRACLE VALLEY WATER COMPANY, INC.,)	W-02235A-05-
COCHISE WATER COMPANY, HORSESHOE)	W-02316A-05-
RANCH WATER COMPANY, CRYSTAL)	W-02230A-05-
WATER COMPANY, MUSTANG WATER)	W-01629A-05-
COMPANY, CORONADO ESTATES WATER)	W-02240A-05-
<u>COMPANY, OWNED BY JOHNNY A. McCLAIN)</u>	REQUEST FOR EMERGENCY
	INTERIM RATE RELIEF

The Arizona Small Utilities Association of Arizona (“ASUA”) hereby submits to the Arizona Corporation Commission (“Commission”) this Application for Emergency Interim Rate Relief for Miracle Valley Water Company, Inc., Cochise Water Company, Horseshoe Ranch Water Company, Crystal Water Company, Mustang Water Company, Coronado Estates Water Company, and Sierra Sunset Water Company, each owned by Johnny A. McClain and collectively referred herein as the “McClain Systems” or “Systems”.

The McClain Systems are plagued with serious financial and operational problems that jeopardize the Systems ability to provide ongoing adequate and reliable water service to its customers. The McClain Systems are currently undergoing bankruptcy proceedings. The Systems are being operated by ASUA as the interim manager. Several of the systems have experienced water outages, sometimes lasting several days. The Systems have also experienced severe cash flow problems, more adequately described below. From the beginning of its tenure

as interim manager, ASUA has infused its own money to operate the Systems. The Systems' rates are not sufficient to operate the utilities or fix the problems.

ASUA believes that these circumstances create an emergency situation that places customers at risk and must be addressed and corrected as soon as possible. An interim rate increase is in the public interest and necessary to address and resolve the Systems' problems.

In support of the Application for Emergency Interim Rate Relief, ASUA states the following:

I. BACKGROUND

There are seven water systems owned and/or operated by Johnny A. McClain. Each of the systems and their current customer count is summarized in Attachment A. These systems have been the subject of much scrutiny by various regulatory authorities such as the Arizona Department of Revenue ("ADOR"), the Arizona Department of Environmental Quality ("ADEQ") and the Arizona Corporation Commission ("Commission"). Mr. McClain has failed to comply with numerous notices of violations issued by ADEQ, and has not paid property taxes or sales taxes for a number of years.

The McClain Systems are currently in bankruptcy proceedings. A purchase and sale agreement is in escrow pending an evaluation and establishment of a rate base valuation by the Commission. The Commission Staff has completed an evaluation of the system assets in Docket No. W-01646A-05-0506 et al. A Recommended Opinion and Order was issued on December 14, 2005 and is pending Commission action.

II. GENERAL CONDITION OF THE WATER SYSTEMS

The McClain Systems are in serious disrepair. For the last 20 years little has been done to adequately maintain the systems. Commission staff has described the physical inadequacies of the system in its report in Docket No. W-01646A-05-0506. The Commission has established hook-up moratoriums for all McClain Systems in Decision No. 68272. It also describes the

improvements and capital investment needed to upgrade the systems (capital expenditures between \$750,000 and \$1,250,000).

However, there is a short term financial need in order to permit timely repairs and improve water service to existing customers.

III. FINANCIAL STATUS

The McClain Systems have experienced negative cash flows at least since ASUA was appointed interim manager in July, 2004. For the nine-month period ending September 30, 2005, the Systems have experienced a negative cash flow of approximately \$30,000 and estimates are that for the year 2005 the total will approximate \$40,000. Meanwhile, the Systems' Accounts Payable is nearing \$100,000. See Attachment B for a summary of the cash loss and Accounts Payable situation. This negative financial situation must be addressed as quickly as possible as several vendors will no longer offer materials or services to ASUA, thus hampering its ability to make need repairs.

The McClain Systems have received a Water Infrastructure Financing Authority loan for \$12,500 and a Pinal County loan of \$10,000 to assist in making emergency repairs. ASUA has forgone receipt of its interim management fees for several months and wishes to maintain the McClain Systems as financially viable as possible.

When ASUA became interim manager in July, 2004, its focus was primarily on repairing leaks and restoring service to customers. As such, the financial results of the operations through December 31, 2004 were atypical. Bill payment and expense recognition were primarily based upon available cash flow. For purposes of determining the current cash flow requirement, the expenses for the first nine months of 2005 are more consistent. Therefore, ASUA has prorated the first nine months of 2005 to estimate its annual cash flow needs. See Attachment B.

Clearly, the existing rates of each of the systems are inadequate to support either short-term or long-term financial viability.

IV. EMERGENCY STATUS

The Commission may order interim rate relief when there is an existing emergency.¹ ASUA believes that given the following facts, the need for emergency interim rate relief is appropriate and in the public interest:

1. The McClain Systems are currently in bankruptcy proceedings.
2. The McClain Systems are in a state of disrepair and significant amounts of capital are needed to upgrade the system.
3. The Systems are experiencing inadequate cash flow to sustain their operations.
4. The ability to maintain service to customers is in doubt and preparation and adjudication of a formal rate proceeding will not provide timely relief.

Emergency interim rates are just and a reasonable first step to remedy the McClain Systems problems.

V. SURCHARGE REQUEST

The McClain Systems will need to increase cash flow by approximately \$11,700 per month to sustain operations, make necessary system repairs, maintain adequate water supplies and make progress in eliminating the high level of Accounts Payable. A monthly per meter surcharge of \$9.00 would be adequate in the short-run. See Attachment C for the method used to determine the monthly surcharge.

VI. CONCLUSION

The McClain Systems constitute an emergency. To correct the system problems will require significant capital expenditures over several years. The current McClain System water rates are inadequate to meet even short-term cash flow needs.

The emergency interim System Improvement Surcharge ("SIS") proposed by ASUA is reasonable and will allow it, as interim manager, to pay debts to local vendors, to make needed

¹ Scates v. Arizona Corporation Commission, 118 Ariz. 531, 578 P.2d 612 (1978).

short-term system repairs and possibly make selected improvements. It is clearly in the best interests of the McClain Systems' customers to authorize this interim increase.

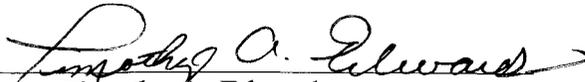
VII. REQUEST FOR RELIEF

Therefore, for all the foregoing reasons, ASUA respectfully requests that the Commission issue an order:

1. Finding that the McClain Systems' problems constitute an emergency.
2. Concluding that it is in the public interest to authorize the requested interim SIS.
3. Ordering ASUA to charge the interim surcharge requested herein pending a determination of a permanent rate case proceeding.
4. Granting any additional and further relief as the Commission deems appropriate.

RESPECTFULLY SUBMITTED this 6 day of January, 2006.

ARIZONA SMALL UTILITIES ASSOCIATION

By 
Timothy A. Edwards
210 N. Central, Suite 6B
Avondale, Arizona 85323
Interim Manager for McClain Systems

Original and 16 copies of the foregoing
filed this 6 day of January, 2006 with:

Docket Control
Arizona Corporation Commission
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Jason Gellman
Legal Division
Arizona Corporation Commission
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McClain Systems
Docket No. W-01646A-05-0xxx et al
Customer Summary
As of November, 2005

ATTACHMENT A

<u>SYSTEM</u>	<u>Number of Customers</u>	<u>%</u>
Miracle Valley Water Company, Inc.	299	23.0%
Cochise Water Company	413	31.7%
Horseshoe Ranch Water Company	220	16.9%
Crystal Water Company	63	4.8%
Mustang Water Company	71	5.5%
Coronado Estates Water Company	209	16.1%
Sierra Sunset Water Company	26	2.0%
Total	<u>1,301</u>	<u>100.0%</u>

ATTACHMENT B

McClain Systems
 Docket No. W-01646A-05-0xxx et al
 Income Statement - Cash Basis

PRO FORMA INCOME STATEMENT

	9 Months Ended 9/30/2005	Pro Forma 12 Months Ended 12/31/2005	
Revenues	<u>\$312,767</u>	<u>\$417,022</u>	
Expenses			
Salaries & Contract Labor	90,989	121,319	For Certified Operator (\$38,000 annually) and 3 laborers.
Repairs & Maintenance	62,437	83,250	Primarily for new pumps and leak repairs.
Interim Manager Fees	51,067	68,089	At \$6.60 per meter per month.
Utilities	48,622	64,829	Primarily Sulpher Springs Coop electricity.
Supplies	26,382	35,175	Significant amount of bottled water & other supplies.
Insurance	14,742	19,656	Hazard and Work Comp Insurance.
Outside Services	9,268	12,358	Primarily CPA and Arizona Blue Stake.
Office Expense	7,671	10,227	Bank charges, printing and postage.
Payroll Taxes	15,245	20,327	Fica, unemployment, etc.
Rent	2,800	3,733	
Miscellaneous	13,120	17,493	ADEQ fees, miscellaneous.
Total Expenses	<u>342,343</u>	<u>456,457</u>	
Cash Basis Operating Loss	<u>(\$29,576)</u>	<u>(\$39,435)</u>	
Current Accounts Payable Balance:			
Arizona Small Utilities Association- interim mgt fees		\$31,447	
Arizona Department of Revenue - sales taxes		22,341	
Water Supply Wholesaler - water related repair supplies		9,455	
Back-hoe Repair		7,819	
Electrical Contractor - repairs		6,949	
All other Vendors		18,406	
		<u>\$96,417</u>	

McClain Systems
Docket No. W-01646A-05-0xxx et al

ATTACHMENT C

	<u>Annual Amount</u>	<u>Monthly Amount</u>
Current Estimated Annual Operating Cash Shortfall	\$40,000	\$3,333
Amortization of Current Accounts Payable over 24 Months	\$100,000	4,167
Additional Allowance for System Improvements for 12 months	\$50,000	4,167
		<u>\$11,667</u> ¹
Current Number of Metered Customers		<u>1,300</u> ²
Average cost per meter (1 / 2)		<u>\$8.97</u>
Proposed System Improvement Surcharge at \$9 per meter per month		<u>\$11,709</u>