

ORIGINAL



0000039768

MEMORANDUM

30A

TO: Docket Control

FROM: Ernest G. Johnson
Director
Utilities Division

for

DATE: January 17, 2006

RE: SECOND AMENDED STAFF REPORT FOR CORONADO UTILITIES, INC., APPLICATION FOR A CERTIFICATE OF CONVENIENCE AND NECESSITY TO PROVIDE WASTEWATER SERVICE TO A PORTION OF PINAL COUNTY AND FOR AUTHORITY TO ISSUE SHORT AND LONG-TERM DEBT (DOCKET NOS. SW-04305A-05-0086 AND SW-04305A-05-0087)

Attached is the **Second Amended** Staff Report for Coronado Utilities, Inc., application for a Certificate of Convenience and Necessity ("CC&N") in Pinal County and for authority to issue short- and long-term debt. Staff recommends approval of the CC&N, Phase 1, Phase 2 and Phase 3 rates, and financing with conditions.

EGJ:LAJ:red

Originator: Linda Jaress

AZ CORP COMMISSION
DOCUMENT CONTROL

2006 JAN 18 A 9:33

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Service List for: Coronado Utilities, Inc.
Docket Nos. SW-04305A-05-0086 and SW-04305A-05-0087

Mr. Jay Shapiro
Mr. Patrick Black
Fennemore Craig, PC
3003 North Central Avenue, Suite 2600
Phoenix, Arizona 85012

Mr. Christopher C. Kempley
Chief, Legal Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Mr. Ernest G. Johnson
Director, Utilities Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Ms. Lyn Farmer
Chief, Hearing Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

**SECOND AMENDED STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION**

CORONADO UTILITIES, INC.

DOCKET NOS. SW-04305A-05-0086

AND

SW-04305A-05-0087

**APPLICATION FOR A
CERTIFICATE OF CONVENIENCE
AND NECESSITY**

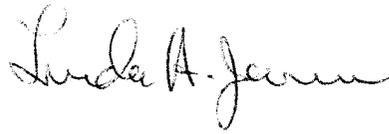
AND

**APPLICATION FOR AUTHORITY
TO ISSUE SHORT- AND LONG-TERM
DEBT FOR ACQUISITION AND
IMPROVEMENT OF WASTEWATER FACILITIES**

JANUARY 17, 2006

STAFF ACKNOWLEDGMENT

The Second Amended Staff Report for Coronado Utilities, Inc. (Docket Nos. SW-04305A-05-0086 and SW-04305A-05-0087) was prepared by the Staff member listed below.

A handwritten signature in black ink, reading "Linda A. Jaress". The signature is written in a cursive style with a large initial "L".

Linda A. Jaress
Executive Consultant III

EXECUTIVE SUMMARY
CORONADO UTILITIES, INC.
DOCKET NOS. SW-04305A-05-0086 AND SW-04305A-05-0087

On December 20, 2005, the Administrative Law Judge (“ALJ”) filed a Procedural Order reopening the hearing on this matter. The procedural order also requested that Staff and Coronado Utilities, Inc. (“Coronado” or “Company”) file information regarding two specific issues. The Procedural Order requested more information:

(1) on the background and effect of a criminal proceeding involving Santec Corporation, an affiliate of Coronado; and

(2) to determine if the rate shock anticipated for customers from the sale of the BHP Copper wastewater treatment facility can be mitigated by a three step rate phase-in, a hook-up fee or by other means.”

Regarding the first request, Staff believes that the recommendations proposed by Staff in the Amended Staff Report sufficiently address the safety concerns and concerns about the effect of any criminal conduct of Santec Corporation (“Santec”) on the operations of Coronado.

Regarding the concern about rate shock, Coronado has proposed rate schedules that have three phases, somewhat mitigating the impact of the substantial rate increases to the customers of Coronado. Staff recommends approval of those rates.

Therefore, Staff recommends approval of the financing application and Certificate of Convenience and under the terms delineated in the Recommendation section of this report.

TABLE OF CONTENTS

Page

INTRODUCTION 1

MORE INFORMATION ON THE BACKGROUND AND EFFECT OF THE CRIMINAL PROCEEDING . 1

MITIGATION OF RATE SHOCK 2

HOOK-UP FEES 3

RECOMMENDATIONS 4

EXHIBITS

RATE DESIGN FOR PHASED-IN RATES LAJ-1

Introduction

On December 20, 2005, the Administrative Law Judge (“ALJ”) filed a Procedural Order reopening the hearing on this matter. The procedural order also requested that Staff and Coronado Utilities, Inc. (“Coronado” or “Company”) file information regarding two specific issues. The Procedural Order requested more information:

“(1) on the background and effect of a criminal proceeding involving Santec Corporation, an affiliate of Coronado; and

(2) to determine if the rate shock anticipated for customers from the sale of the BHP Copper wastewater treatment facility can be mitigated by a three step rate phase-in, a hook-up fee or by other means.”

More Information on the Background and Effect of the Criminal Proceeding

On January 12, 2006, Staff filed the following documents in these dockets regarding the criminal proceeding against Santec Corporation (“Santec”), Coronado’s affiliate:

1. A copy of the Arizona Division of Occupational Safety and Health (“ADOSH”) Reports, Inspection Nos. 304944523 and 304839483.
2. A copy of the Rural Metro Fire Department Incident Report, Incident No. 01-2001-0006196-000.
3. A copy of the Yuma County Sheriff’s Department Report, Incident No. 2001-19486.
4. A copy of the Industrial Commission of Arizona (“ICOA”), ADOSH, Fatality Report regarding Gary V. Lanser.
5. A copy of the ICOA Citation and Notification of Penalty, Inspection No. K0234-304944523.
6. A copy of the Indictment of Santec Corporation, amongst other entities and persons, CR No. 2002-01238.
7. A copy of the Plea Agreement Santec Corporation entered into with the State of Arizona regarding CR No. 2002-01238.
8. A copy of the Minute Entry entitled “Imposition of Sentence” for Santec Corporation. CR No. 2202-01238.

Staff believes these documents fulfill the Procedural Order’s requirement to provide background of the criminal proceeding. Regarding the effect of the criminal proceeding which

Staff was asked to address, Staff believes that the conditions recommended in its Amended Staff Report will help reduce or eliminate accidents at the Coronado facilities. Those recommendations are as follows:

1. That all operators, agents, employees or operators including employees and agents of contractors and/or subcontractors operating the Coronado facilities must comply with all Arizona Division of Occupational Safety and Health (“ADOSH”) requirements including any and all training required by ADOSH to operate wastewater facilities.
2. On an annual basis, on the anniversary date of the Decision in this matter, for three years, Coronado must file in Docket Control, as a compliance item, certification from ADOSH that it has availed itself of ADOSH consultation services and its operators, agents, employees including employees and agents of contractors/and or subcontractors operating the Coronado facilities have taken appropriate training.

However, Staff has reviewed the two recommendations shown above and would like to modify them to also apply to any person “constructing” facilities rather than applying only to those who “operate” the facilities.

Mitigation of Rate Shock

The Recommended Opinion and Order (“ROO”) issued in this docket took a significant step in mitigating rate shock by reducing the initial residential rates from the level recommended by Staff and the Company. Since the ROO and the Procedural Order was issued, BHP Copper (“BHP”) and Coronado reached an agreement whereby BHP would subsidize the rates of Coronado for one year. This is explained in more detail in the December 28, 2005 testimony of Mr. Jason Williamson, witness for and part owner of Coronado.

The recommended rates and phases for residential customers are as follows:

1. Phase 1: Initial rates of \$27.00 per month.
2. Phase 2: \$37.00 per month effective when all the following three criteria are met:
 - a) The new wastewater treatment plant and system are in service;
 - b) The Company files with Docket Control an Arizona Department of Environmental Quality (“ADEQ”) Approval of Construction;
 - c) The Company gives customers notice of the rate increase in a form acceptable to Staff and at least 30 days before the rates are to be implemented.

3. Phase 3: \$46.50 per month effective twelve months after the Phase 2 rates go into effect.
4. The recommended rates for residential and all other customer classes are attached to this report as Schedule LAJ-1. For all phased in rates, the second and third phases should be implemented under the same restrictions as for the phases for the residential rates.

Integral to the Phase 1 rates is the prohibition (to which Coronado has agreed) against recording an allowance for funds used during construction ("AFUDC") until Phase 2 rates become effective. This prohibition is based on the concept that AFUDC is a deferral of the recovery of interest on debt for construction. Phase 1 rates include amounts for debt service. Therefore, allowing Coronado to record AFUDC would ultimately result in double recovery of interest.

Staff believes these proposed rates and phases are superior to those previously recommended by Staff, the Company and the ROO because they include an additional phase reducing rates from the previous recommended levels for one year. However, Staff also recommends that Coronado be required to file a rate case fifteen months after the implementation of Phase 2 rates to insure that the rates and costs are synchronized. This is a modification to Staff's earlier recommendation that a rate case be filed during its fourth year of operations using its third year as the test year.

Hook-up Fees

The Procedural Order also requested consideration of a hook-up fee to mitigate the effect of rate shock. Staff was further motivated to examine this option after a newspaper article appeared in the Arizona Republic on December 12, 2005, which said that 35,000 homes were "envisioned" in or around Coronado's proposed service territory. However, both the Company and BHP responded to Staff's data requests about this article and demonstrated that development in the area was in only the most initial preparation stages and that it would be at least several years before new homes would be built, if any are built at all.

Hook-up fees are often a good method of protecting current customers from the costs of construction to serve new and future customers. In Coronado's case, the new plant is being built to serve current customers and there will be little or no extra capacity to serve new customers. Also, Staff believes that setting hook-up fees in this case would not be productive because for the foreseeable future, little growth is expected and the revenues from the hook-up fees is likely to be de minimus.

Recommendations

Staff recommends the application for approval of a CC&N and financing with the following conditions:

Regarding safety, Staff recommends:

1. That all operators, agents, employees or operators including employees and agents of contractors and/or subcontractors operating or constructing the Coronado facilities must comply with all ADOSH requirements including any and all training required by ADOSH to operate wastewater facilities.
2. On an annual basis, on the anniversary date of the Decision in this matter, for three years, Coronado must file in Docket Control, as a compliance item, certification from ADOSH that it has availed itself of ADOSH consultation services and its operators, agents, employees including employees and agents of contractors/and or subcontractors operating or constructing the Coronado facilities have taken appropriate training.

Regarding rates, Staff recommends:

3. That the Commission authorize Coronado Utilities, Inc. to charge the wastewater rates and charges shown on Schedule LAJ-1.
4. That Phase 2 rates should become effective when all the following three criteria are met: The new wastewater treatment plant and system are in service; the Company files with Docket Control, as a compliance item, an ADEQ Approval of Construction and; the Company gives customers notice of the rate increase in a form acceptable to Staff and at east 30 days before the rates are to be implemented.
5. That the Commission make a fair value rate base finding of \$3,096,163.
6. That Coronado use the depreciation rates as stated in the Staff Report filed on May 7, 2005.
7. That Coronado be ordered to file a rate application fifteen months after the implementation of Phase 2 rates.
8. That the Commission require Coronado Utilities, Inc. to maintain its books and records in accordance with the National Association of Regulatory Utility Commissioners ("NARUC") Uniform System of Accounts for Sewer Utilities.

9. That the Commission require Coronado Utilities, Inc., to file with Docket Control, as a compliance item, a tariff consistent with the rates and charges authorized by the Commission within 30 days of the effective date of a decision in this matter.

Regarding financing, Staff recommends:

10. That Coronado be authorized to obtain \$2,650,800 of long-term debt financing on the terms and conditions consistent with or better than those used in Staff's pro forma analysis subject to establishment of rates that provide Staff's recommended operating income.
11. That Coronado's initial capitalization be comprised of at least \$878,863 of equity.
12. That Coronado be required to retain seventy-five percent of its net operating income until equity represents forty percent of total capital.
13. That Coronado be required to file in Docket Control by April 15th of each year a Statement of Liabilities and Stockholders Equity until and including such time as the equity represents forty percent of total capital.
14. That the Commission approve the granting of liens in favor of the lender as required to secure the borrowings authorized.
15. That no loan funds be applied to operating expenses or income.
16. That Coronado be authorized to engage in any transaction and to execute any documents necessary to effectuate the financing authorizations granted.
17. That Coronado be ordered to file copies of all executed financing documents with Docket Control within 90 days of loan closing.

Regarding other compliance, Staff recommends:

18. That the Commission require Coronado Utilities, Inc., to file with Docket Control, as a compliance item, a copy of the Pinal County franchise within 365 days of the effective date of the decision in this matter.
19. That the Commission require Coronado Utilities, Inc., to file with Docket Control, as a compliance item, a copy of the Arizona Department of Environmental Quality Unified Water Quality Permit for the San Manuel Wastewater Treatment Facility authorizing a treatment and disposal capacity of 350,000 gallons per day within 365 days of the effective date of the decision and order in this matter.

Coronado Utilities, Inc.

Docket Nos. SW-04305A-05-0086 and SW-04305A-05-0087

Page 6

Staff further recommends that the Commission's Decision granting this Certificate of Convenience and Necessity to Coronado Utilities, Inc., be considered null and void after due process should Coronado fail to meet Conditions 9, 18 and 19 within the time specified.

**RATE DESIGN
FOR PHASED-IN RATES**

PHASE 1

Monthly Customer Charges	Phase 1
Residential	\$ 27.00
Commercial	\$ 7.50
Mobile Home Park - Winter Only (See Note A)	\$ 7.50
School	\$ 7.50
Volumetric Rates - Based on Metered Water Usage	
Commercial - per 100 gallons of water usage	\$ 0.6400
Mobile Home Park - per 100 gallons of water usage (Winter Only - See Note A)	\$ 0.3700
School - per 100 gallons of water usage	\$ 0.2000
Volumetric Rates - Based on Number of Units	
Mobile Home Park - monthly rate per occupied space (Summer Only - See Note A)	\$ 20.71
Effluent Sales	
Per 1,000 Gallons for General Irrigation	\$ 0.15
Per Acre Foot (or 325,851 gallons) for General Irrigation	\$ 48.88

PHASE 2

Monthly Customer Charges	Phase 2
Residential	\$ 37.00
Commercial	\$ 7.50
Mobile Home Park - Winter Only (See Note A)	\$ 7.50
School	\$ 7.50
Volumetric Rates - Based on Metered Water Usage	
Commercial - per 100 gallons of water usage	\$ 0.8100
Mobile Home Park - per 100 gallons of water usage (Winter Only - See Note A)	\$ 0.4700
School - per 100 gallons of water usage	\$ 0.2561
Volumetric Rates - Based on Number of Units	
Mobile Home Park - monthly rate per occupied space (Summer Only - See Note A)	\$ 31.86
Effluent Sales	
Per 1,000 Gallons for General Irrigation	\$ 0.15
Per Acre Foot (or 325,851 gallons) for General Irrigation	\$ 48.88

PHASE 3

Monthly Customer Charges	Phase 3
Residential	\$ 46.50
Commercial	\$ 7.50
Mobile Home Park - (Winter Only - See Note A)	\$ 7.50
School	\$ 7.50
Volumetric Rates - Based on Metered Water Usage	
Commercial - per 100 gallons of water usage	\$ 0.9800
Mobile Home Park - per 100 gallons of water usage (Winter Only - See Note A)	\$ 0.5700
School - per 100 gallons of water usage	\$ 0.3122
Volumetric Rates - Based on Number of Units	
Mobile Home Park - monthly rate per occupied space (Summer Only -See Note A)	\$ 31.86
Effluent Sales	
Per 1,000 Gallons for General Irrigation	\$ 0.15
Per Acre Foot (or 325,851 gallons) for General Irrigation	\$ 48.88

Note A: Summer (April, May, June, July, August, September)
Winter (January, February, March, October, November, December)

ORIGINAL



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MEMORANDUM

RECEIVED

30A

TO: Docket Control

FROM: Ernest G. Johnson
Director
Utilities Division

for

2006 JAN 18 A 9:34

AZ CORP COMMISSION
DOCUMENT CONTROL

DATE: January 17, 2006

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EGJ:LAJ:red

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**SECOND AMENDED STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION**

CORONADO UTILITIES, INC.

DOCKET NOS. SW-04305A-05-0086

AND

SW-04305A-05-0087

**APPLICATION FOR A
CERTIFICATE OF CONVENIENCE
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AND

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TO ISSUE SHORT- AND LONG-TERM
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JANUARY 17, 2006

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Linda A. Jaress
Executive Consultant III

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DOCKET NOS. SW-04305A-05-0086 AND SW-04305A-05-0087

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TABLE OF CONTENTS

Page

INTRODUCTION.....1

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 - c) The Company gives customers notice of the rate increase in a form acceptable to Staff and at least 30 days before the rates are to be implemented.

3. Phase 3: \$46.50 per month effective twelve months after the Phase 2 rates go into effect.
4. The recommended rates for residential and all other customer classes are attached to this report as Schedule LAJ-1. For all phased in rates, the second and third phases should be implemented under the same restrictions as for the phases for the residential rates.

Integral to the Phase 1 rates is the prohibition (to which Coronado has agreed) against recording an allowance for funds used during construction ("AFUDC") until Phase 2 rates become effective. This prohibition is based on the concept that AFUDC is a deferral of the recovery of interest on debt for construction. Phase 1 rates include amounts for debt service. Therefore, allowing Coronado to record AFUDC would ultimately result in double recovery of interest.

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Recommendations

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Regarding rates, Staff recommends:

3. That the Commission authorize Coronado Utilities, Inc. to charge the wastewater rates and charges shown on Schedule LAJ-1.
4. That Phase 2 rates should become effective when all the following three criteria are met: The new wastewater treatment plant and system are in service; the Company files with Docket Control, as a compliance item, an ADEQ Approval of Construction and; the Company gives customers notice of the rate increase in a form acceptable to Staff and at east 30 days before the rates are to be implemented.
5. That the Commission make a fair value rate base finding of \$3,096,163.
6. That Coronado use the depreciation rates as stated in the Staff Report filed on May 7, 2005.
7. That Coronado be ordered to file a rate application fifteen months after the implementation of Phase 2 rates.
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9. That the Commission require Coronado Utilities, Inc., to file with Docket Control, as a compliance item, a tariff consistent with the rates and charges authorized by the Commission within 30 days of the effective date of a decision in this matter.

Regarding financing, Staff recommends:

10. That Coronado be authorized to obtain \$2,650,800 of long-term debt financing on the terms and conditions consistent with or better than those used in Staff's pro forma analysis subject to establishment of rates that provide Staff's recommended operating income.
11. That Coronado's initial capitalization be comprised of at least \$878,863 of equity.
12. That Coronado be required to retain seventy-five percent of its net operating income until equity represents forty percent of total capital.
13. That Coronado be required to file in Docket Control by April 15th of each year a Statement of Liabilities and Stockholders Equity until and including such time as the equity represents forty percent of total capital.
14. That the Commission approve the granting of liens in favor of the lender as required to secure the borrowings authorized.
15. That no loan funds be applied to operating expenses or income.
16. That Coronado be authorized to engage in any transaction and to execute any documents necessary to effectuate the financing authorizations granted.
17. That Coronado be ordered to file copies of all executed financing documents with Docket Control within 90 days of loan closing.

Regarding other compliance, Staff recommends:

18. That the Commission require Coronado Utilities, Inc., to file with Docket Control, as a compliance item, a copy of the Pinal County franchise within 365 days of the effective date of the decision in this matter.
19. That the Commission require Coronado Utilities, Inc., to file with Docket Control, as a compliance item, a copy of the Arizona Department of Environmental Quality Unified Water Quality Permit for the San Manuel Wastewater Treatment Facility authorizing a treatment and disposal capacity of 350,000 gallons per day within 365 days of the effective date of the decision and order in this matter.

Coronado Utilities, Inc.

Docket Nos. SW-04305A-05-0086 and SW-04305A-05-0087

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Staff further recommends that the Commission's Decision granting this Certificate of Convenience and Necessity to Coronado Utilities, Inc., be considered null and void after due process should Coronado fail to meet Conditions 9, 18 and 19 within the time specified.

**RATE DESIGN
FOR PHASED-IN RATES**

PHASE 1

Monthly Customer Charges	Phase 1
Residential	\$ 27.00
Commercial	\$ 7.50
Mobile Home Park - Winter Only (See Note A)	\$ 7.50
School	\$ 7.50
Volumetric Rates - Based on Metered Water Usage	
Commercial - per 100 gallons of water usage	\$ 0.6400
Mobile Home Park - per 100 gallons of water usage (Winter Only - See Note A)	\$ 0.3700
School - per 100 gallons of water usage	\$ 0.2000
Volumetric Rates - Based on Number of Units	
Mobile Home Park - monthly rate per occupied space (Summer Only - See Note A)	\$ 20.71
Effluent Sales	
Per 1,000 Gallons for General Irrigation	\$ 0.15
Per Acre Foot (or 325,851 gallons) for General Irrigation	\$ 48.88

PHASE 2

Monthly Customer Charges	Phase 2
Residential	\$ 37.00
Commercial	\$ 7.50
Mobile Home Park - Winter Only (See Note A)	\$ 7.50
School	\$ 7.50
Volumetric Rates - Based on Metered Water Usage	
Commercial - per 100 gallons of water usage	\$ 0.8100
Mobile Home Park - per 100 gallons of water usage (Winter Only - See Note A)	\$ 0.4700
School - per 100 gallons of water usage	\$ 0.2561
Volumetric Rates - Based on Number of Units	
Mobile Home Park - monthly rate per occupied space (Summer Only - See Note A)	\$ 31.86
Effluent Sales	
Per 1,000 Gallons for General Irrigation	\$ 0.15
Per Acre Foot (or 325,851 gallons) for General Irrigation	\$ 48.88

PHASE 3

Monthly Customer Charges	Phase 3
Residential	\$ 46.50
Commercial	\$ 7.50
Mobile Home Park - (Winter Only - See Note A)	\$ 7.50
School	\$ 7.50
Volumetric Rates - Based on Metered Water Usage	
Commercial - per 100 gallons of water usage	\$ 0.9800
Mobile Home Park - per 100 gallons of water usage (Winter Only - See Note A)	\$ 0.5700
School - per 100 gallons of water usage	\$ 0.3122
Volumetric Rates - Based on Number of Units	
Mobile Home Park - monthly rate per occupied space (Summer Only -See Note A)	\$ 31.86
Effluent Sales	
Per 1,000 Gallons for General Irrigation	\$ 0.15
Per Acre Foot (or 325,851 gallons) for General Irrigation	\$ 48.88

Note A: Summer (April, May, June, July, August, September)
Winter (January, February, March, October, November, December)