

ORIGIN



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MEMORANDUM

TO: Docket Control

FROM: Ernest G. Johnson *EGJ*
Director
Utilities Division

DATE: February 2, 2007

RE: STAFF REPORT FOR DONEY PARK WATER COMPANY'S REQUEST FOR AUTHORIZATION TO ISSUE LONG-TERM DEBT (DOCKET NO. W-01416A-06-0719)

Attached is the Staff Report for Doney Park Water Company's application for authorization to issue long-term debt. Staff recommends approval.

Any comments to this Staff Report should be filed in Docket Control by February 16, 2007.

EGJ:All:red

Originator: Alexander Ibhade Igwe

AZ CORP COMMISSION
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Service List for: Doney Park Water Company
Docket No. W-01416A-06-0719

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**STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION**

DONEY PARK WATER COMPANY

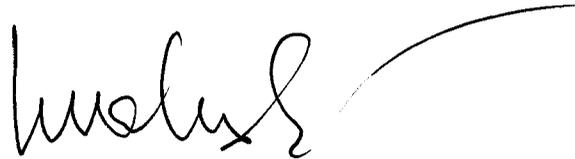
DOCKET NO. W-01416A-06-0719

**APPLICATION FOR APPROVAL
OF FINANCING**

FEBRUARY 2, 2007

STAFF ACKNOWLEDGMENT

The Staff Report for Doney Park Water Company, Docket No. W-01416A-06-0719 was the responsibility of the following Staff members listed below. Alexander Ihade Igwe was responsible for reviewing the application and performing pertinent financial analysis; Jian Liu analyzed the engineering issues; and Carmen Madrid researched the Consumer Service issues.



Alexander Ihade Igwe
Executive Consultant III



Jian Liu
Utilities Engineer



Carmen Madrid
Public Utility Consumer Analyst I

**EXECUTIVE SUMMARY
DONEY PARK WATER COMPANY
DOCKET NO. W-01416A-06-0719**

On November 13, 2006, Doney Park Water Company ("Doney Park" or "Company") filed an application with the Arizona Corporation Commission ("Commission") requesting authorization to issue up to \$1,530,000 of long-term debt with the Industrial Development Authority ("IDA") of Coconino County. The Company states that the loan proceeds will fund drilling of two new wells, installation of appurtenances, interconnection of the new wells, and the related finance costs. The proposed debt is repayable over 15-years at an interest rate of 1.05 basis points above the prevailing 10 year Treasury bond rate. At a projected interest rate of 5.85 percent, the proposed debt could result in an annual interest and principal payments of approximately \$153,448. The Company states that the cash flow from its Development Fees and operating income would be sufficient to fulfill its proposed debt obligations. Therefore, the Company's proposal would not trigger a rate increase nor result in additional costs to rate payers.

The Company claims that the new wells are necessary to mitigate low production by its two existing wells, provide necessary back-ups, insure system reliability and minimize the possibility of any curtailment during the summer months.

Staff's financial analysis finds that the Company has sufficient cash flow from its operations and collection of Development Fees to meet the interest and principal payments on the proposed debt. Staff's analysis further shows that the Company would have a Debt Service Coverage ("DSC") of 3.10, if authorized to incur its proposed long-term debt. A DSC of 3.10 indicates that Doney Park has the ability to generate sufficient cash flow from its operations to meet the anticipated debt obligations. Based on the projected customer growth, we estimate that Doney Park could generate additional \$136,000 from Development Fees, for the payment of its debt obligations.

Staff's engineering analysis indicates that the Company's system consists of six wells, producing approximately 1,675 gallons per minute, and twenty-two storage tanks with total capacity of 4.497 million gallons. Further analysis projects that the Company has an annual growth rate of approximately 120 new connections, for the next five years. Based on the current water use data provided by the Company, Staff initially concluded that the existing water systems have adequate capacity to support its growth projection, and that the proposed wells were not necessary for present or future provision of service. However, the Company has provided additional information demonstrating its difficulty in maintaining tank pressures as well as tank levels, during high peak demands, usually between Memorial Day and the Fourth of July. Doney Park attributes this higher than normal demand to influx of visitors during the above referenced period. Also, the Company states that it has a water supply agreement with the U. S. Forest Service, requiring it to maintain adequate capacity for fire fighting in the same period. Doney Park claims that it has experienced numerous low pressure calls on weekends during its high peak demands and that capacity shortfalls have occurred when all its wells were producing at full capacity. In conclusion, the Company contends that the proposed new wells are necessary to enhance its ability to meet higher than normal peak demands and effectively manage any

unforeseen emergencies, such as well pumps failure. Based on the additional information provided by the Company, Staff finds that Doney Park has a unique and complex water system, with a peak day demand that is greater than that of a typical water system. As a result, Staff revised its initial system analysis to account for the greater than normal demand placed on the systems during peak demands. Staff concludes that the two new wells may be necessary to enable Doney Park meet its unusual peak demands.

Staff's financial analysis indicates that the Company has the ability to meet its proposed debt obligations while the revised engineering analysis supports its proposal to drill two new wells, due to a higher than normal peak day demand. Accordingly, Staff recommends approval of the Company's proposal to incur up to \$1,530,000 in long-term debt for the purpose of drilling two new wells as well as installation of the related appurtenances.

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Introduction

On November 13, 2006, Doney Park Water Company ("Doney Park" or "Company") filed an application with the Arizona Corporation Commission ("Commission"), requesting authorization to issue up to \$1,530,000.00 in long-term debt with the Industrial Development Authority ("IDA") of Coconino County.

Public Notice

Notice of the pending financing application was published in the Arizona Daily Sun, a newspaper widely circulated in Flagstaff, Coconino County, on December 2, 2006. A copy of an affidavit attesting to publication of the notice is attached.

Background

Doney Park is a member-owned non-profit corporation certificated to provide water service in Coconino County. It currently serves approximately 3,300 customers, with a reported growth of 80 and 56 new connections in 2005 and 2004, respectively. The Company's current rates and charges were approved in Commission Decision No. 58752, effective September 1, 1994.

The Transaction

Doney Park requests the Commission authorization to obtain up to \$1,530,000 in long-term debt from IDA. The proposed loan proceeds will fund drilling of two new wells, installation of pertinent appurtenances, interconnection of the new wells as well as for related finance costs. The Company indicates that the proposed loan would be secured with its general revenues, thus its assets would not be encumbered as a result of the new debt. The proposed loan is repayable over 15 years at an interest rate of 1.05 basis points above the prevailing 10 year Treasury bond rate. Based on a projected interest rate of 5.85 percent, the Company estimates a monthly interest and principal payments of \$12,787.35. The Company states that the cash flow from its Development Fee, as authorized in Decision No. 54298, and operating income would enable it to fulfill its debt obligations. Decision No. 54298 authorized the Company to impose a \$2,000 Development Fee on each new connection and the proceeds are being treated as a component of equity.

Doney Park claims that the new wells are necessary to mitigate low production by its two existing wells and obviate the related high cost of maintenance. Also, the proposed wells would provide necessary back-ups, insure system reliability and minimize the possibility of any curtailment during the summer months.

The Company requests expedited processing by the Commission. It states that timely Commission approval is necessary to enable the contractor to commence drilling in January 2007. Doney Park anticipates that if drilling commences in January 2007, the wells would

provide additional production for the summer months. In addition, the Company asserts that timely approval by the Commission would enhance its potential of securing IDA funding, since funding is based on availability and on a first-come first-serve basis.

Financial Analysis

Based on a maximum loan amount of \$1,530,000, the Company's proposal will result in a yearly interest and principal payment of \$153,448. The Company's audited 2005 financial statement reports no long-term debt but shows \$3,609,493 in Advances in Aid of Construction. Also, the Company reported total current assets of \$777,146 and total current liabilities of \$383,563.

Staff's financial analysis indicates that approval of the Company's proposed debt would result in a Debt Service Coverage ("DSC") ratio of 3.10 and a Times Interest Earned Ratio ("TIER") of negative 1.55. The DSC represents the number of times internally generated cash will cover required principal and interest payments on long-term debt. A DSC greater than 1.0 indicates that operating cash flow is sufficient to cover debt obligations. As indicated above, Staff's calculated DSC shows that the Company's internally generated cash flow would be adequate to meet principal and interest payments of its proposed long-term debt. The TIER represents the number of times earnings will cover interest expense on long-term debt. A TIER greater than 1.0 means that operating income is greater than interest expense. A TIER less than 1.0 is not sustainable in the long term but does not necessarily mean that debt obligations cannot be met in the short-term.

Further, Doney Park indicates that the Commission authorized it to collect a one time \$2,000 Development Fee from each new connection (Decision No. 54298). In 2004 and 2005, the Company reported an average growth of 68 new connections, representing an aggregate annual Development Fee of \$136,000. From the foregoing, Staff finds that the Company could generate significant cash flow from Development Fees, thus enhancing its ability to meet the proposed debt obligations.

Engineering Analysis

The Company's existing water system consists of six wells producing approximately 1,675-gallons per minutes ("GPM"), and twenty-two storage tanks with total storage tank capacity of 4.497 million-gallons. Its projected growth for the next five years is 120 new connections per year. Based on the current water use data provided by the Company, Staff initially concluded that the existing water systems have adequate capacity to support its growth projection, and that the proposed wells were not necessary for present or future provision of service. However, the Company has provided additional information demonstrating its difficulty in maintaining tank pressures as well as tank levels, during high peak demands, usually between Memorial Day and Fourth of July. Doney Park attributes this higher than normal demand to influx of visitors during the above referenced period. Also, the Company states that it has a water supply agreement with the U. S. Forest Service, requiring it to maintain adequate capacity

for fire fighting in the same period. Doney Park claims that it has experienced numerous low pressure calls on weekends during high peak demands and that these capacity shortfalls occurred when its wells were producing at full capacity. In conclusion, the Company contends that the proposed new wells would enhance its ability to meet higher than normal peak demands, especially in the event of unforeseen emergencies, such as well pumps failure. Based on the additional information provided by the Company, Staff finds that Doney Park has a unique and complex water system, with a peak day demand that is greater than that of a typical water system. As a result, Staff revised its initial system analysis to account for the greater than normal demand, placed on the Company's systems during peak demands. Staff concludes that the two new wells may be necessary to enable Doney Park meet its unusual peak demands.

Staff's engineering analysis found the Company's costs estimates to be reasonable. However, no "used and useful" determination of the proposed plant was made, and no particular future treatment should be inferred for rate making or rate base purposes.

Compliance Issues

Arizona Department of Environmental Quality ("ADEQ") has determined that this system has no deficiencies and is currently delivering water that meets the water quality standards required by the Arizona Administrative Code, Title 18, Chapter 4.

Staff did not find any compliance issues with the Company.

Consumer Services Issues

Staff's inquiry from the Corporations Section of the Arizona Corporation Commission, confirms that the company is in good standing.

Staff's search of the Consumer Services database identified eight complaints in 2006, on billing, new service, quality of service and disconnect/terminations. Also, there was an inquiry on disconnection/termination. All the complaints have been resolved.

Recommendations

Staff recommends approval of the Company's proposal to obtain a long-term debt in an amount up to \$1,530,000 from IDA.

Staff further recommends authorizing the Company to engage in any transactions and to execute or cause to be executed any documents so as to effectuate the authorizations requested with the application.

Staff further recommends that the Company submit to the Commission within 60 days of the loan package closing, a copy of all notes and other documents memorializing the authorized transaction.

FINANCIAL ANALYSIS

Selected Financial Data
Including Immediate Effects of the Proposed Debt

| | [A] <u>12/31/2005</u> | | [B] <u>Pro Forma</u> | |
|----|--------------------------|--------------|-------------------------|---------------|
| 1 | Operating Income | \$ (135,883) | \$ (135,883) | |
| 2 | Depreciation & Amort. | 612,184 | 612,184 | |
| 3 | Income Tax Expense | 0 | 0 | |
| 4 | | | | |
| 5 | Interest Expense | 0 | 87,762 | |
| 6 | Repayment of Principal | 0 | 65,686 | |
| 7 | | | | |
| 8 | | | | |
| 9 | TIER | | | |
| 10 | [1+3] ÷ [5] | N/A | -1.55 | |
| 11 | DSC | | | |
| 12 | [1+2+3] ÷ [5+6] | N/A | 3.10 | |
| 13 | | | | |
| 14 | | | | |
| 15 | | | | |
| 16 | | | | |
| 17 | | | | |
| 18 | Short-term Debt | \$383,563 | \$449,249 | 30.8% 16.2% |
| 19 | | | | |
| 20 | Long-term Debt | | \$1,464,314 | 0.0% 52.7% |
| 21 | | | | |
| 22 | Common Equity | \$863,368 | \$863,368 | 69.2% 31.1% |
| 23 | | | | |
| 24 | Total Capital | \$1,246,931 | \$2,776,931 | 100.0% 100.0% |
| 25 | | | | |
| 26 | | | | |
| 27 | | | | |

MEMORANDUM

DATE: January 22, 2007

TO: Alexander Igwe
Executive Consultant III
Utilities Division

FROM: Jian W. Liu 
Utilities Engineer
Utilities Division

RE: Doney Park Water
Docket No. W-01416A-06-0719 (Financing)

Introduction

Doney Park Water (“Doney Park” or “the Company”) presently provides utility service to approximately 3,300 water customers near Flagstaff in Coconino County, Arizona. The Company is an Arizona nonprofit member-owned corporation providing water service in Township 21 North Ranges 8 and 9 East, Township 22 North Ranges 8 and 9 East and Township 23 North Range 8 East. Doney Park’s business office is located at 5290 E Northgate Loop, Flagstaff, Arizona 86004.

Financing Application

On November 13, 2006, the Company filed an application with the Arizona Corporation Commission (“Commission”) requesting authority to issue up to \$1.530 million in long-term indebtedness with the Industrial Development Authority of Coconino County (“IDA”).

The Company is planning to drill two new wells in order to meet existing and projected water demands. The purpose of this IDA financing is to pay the costs of drilling, equipping and interconnecting two new wells, including certain costs of securing financing.

Engineering Analysis

The existing water system consists of six wells producing approximately 1,675 gallons per minute (“GPM”) total capacity, and 22 storage tanks (total storage tank capacity is 4.497 million gallons). The Company’s growth projection is approximately 120 new service connections per year for the next five years.

Based on its typical system analysis using the most recent available water use data and current growth projections, Staff initially concluded that Doney Park's existing water system had adequate capacity and that the proposed wells may not be needed.

At the request of the Company, a meeting was held on December 22, 2006 and the Company explained to Staff its rationale for adding the wells. The plant facilities were visited on January 4, 2007 by Jian Liu, Staff Utilities Engineer, in the accompaniment of Bill Linville, the General Manager of the Doney Park.

Doney Park's Certificate of Convenience and Necessity covers approximately 44 square miles in rural Northern Arizona. There are 18 pump stations and 22 pressure zones for the water system. The Company provided information to Staff (January 10, 2007 letter) indicating that, over the last three years, the Company has had considerable problems maintaining pressure and tank levels during high demand times, primarily from Memorial Day through the Fourth of July. The Company sees a large influx of visitors from the Valley that come to visit family and friends and to escape the summer heat. This increase in demand also takes place during the high fire season. Doney Park's main storage tanks are located on U.S. Forest Service lands. The Company has agreed to provide the U.S. Forest Service with water for fighting wild fires. Doney Park has experienced numerous low pressure calls on weekends from its members/customers during high demand periods. The pressure problems and reduction in storage all occurred during normal operating conditions where the Company's existing wells were in full operation. The Company is concerned that in the event a well pump fails during a peak period a water shortage will occur.

Based on its investigation, Staff has concluded that Doney Park has a unique and complex water system and peak day demand placed on Doney Park's system is significantly greater than that of the typical water system. Accordingly, Staff revised its initial system analysis to account for the greater demand placed on the system during peak usage. In light of this, Staff supports the proposed well additions if the Company's financial condition supports approval of this financing application.

Cost Analysis

The Company's estimated cost for the proposed two new wells is as follows:

| | | | |
|-------------------------------------|-------------|------------|---------|
| Total Cost for one new well: | \$675,000 | | |
| Including: | Quantity | Unit Price | Total |
| Borehole Drilling(16-inch diameter) | 420 feet | \$300 | 126,000 |
| Borehole Drilling(12-inch diameter) | 1,560 feet | \$235 | 366,600 |
| Blank Casing | 2,000 feet | \$48 | 96,000 |
| Others | | | 86,400 |
| Total for two new wells: | \$1,350,000 | | |

Staff has reviewed the Company's estimates and concludes that they are reasonable. However, no "used and useful" determination of the proposed plant was made, and no particular future treatment should be inferred for rate making or rate base purposes.

Compliance

Arizona Department of Environmental Quality (ADEQ) Compliance

ADEQ has determined that this system has no deficiencies and is currently delivering water that meets the water quality standards required by the Arizona Administrative Code, Title 18, Chapter 4. (Report dated Nov 22, 05).

Arizona Corporation Commission (ACC) Compliance

According to the Utilities Division Compliance Section (Compliance Section Email dated December 8, 2006), the Company has no outstanding compliance issues with the ACC.

Conclusion

Staff concludes that the plant additions and their associated costs are reasonable and appropriate. However, no "used and useful" determination of the proposed plant was made, and no particular future treatment should be inferred for rate making or rate base purposes.

AFFIDAVIT/PROOF OF PUBLICATION

STATE OF ARIZONA

} ss.

County of Coconino

Bobbie Crosby being duly sworn, deposes and says:

That she is the legal clerk of the Arizona Daily Sun

a newspaper published at Flagstaff, Coconino County, Arizona; that the

legal 8760

a copy of which is

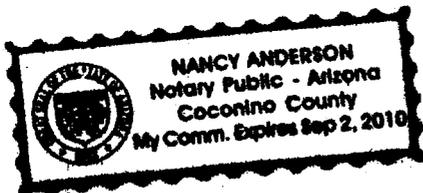
hereunto attached, was first published in said newspaper in its issue dated

the 2 day of December, 2006 and was

published in each one issue of said newspaper for one

consecutive day the last publication being in the issue dated the

2 day of December, 2006.



[Signature]

Subscribed and sworn to before me this

14 day of December, 2006

Nancy Anderson

[Signature]

Notary Public

My Commission expires 9-2-2010

OF AN APPLICATION FOR AN ORDER AUTHORIZING THE ISSUANCE OF DEBT BY DONEY PARK WATER

Doney Park Water (Applicant) filed an Application with the Arizona Corporation Commission (Commission) for an order authorizing Applicant to issue One Million Five Hundred Thirty Thousand Dollars (\$1,530,000.00) in debt to make improvements to its water distribution system, including the drilling of two (2) new wells. The application is available for inspection during regular business hours at the office of the Commission in Phoenix, Arizona, and the Company's offices at 5290 East Northgate Loop, Flagstaff, Arizona 86004-6204.

Intervention in the Commission's proceedings on the application shall be permitted to any person entitled by law to intervene and having a direct substantial interest in this matter. Persons desiring to intervene must file a Motion to Intervene and thirteen copies with the Commission's Docket Control at 1200 West Washington, Phoenix, Arizona and serve a copy upon the Applicant c/o William Sullivan, Curtis, Goodwin, Sullivan, Udall & Schwab, P.L.C., 2712 North 7th Street, Phoenix, Arizona 85006. The Motion to Intervene, at a minimum, shall contain the following information:

1. The name, address and telephone number of the proposed intervenor and of any person upon whom service of documents is to be made if different than the intervenor.
2. A short statement of the proposed intervenor's interest in the proceeding.
3. Whether the proposed intervenor desires a formal evidentiary hearing on the application and the reasons for such a hearing.
4. A statement certifying that a copy of the Motion to Intervene has been mailed to Applicant. The granting of Motions to Intervene shall be governed by A.A.C. R14-3-105, except that all Motions to Intervene must be filed on, or before, the 15th day after the date this notice is published.