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MEMORANDUM

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ORIGINAL

TO: Docket Control

FROM: Ernest G. Johnson
Director
for Utilities Division

DATE: November 9, 2007

RE: STAFF REPORT FOR WILHOIT WATER COMPANY, INC. – BLUE HILLS NO. 3's APPLICATION FOR A PERMANENT RATE INCREASE (DOCKET NO. W-02065A-07-0313)

Attached is the Staff Report for Wilhoit Water Company, Inc. – Blue Hills No. 3's application for a permanent rate increase. Staff recommends approval of the rate increase application using Staff's recommended rates and charges. Staff also recommends an arsenic remedial surcharge mechanism to address the removal of arsenic from the Company's water supply.

Any party who wishes may file comments to the Staff Report with the Commission's Docket Control by 4:00 p.m. on or before November 19, 2007.

EGJ:DRE:red

Originator: Darak R. Eaddy

Arizona Corporation Commission
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Service List for: Wilhoit Water Company, Inc. - Blue Hills No. 3
Docket No. W-02065A-07-0313

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STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION

WILHOIT WATER COMPANY, INC. -
BLUE HILLS NO. 3

DOCKET NO. W-02065A-07-0313

APPLICATION FOR A
PERMANENT RATE INCREASE

NOVEMBER 9, 2007

STAFF ACKNOWLEDGMENT

The Staff Report for Wilhoit Water Company, Inc. - Blue Hills No. 3, Docket No. W-02065A-07-0313, was the responsibility of the Staff members listed below. Darak R. Eaddy was responsible for the financial review and analysis of the Company's application, recommended revenue requirements, rate base and rate design. Marlin Scott, Jr. was responsible for the engineering and technical analysis. Guadalupe Ortiz was responsible for reviewing the Commission's records on customer complaints filed with the Commission.

Darak R. Eaddy

Darak R. Eaddy
Public Utility Analyst II

Marlin Scott

Marlin Scott, Jr.
Utilities Engineer

Guadalupe Ortiz

Guadalupe Ortiz
Public Utilities Consumer Analyst I

EXECUTIVE SUMMARY
WILHOIT WATER COMPANY, INC. - BLUE HILLS NO. 3
DOCKET NO. W-02065A-07-0313

Wilhoit Water Company, Inc. ("Wilhoit") is engaged in the business of providing potable water service to customers in Yavapai County. Wilhoit is composed of three independent water systems. The Blue Hills water system is located in the town of Dewey in Yavapai County, Arizona providing service to a certificated area of 1/32 square miles or 20 acres. The Thunderbird Meadows water system is located in Wilhoit, Arizona, and the Yavapai Estates system is located in Chino Valley, Arizona. The three Wilhoit water systems along with the Dells Water Company ("Dells") are all managed by the same parent company which is Glenarm Land Company.

Utilities Division Staff ("Staff") recommendations will only be presented for the Blue Hills Water System ("Blue Hills" or "Company") in this Report. Please see Staff's separately filed Reports for the other two Wilhoit systems and Dells. Blue Hills provides services to approximately 64 customers and its current rates were effective January 1, 1993, per Arizona Corporation Commission Decision No. 58102.

The Company proposes total operating revenue of $31,403[1], an increase of $13,945, or 79.88 percent over test year revenue of $17,458. Staff recommends total operating revenue of $26,242, an increase of $5,292, or 25.26 percent over the Staff-adjusted test year revenue of $20,950. The Company's proposed revenues result in an operating income of $3,308. Staff recommended revenues would result in an operating income of $3,968.

The Company has proposed an original cost rate base ("OCRB") of $1,250, and an operating margin of 10.53 percent. The Company claims that its proposed rate increase is necessary at this time to help pay for system maintenance as well as a modest return on the Company's investment. The Company's proposed rates would increase the typical residential bill with a median usage of 3,404 gallons from $18.04 to $32.64 for an increase of $14.60 or 80.9 percent.

Staff has recommended an OCRB of $5,108, and an operating margin of 15.12 percent. Staff's recommended rates would increase the typical residential bill with a median usage of 3,404 gallons from $18.04 to $22.82, an increase of $4.78 or 26.5 percent.

Blue Hills is not in compliance with Decision No. 58102, dated December 9, 1992, in which it was ordered to make arrangements with the appropriate taxing authorities to repay all accrued property taxes. Staff recommends that rates authorized in this case not become effective until the month subsequent to the Company filing in this docket a finalized plan (agreement with the Yavapai County Treasurer's Office) for payment of all of its delinquent property taxes owed on its utility property in Yavapai County.

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[1] The Company requested total operating revenue of $31,403 on page 6 of the application. However, the Company's proposed rates would actually produce $33,941 in revenues.

Currently the Company is not delivering water that meets the U.S. Environmental Protection Agency arsenic standards. The Company will need to procure funds for the engineering, construction, and installation of an arsenic treatment system. Because the Company lacks the funds to purchase an arsenic treatment system, Staff has recommended an arsenic remedial surcharge mechanism that will establish the methodology and conditions for setting an arsenic surcharge to provide such funds.

TABLE OF CONTENTS

SCHEDULES

ATTACHMENT

Fact sheet

Type of Ownership: Arizona "C" Corporation.

Location: The Company serves water customers in the town of Dewey in Yavapai County, Arizona.

Active Management Area: The Company is located in the Prescott Active Management Area.

Rates: Permanent rate increase application filed: May 21, 2007. The application became sufficient on September 10, 2007.

Current Rates: Decision No. 58102, December 9, 1992, with rates effective January 1, 1993.

Prior Test Year: December 31, 1990.

Current Test Year Ended: December 31, 2006.

Metered Rates:

	Company Current Rates	Company Proposed Rates	Staff Recommended Rates
Monthly Minimum Charge			
5/8 X ¾ – inch meter	$ 8.00	$ 10.00	$ 12.00
¾ – inch meter	$ 8.00	$ 10.00	$ 12.00
1 – inch meter	$ 18.00	$ 22.50	$ 30.00
1 - ½ – inch meter	$ 40.00	$ 50.00	$ 60.00
2 – inch meter	$ 64.00	$ 80.00	$ 96.00
3 – inch meter	$120.00	$ 150.00	$ 192.00
4 – inch meter	$200.00	$ 250.00	$ 300.00
5 – inch meter	$300.00	$ 375.00	$ 450.00
6 – inch meter	$400.00	$ 500.00	$ 600.00
Gallons in minimum	0	0	0
Tier One from 1 gallon to 6,000 gallons	$2.95	$6.65	
Tier Two all gallons over 6,000	$3.78	$9.30	
Tier One from 1 gallon to 3,000 gallons			$3.00
Tier Two from 3,001 gallons to 10,000 gallons			$4.50
Tier Three all gallons over 10,000			$5.40

Fact Sheet (Continued)

	Company Current Rates	Company Proposed Rates	Staff Recommended Rates
Typical residential bill:			
Average use (4,639 gallons)	$21.68	$40.85	$28.37
Median use (3,404 gallons)	$18.04	$32.64	$22.82

Customers:

Number of customers in prior test year (12/31/99): 46

Average Number of customers in the current test year (12/31/05): 64

Current test year customers by meter size:

5/8 X 3/4 – inch	64
3/4 – inch	0
1 – inch	0
1 1/2 – inch	0
2 – inch	0
4 – inch	0
6 – inch	0

Seasonal customers: N/A

Notifications:

An affidavit of mailing of the customer notification was docketed on June 19, 2007.

Number of opinions filed against the rate increase application: 0.

Number of customer complaints filed against the Company from January 1, 2004 to present: 5.

Percentage of complaints to customer base: 7.81 percent (5 / 64).

All complaints have been resolved and closed.

Summary of Filing

The test year results as adjusted by Utilities Division Staff ("Staff"), for Wilhoit Water Company, Inc. - Blue Hills No. 3 ("Blue Hills" or "Company") reflect total operating revenue of $20,950 and an operating loss of $324 for no operating margin as shown on Schedule DRE-1. The original cost rate base ("OCRB") as adjusted by Staff is $5,108.

Blue Hills' proposed rates, as requested, would produce total operating revenue of $31,403[2] and operating income of $3,308, or a 10.53 percent operating margin. The Company proposed OCRB is $1,250. The Company's proposed rates would increase the typical residential bill,[3] with a median usage of 3,404 gallons, from $18.04 to $32.64 for an increase of $14.60, or 80.9 percent as shown on Schedule DRE-5.

Staff recommends rates that would produce total operating revenue of $26,242 and operating income of $3,968, or a 15.12 percent operating margin. Staff recommends an OCRB of $5,108. Staff's recommended rates would increase the typical residential bill with a median usage of 3,404 gallons, from $18.04 to $22.82 for an increase of $4.78 or 26.5 percent as shown on Schedule DRE-5.

The Company is seeking a rate increase in order to acquire funds to aid in maintenance of its existing system. The Company is also seeking a modest return on its investment. The Company states in its application that it has not had a rate adjustment since 1992 and the costs to operate the water company have increased with inflation in the interim.

Blue Hills is located in the town of Dewey in Yavapai County, Arizona and covers a certificated area of approximately 1/32 square-miles or 20 acres.

During the test year ended December 31, 2006, Blue Hills provided potable water service to a total of 64 metered customers. All of the metered customers in the test year were served with 5/8 x 3/4-inch meters. The Company also operates a coin-operated standpipe.

The Company's water currently does not meet the Arizona Department of Environmental Quality's ("ADEQ") arsenic standards. The Company is seeking bids for the purchase of an arsenic treatment system to address the problem.

The Company utilized a test year ending December 31, 2006. The Company is registered as an Arizona "C" corporation with the Corporations Division of the Arizona Corporation Commission ("Commission").

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[2] The Company requested total operating revenue of $31,403 on page 6 of the application. However, the Company's proposed rates would actually produce $33,941 in revenues.

[3] 5/8 x 3/4 –inch meter.

Company Background

Blue Hills is a public utility corporation subject to the jurisdiction of the Commission. Blue Hills was granted a Certificate of Convenience and Necessity ("CC&N") in Decision No. 39691, effective October 24, 1968.

The Wilhoit Water Company, Inc. ("Wilhoit") is composed of three independent systems. Wilhoit is comprised of the Blue Hills system, the Thunderbird Meadows ("Thunderbird") water system located in Wilhoit, Arizona, and the Yavapai Mobile Home Estates ("Yavapai") system located in Chino Valley, Arizona. The three Wilhoit water systems along with the Dells Water Company ("Dells") are all managed by the same parent company which is Glenarm Land Company ("Glenarm").

The current rates have been in effect since January 1, 1993 per Decision No. 58102.

The Company has no advances in aid of construction or contributions in aid of construction.

The Company is located in the Prescott Active Management Area. Since the Company uses less than 250 acre-feet of water per year, it is considered a small provider by the Arizona Department of Water Resources and is not subject to the gallons per capita per day limit and conservation rules. The Company is only required to monitor and report water use.

On May 21, 2007, Blue Hills filed this application for a permanent rate increase.

Consumer Services

A review of the Consumer Services Section database from January 1, 2004, through October 1, 2007, revealed that there were no opinions filed opposing the rate increase request. The review revealed that in 2004 there was one complaint about the quality of service and no opinions or inquiries. In 2005, there were four complaints (three quality of service, one billing) and no opinions or inquiries. Finally, from 2006 to present, there have been no complaints, inquiries, or opinions. All complaints have been resolved and closed.

Compliance

Staff's review of the Decision No. 58102 and related Staff memorandums revealed several areas of non-compliance with previous Commission Orders. A discussion of each non-compliance issue is presented below:

Sale of Assets and Cancellation of a Portion of the Wilhoit Certificate of Convenience and Necessity ("CC&N") Docket No. W-02056A-03-0490

On July 16, 2003, in Docket No. W-02056A-03-0490, Wilhoit filed an application for approval of the sale of that portion of its assets used to serve the Glenarm Farms water system to the City of Avondale and to cancel that portion of its CC&N. The assets requested to be transferred were encumbered by Maricopa County tax liens at the time totaling approximately $215,000.

The application indicated that the sale was being entered into under threat of condemnation. A Staff Report filed October 6, 2003, recommended approval of the sale and that the Commission order Wilhoit to file evidence that the State of Arizona would be paid amounts to satisfy the outstanding personal property tax obligation before the close of escrow.

The City of Avondale argued that the delinquent tax would be extinguished upon the sale to the City of Avondale in its capacity as a subdivision of the state. Staff's closing brief, however, indicated that cities are required to pay delinquent property taxes attached to the property they acquire. At the time of the hearing on the matter, the City of Avondale was on record as already providing service to the customers in the Glenarm Farms area.

Following a hearing, a Proposed Order was issued on January 7, 2004, which recommended approval of the sale and cancellation of a portion of the CC&N subject to several conditions, one of which was the filing of evidence that the outstanding tax liens were satisfied before the close of escrow or 30 days from the Decision, whichever occurred first.

According to the Commission's records, Wilhoit requested that consideration of the Proposed Order be pulled from the Open Meeting agenda and it was. Wilhoit never subsequently requested that it be placed back on the agenda. On June 7, 2004, the Commission's Legal Division sent a letter to Mr. Douglas Martin who represented Wilhoit Water Company, requesting that the Company have the case placed on an Open Meeting agenda before December 31, 2004. There was no docketed response to the letter.

The sale and deletion docket remains open and Wilhoit is still the Company of record for this area on the Commission's maps and records. To facilitate the processing of the case, Staff sent a letter to the parties of record on September 13, 2006, requesting the following information:

1. Has the transaction been consummated? If so, on what date?
2. Please provide a copy of the executed sales agreement.
3. What are the parties intentions regarding the Proposed Order and the Commission's review and vote on this matter?
4. What is the status of the property tax delinquencies of Wilhoit Water Company relative to the area transferred to Avondale?

Staff did not receive any responses from any party and the letter to Wilhoit's attorney was returned as non-deliverable.

On June 21, 2007, in the course of the current rate cases, Staff sent Wilhoit a data request which included the four questions listed above. Wilhoit responded to that data request producing the sales agreement with the City of Avondale dated July 3, 2003. Wilhoit also represented that the sale was consummated on September 10, 2004, and that the attorney for the City of Avondale has been unable to resolve the tax issue.

The transfer case is now over four years old. Wilhoit's wells and pipe in the transfer area have been abandoned and are not included in the current rate requests. The City of Avondale is now directly serving the customers in the transfer area. Staff concludes that it would not be in the public interest to pursue or further process the sale of assets and CC&N cancellation for the Glenarm Farms area and recommends that the Commission administratively close Docket No. W-02056A-03-0490 and remove the appropriate area from Wilhoit's service territory as shown on the Commission's CC&N maps.

Prior Rate Case Docket No. W-02065A-90-005

In Decision No. 57237, dated February 14th, 1991, the Commission expressed concern over probable cross-subsidization among Wilhoit's water systems. Accordingly, Wilhoit was ordered to maintain separate records of revenues, expenses, and rate bases for each of its systems. In the following rate case (Docket No. W-02065A-92-0120), Wilhoit was in compliance with this recordkeeping provision of the Order. However, the Company is no longer in compliance, and it could not support separate expenses and rate bases for each of its systems in the current rate case. Wilhoit is out of compliance with the National Association of Regulatory Utility Commissioners ("NARUC") Uniform System of Accounts ("USOA").

Prior Rate Case Docket No. W-02065A-92-0120

Staff's review of a notice of legal action dated September 14, 1993, as filed by the Legal Division of the Commission revealed that there are several compliance items unresolved that arose from Decision No. 58102 dated December 9, 1992. Wilhoit was required to do the following:

a. Wilhoit Water Company, Inc. shall file copies with the Director of the Utilities Division of "paid-in-full" tax statements for current property tax payments within 90 days of the tax statement due date (Due 2/1/93).

b. Wilhoit Water Company, Inc. shall make arrangements with the appropriate taxing authorities to repay all accrued property tax and associated interest and to provide written summary to the Director of Utilities Division of the details of such arrangements/agreements (Due 6/9/93).

Wilhoit is not current on its property and sales tax payments. In addition, Wilhoit has delinquent taxes going back to the early 1990's. Copies of the amounts owed separated by water system from the Yavapai County Assessors' web site (dated October 23, 2007) are as follows:

Parcel No.	Company/Water System	Back Taxes Owed
907-60-190	The Dells Water Company	$ 6,316.40
929-92-340	Wilhoit Water Company Thunderbird Meadows	$39,661.22
929-92-290	Wilhoit Water Company Blue Hills #3	$ 6,746.51
929-95-120	Wilhoit Water Company Yavapai Mobile Home Estates	$26,735.81
929-95-131	Wilhoit Water Company Yavapai Mobile Home Estates	$ 154.13
Total Back Taxes Owed, as of October 23, 2007		$79,614.07

According to a response to a Staff data request, Wilhoit through its Attorney's Martin & Bell, L.L.C., contacted the Yavapai County Treasurer's Office. Martin & Bell submitted a memo to Staff stating that Ross Jacobs, the County Treasurer "indicated a desire to work with the water companies to pay the back taxes in a timely fashion and indicated that he would be open to abating, an as yet undefined portion of the penalties and interest, if a reasonable repayment plan could be fashioned."

Wilhoit's attorneys indicated to Mr. Jacobs "that the Company did not currently have the financial wherewithal to commit to a repayment schedule, but that if the current rate requests pending before the ACC were successful, Wilhoit and Dells would be prepared to enter into a repayment agreement."

As Wilhoit has not made good on past compliance requirements from the previous cases, and there is a pattern of the Company not paying taxes, Staff concludes that it is appropriate to defer the effective date for any new rates approved regarding any of the Wilhoit systems or Dells until the month subsequent to the date a copy of a final agreement between Wilhoit and the Yavapai County Treasurer's office regarding payment of delinquent taxes is filed in this docket.

Other Compliance Items

The Company is in good standing with the Corporations Division of the Commission as of October 1, 2007.

Engineering

The water system was field inspected on September 17, 2007, by Marlin Scott, Jr., Staff Utilities Engineer, in the accompaniment of Jim West, consultant for the Company. A complete discussion of Staff's technical findings and recommendations and a complete description of the water system are provided in the attached Engineering Report.

Arsenic

According to the ADEQ Monitoring Assistance Program analysis report for 2007, the Company's composite arsenic level from its two wells was reported at 18 parts per billion ("ppb"). Based on this arsenic level, the Company indicated it is currently seeking bids for the engineering, construction, and installation of an arsenic treatment system.

Rate Base

Staff's adjustments increased the Company's proposed rate base by $3,858 from $1,250 to $5,108 as shown on Schedule DRE-2, page 1. Details of Staff's adjustments are discussed below.

Plant in Service

Staff's adjustments to plant in service resulted in a net increase of $1,638, from $44,186 to $45,824 as shown on Schedule DRE-2, page 2.

Structures & Improvements – Adjustment A increases the structures and improvements account by $1,638, from $1,200 to $2,838 as shown on Schedule DRE-2, pages 2 and 3. Staff's adjusted amount reflects the capitalization of the cost of a fence put around a water tank.

Accumulated Depreciation

Staff increased accumulated depreciation by $41 from $42,936 to $42,977 as shown on Schedule DRE-2, page 3. The increase is based upon the adjustment Staff made to plant in service and the addition of a half year of depreciation expense relating to this plant addition to the accumulated depreciation account.

Working Capital

Staff's adjustments to working capital resulted in a net increase of $2,261, from $0 to $2,261 as shown on Schedule DRE-2, pages 1 and 5, as a result of increasing cash working capital.

Cash working capital was calculated by using the formula method which equals one-eighth of the operating expenses less depreciation, taxes, purchased power and purchased water expenses, plus one twenty-fourth of purchased power and purchased water expenses.

Operating Income Statement

Operating Revenue

Staff adjustment to operating revenue resulted in an increase of $3,492 from $17,458 to $20,950 as shown on Schedule DRE-3, page 1.

Staff's adjustment relates to the revenues of the coin-operated standpipe that the Company operates. Despite several requests for the test year revenues of the standpipe, the Company was unable to provide Staff with any information on the operations of the standpipe. Because the Company does not possess any accurate figures for total water pumped during the test year, Staff is unable to compute standpipe sales in this alternative method as well. Additionally, the Company stated that the only Company representative able to supply any operational or financial information on the standpipe was Company owner Robert Conlin, who has since passed away.

Because these non-metered revenues are essential to Staff's ability to set rates for the Company's requested rate increase and because the Company is unable to provide Staff with any operational or financial information on these revenues; Staff has imputed non-metered revenues for the Company at 20 percent of the Company's metered revenues. This amounts to the $3,492 adjustment Staff made to the Company's total operating revenue.

The 20 percent rate was chosen by Staff for several reasons. First, the area in which the Company operates is very rural which increases the likelihood there is a segment of the population that do not connect directly into any water system and instead depend on standpipes and bulk water for their water usage. Second, the Company's certificated area is one in which there is a significant livestock presence which again would increase the likelihood of the usage of bulk water. Finally, Staff, based on its analysis of the Company's system and the area, believes that the 20 percent standpipe-to-metered revenue rate is reasonable and can be supported by the Company's current water system.

Operating Expenses

As previously mentioned in the Compliance section of this report, Wilhoit did not maintain records to separately identify expenses for its individual water systems. As a result identifying the expenses directly attributable to the individual Wilhoit systems or Dells could not be achieved. In an attempt to overcome this recordkeeping deficiency, Glenarm allocated certain expenses among its systems using the following percentages: Thunderbird, 45 percent; Yavapai, 35 percent; Blue Hills, 20 percent; and Dells, 0 percent. According to Glenarm, these allocation factors represent relative customer counts for the systems at an unspecified historical date.

Staff developed an alternate allocation factor for allocating expenses that could not be directly attributed to one of the Wilhoit systems or Dells since the customer counts used by Wilhoit are stale and because in some instances customer count is not the preferred allocation basis. Staff's customer based allocation factors by water system are as follows: Thunderbird, 34.69 percent; Yavapai, 29.81 percent; Blue Hills, 17.34 percent; and Dells 18.16 percent.

Staff adjustment to operating expenses resulted in a decrease of $6,822 from $28,095 to $21,274 as shown on Schedule DRE-3 page 1. The adjustments are explained below.

Salaries and Wages – Adjustment B decreased salaries and wages by $2,106 from $9,778 to $7,672 as shown on Schedule DRE-3, pages 1 and 2. Wilhoit's total salary and wage expense for the test year for the three Wilhoit companies and Dells amounted to $44,231. Staff's adjustment reflects the allocation methodology that Staff utilized.

Repairs and Maintenance Expense – Adjustment C decreases repairs and maintenance by $2,358 from $7,133 to $4,775 as shown on Schedule DRE-3, pages 1 and 3. The Company's repairs and maintenance expense is composed of $4,465 in costs directly assignable to Blue Hills and $310 for Blue Hills' allocated portion of shared repairs and maintenance (mostly small items not directly linked to any one of the water companies). Staff's adjustment reflects the allocation methodology that Staff utilized.

Office Supplies and Expenses – Adjustment D decreases office supplies and expenses by $252, from $703 to $451 as shown on Schedule DRE-3, pages 1 and 4. The Company's office supplies and expense is composed of $315 in postage costs directly assignable to Blue Hills and $136 for Blue Hills' allocated portion of shared office expenses (such as ink cartridges, envelopes, tape, pens, etc.). Because the Company did not maintain any records for office supplies and expenses for the test year, Staff computed a reasonable expense for office supplies and expenses. Staff's adjustment reflects the allocation methodology that Staff utilized.

Outside Services – Adjustment E increases outside services expense by $408, from $0 to $408 as shown on Schedule DRE-3, pages 1 and 5. Staff moved costs submitted by the Company as water testing cost, which should have been recorded as outside services, as this portion of the submitted water testing costs were performed by outside companies.

Water Testing – Adjustment F decreases water testing by $408 from $1,853 to $1,445 as shown on Schedule DRE-3, pages 1 and 5. This adjustment reflects Staff's shifting some costs that should have been recorded as outside services from this account, and the normalized annual water testing costs determined by Staff and reported in the attached Engineering Report.

Rents Expense – Adjustment G increases rents expense by $250, from $1,400 to $1,650 as shown on Schedule DRE-3, pages 1 and 5. The Company stated in response to a data request that the combined rents expense for the four water companies was $6,600. Staff's adjustment reflects the use of a four-way split amongst the four companies. 25 percent of the combined rents expense for the companies was allocated to Blue Hills.

General Liability Insurance Expense – Adjustment H decreases general liability insurance expense by $87, from $661 to $574 as shown on Schedule DRE-3, pages 1, and 5. The Company provided a 2006 insurance policy that covered the four water companies with a $3,307 annual premium. Staff's adjustment reflects the allocation methodology that Staff utilized.

Miscellaneous Expense – Adjustment I decreases miscellaneous expense by $2,073, from $2,173 to $100 as shown on Schedule DRE-3, pages 1, and 6. Staff allocated shared miscellaneous expenses of $399 amongst the four water companies by utilizing the number of customers for each water company. Staff disallowed $2,073 in directly assignable miscellaneous expenses as the Company could provide no invoices for the claimed expenses. Staff noted that miscellaneous expense for the year prior to the test year only amounted to $292.

Depreciation Expense – Adjustment J increases depreciation expense by $55, from $0 to $55 as shown on Schedule DRE-3, pages 1, and 7. This adjustment reflects Staff's calculation of depreciation expense on the capitalized cost of a fence installed around a water tank applying Staff's recommended depreciation rates to Staff's recommended plant balances for Blue Hills.

Taxes Other Than Income Expense – Staff's Adjustment K decreases taxes other than income expense by $1,355, from $1,355 to $0 as shown on Schedule DRE-3, pages 1, and 8. This adjustment reflects Staff's removal of $1,355 identified as sales tax expense in account number 770.20 of the Company's general ledger. These sales taxes were paid to the Arizona Department of Revenue and should be removed from expenses, since the corresponding collected taxes were removed from revenue.

Property Taxes – Staff's Adjustment L increases property taxes by $1,055, from $0 to $1055 as shown on Schedule DRE-3, pages 1, and 8. This adjustment reflects the property taxes for the 2006 test year.

Income Tax – Staff's Adjustment M increases interest expense by $50, from $0 to $50 as shown on Schedule DRE-3, pages 1, and 8. This adjustment reflects Staff's computation of income tax expense given Staff's adjustments to operating revenue and operating expenses.

Operating Margin

The Company's proposed rates and charges would provide an operating income of $3,308 for an operating margin of 10.53 percent.

Staff's recommended rates and charges would provide an operating income of $3,968 for an operating margin of 15.12 percent.

Revenue Requirement

Staff recommends total operating revenue of $26,242, an increase of $5,292, or 25.26 percent above Staff's adjusted test year revenue of $20,950. Staff's recommended revenue provides operating income of $3,968 for an operating margin of 15.12 percent as shown on Schedule DRE-1.

Staff was unable to derive the revenue requirement by applying a rate of return on rate base because the Company's extremely low rate base did not produce sufficient revenues for the Company's operating needs. Therefore, Staff derived revenue requirement by use of an operating margin percentage.

Operating margin represents the proportion of funds available to pay debt service and other below the line expenses.[4] A 15.12 percent operating margin provides ample funds to manage contingencies, operating expenses, below the line expenses, etc.

Rate Design

Schedule DRE-4 presents a complete list of the Company's present, proposed, and Staff's recommended rates and charges.

The Company's present monthly customer charges vary by meter size as follows: 5/8 - 3/4 inch $8.00; 3/4-inch, $8.00; 1-inch, $18.00; 1½-inch, $40.00; 2-inch, $64.00; 3-inch, $120.00; 4-inch, $200.00; 5-inch, $300.00; and 6-inch, $400.00. No gallons are included in the minimum. The present commodity rate is $2.95 per thousand gallons of usage up to 6,000 gallons of usage; and $3.78 per thousand gallons of usage above 6,000 gallons.

The Company has requested an inverted two-tier rate structure with a break-over point at 6,000 gallons. Staff recommends an inverted three-tier rate structure with break-over points at 3,000 and 10,000 gallons. Staff recommends three tiers rather than two because it encourages efficient water usage by assigning higher costs to customers within the same customer class who use more than the average.

The Company's proposed rates would increase the typical residential bill with a median usage of 3,404 gallons from $18.04 to $32.64 for an increase of $14.60 or 80.9 percent.

Staff's recommended rates would increase the typical residential bill with a median usage of 3,404 gallons from $18.04 to $22.82 for an increase of $4.78 or 26.5 percent.

Standpipe Service

The Company is currently operating a standpipe although it does not have a tariff rate for such a service. Typically companies without tariff rates for bulk water charge its highest tier rate for the service. For Blue Hills this would be $3.78 per thousand gallons of usage however, Staff discovered in its audit that the Company was charging a rate of $5.00 per thousand gallons of usage. In addition, the Company's record-keeping of the standpipe operations was found to be

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[4]Operating margin is calculated by dividing operating income by total operating revenue.

very lacking with little internal control over funds collected and non-existent accounting for its operations. Staff recommends a $5.40 rate which is consistent with Staff's third tier rate. Staff further recommends that the Company file with Docket Control, as a compliance item in this docket, the monthly revenues from its standpipe service. Staff recommends that this filing be done on a quarterly basis beginning 90 days after the decision in the current rate increase application and should continue until further notice from the Commission. Staff further recommends the Company maintain records of its standpipe service operations in compliance with the NARUC USOA.

Miscellaneous Service Charges

The Company has proposed increases to its establishment, reconnection, meter test (if correct), NSF check, meter re-read, and late fees. Staff notes that any increase in miscellaneous service charges recommended by Staff will have no effect on Staff's total annual operating revenue. This is because Staff offsets any increase in miscellaneous service charges with an equal decrease in metered revenue.

For all the service charges the Company proposes to increase, the Company only had one delinquent reconnection and one NSF check for the 2006 test year. In addition Staff reviewed the miscellaneous service charges in question and found that for most of the service charges, the current rates are within the range of service charges typically approved by the Commission. Therefore, Staff only recommends an increase in the NSF check fee to $30.00 and that there be no increase for all other proposed service charge increases. Staff also recommends the Company's late fee be 1.5 percent of the unpaid monthly balance.

Service Line and Meter Installation Charges

Staff recommends approval of Staff's Service Line and Meter Installation Charges as shown on Table C in Section H of the attached Staff Engineering Report.

For monthly service charges for fire sprinklers, Staff recommends charges that are consistent with other water companies' tariffs.

Arsenic Remedial Surcharge Mechanism ("ARSM")

Introduction

Currently the Company is not delivering water that meets the U.S. Environmental Protection Agency ("EPA") arsenic standards. The EPA has reduced the arsenic maximum contaminant level in drinking water from 50 ppb to 10 ppb. According to the ADEQ Monitoring Assistance Program analysis report for 2007, the Company's composite arsenic level from its two wells was reported at 18 ppb.

Purpose and Terms of the ARSM

The Company will need funds for the engineering, construction, and installation of an arsenic treatment system. However, the Company does not currently have a definitive dollar amount for the treatment system, nor will it have an exact amount before the final processing of this rate increase application.

Staff has determined a reasonable estimate of the cost of an arsenic treatment system for Blue Hills to be $40,000. Staff recommends the Company contact the Water Infrastructure and Finance Authority of Arizona ("WIFA") and begin the process to secure a WIFA loan to purchase the treatment system. Although the final total loan amount may differ, Staff recommends a WIFA loan up to the total of $40,000 for an arsenic treatment system.

Because the final costs of the treatment system and the final details of the WIFA loan will not be known until after the final processing of this rate increase application, Staff is recommending an arsenic remedial surcharge mechanism ("ARSM") for the Company. An ARSM is appropriate because the Company currently has an arsenic problem with its drinking water, and because of the Company's size and limited current financial situation, it does not have access to other funding sources to correct the arsenic problem.

The ARSM will establish the methodology that will detail how the surcharge to provide funds for the debt service on the WIFA loan will be calculated and applied to the rates established in this rate increase application. Once Blue Hills has a definitive loan amount and other loan covenants, the Company can submit an arsenic removal surcharge application to the Commission in order to receive the surcharge using the methodology Staff has defined in this Report.

Engineering Analysis of the ARSM

A field inspection of the Blue Hills water system was conducted on September 17, 2007. Staff has determined that Blue Hills is in need of an arsenic treatment system for its water system.

Financial Analysis

Staff's analysis is based on Staff's recommended rates and the Company's financial statements dated December 31, 2006. The financial analysis shown on Schedule DRE-6 presents selected financial information from the financial statements and the pro forma effect of a hypothetical $40,000 WIFA loan.

Schedule DRE-6 also shows the capital structure and ratios for debt service coverage ("DSC") and times interest earned ratio ("TIER"). DSC represents the number of times internally generated cash (i.e., earnings before interest, income tax, depreciation, and amortization expenses) covers required principle and interest payments on debt. A DSC greater than 1.0 means operating cash flow is sufficient to cover debt obligations. TIER represents the number of times earnings before income tax expense covers interest expense on 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.

Schedule DRE-6, column B, shows that the pro forma effect on the Company's financial ratios of obtaining a hypothetical $40,000 loan at an interest rate of 8.0 percent and implementation of Staff's recommended permanent rates is to produce a TIER of 2.92 and a DSC of 2.32. These ratios indicate that Blue Hills would have sufficient earnings and operating cash flow to meet the long-term debt obligations of a $40,000 loan.

Additional Surcharge Revenue Required to Preserve Cash Flow

The Company must comply with the EPA arsenic drinking water standard regardless of its financial position. Accordingly, Staff calculated the additional annual revenue that Blue Hills would require (given adoption of Staff's recommended permanent rates) to meet its obligations on a hypothetical $40,000 loan, and provide the Company with the same amount of cash flow it would have had before the loan. As shown on Schedule DRE-7, on a hypothetical $40,000 WIFA loan, the Company would need an additional $845 for principal, $3,169 for interest expense, and $224 for income taxes on the additional revenue for a total of $4,239.

Calculation of Surcharge

The following is the methodology that Staff recommends to calculate the arsenic surcharge the Company would receive to provide funds for the debt service on the loan the Company will need to purchase an arsenic treatment system. For illustrative purposes, Staff utilized the previously mentioned hypothetical $40,000 WIFA Loan applied to its methodology to calculate the arsenic surcharge. Schedule DRE-8 also shows Staff's calculation of the Company's arsenic surcharge with the previously mentioned $40,000 hypothetical WIFA loan.

Staff recommends the following steps to calculate the arsenic surcharge once the Company has a definitive loan amount and other covenants secured.

Example - For Illustrative Purposes Only

Loan amount: $40,000
Term: 20 years
Stated Annual Interest Rate: 8.00%

Step 1. <u>Find the Annual Payment on the Loan</u>

Refer to Table A, the Conversion Factor Table. Reading the table from top to bottom, find the interest rate in Column A that is equal to the stated annual interest rate of the loan. Reading across the table, find the Annual Payment Conversion Factor in Column B that corresponds with the loan interest rate (in the event that the loan interest rate is different from the interest rates in Table A, use the next higher interest rate that can be found in Table A). Multiply that annual payment conversion factor by the total amount of the loan to calculate the annual debt service on the loan.

Result

0.10037	Annual payment conversion factor
x $ 40,000	(*) Times total amount of the loan
$ 4,015	(=) Equals annual debt service on the loan (rounded)

Step 2. Find the Annual Interest Payment on the Loan

Refer to Table A and find the annual interest payment conversion factor in Column C that corresponds with the stated annual interest rate of the loan. Multiply the annual interest payment conversion factor by the total amount of the loan to calculate the annual interest expense on the loan.

Result

0.07924	Annual interest payment conversion factor
x $ 40,000	(*) Times total amount of the loan
$ 3,169	(=) Equals annual interest expense on the loan (rounded)

Step 3. Find the Annual Principal Payment on the Loan

Refer to Table A and find the annual principal payment conversion factor in Column D that corresponds with the stated annual interest rate of the loan. Multiply the annual principal payment conversion factor by the total amount of the loan to calculate the annual principal payment on the loan.

Result

0.02114	Annual principal payment conversion factor
x $ 40,000	(*) Times total amount of the loan
$ 846	(=) Equals annual principal payment on the loan

Step 4. Find the Gross Revenue Conversion Factor (GRCF)

The GRCF calculated below is used in step 5.

$$\text{GRCF} = \frac{1}{\text{1- Effective incremental income tax rate}}$$

$$\text{CRCF} = \frac{1}{1 - 0.2092} = \frac{1}{0.7907} = 1.2646$$

Step 5. Find the Incremental Income Tax Factor

The incremental income tax factor is calculated below:

$$\begin{aligned}\text{Incremental Income Tax Factor} &= \text{GRCF} - 1 \\ &= 1.2646 - 1 \\ &= 0.2646\end{aligned}$$

Step 6. Find the Annual Income Tax Component of the Surcharge Revenue

Multiply the incremental income tax factor by the annual principal payment on the loan determined in step 3 to calculate the income tax component of the annual surcharge revenue.

Result

0.2646	Incremental income tax conversion factor
x $ 846	(*) Times the annual principal payment on the loan
$ 224	(=) Equals the annual income tax component of the annual surcharge revenue

Step 7. Find the Debt Service Component of the Annual Surcharge Revenue

Add the annual interest expense on the loan determined in step 2 to the annual principal payment determined in step 3. The sum is the debt service component of the annual surcharge revenue.

Result

$ 3,169	Annual interest payment on the loan (Step 2)
+ $ 846	(+) Plus annual principal payment (Step 3)
$ 4,015	(=) Equals the debt service component of the annual surcharge revenue

Step 8. Find the Total Annual Surcharge Revenue Requirement Needed for the Loan.

Add the annual income tax component determined in step 6 to the annual debt service component determined in step 7. The sum equals the annual surcharge revenue requirement for the loan.

Result

$ 224	Annual income tax component (Step 6)
+ $ 4,015	(+) Plus annual principal payment (Step 7)
$ 4,239	(=) Equals the total annual surcharge revenue requirement for the loan.

Step 9. Find the equivalent bills.

Multiply the NARUC meter capacity multiplier by the number of current customers and by the number of months per year. The sum of the products equals the equivalent bills.

Result

Col A	Col B	Col C	Col D	Col E
Meter Size	NARUC Meter Capacity Multiplier	Number of Customers	Number of Months in Year	Equivalents Bills Col B x C x D
5/8"x 3/4" Meter	1	64	12	768
3/4" Meter	1.5	0	12	0
1" Meter	2.5	0	12	0
1½" Meter	5	0	12	0
2" Meter	8	0	12	0
3" Meter	15	0	12	0
4" Meter	25	0	12	0
6" Meter	50	0	12	0
			Total	768

Step 10. Find the monthly surcharge for 5/8" x 3/4" customers.

Divide the result obtained in step 8 by the number of equivalent bills calculated in step 9 to obtain the monthly surcharge for 5/8" x 3/4" customers.

Result

$ 4,239	Total annual surcharge revenue requirement for the loan (Step 8)
÷ 768	Number of equivalent bills (Step 9)
$ 5.52	(=) Equals the total annual surcharge revenue requirement for the loan (rounded).

Step 11. Find the monthly surcharge for the remaining meter size customers.

Multiply the result obtained in step 10 by the NARUC meter capacity multipliers to obtain the monthly surcharge for all other meter sizes.

Col A	Col B	Col C	Col D	
Meter Size	NARUC Meter Capacity Multiplier	5/8" x 3/4" Customer Surcharge	Surcharge by Meter Size Col B X C	
5/8"x 3/4" Meter	1	5.52	$	5.52
3/4" Meter	1.5	5.52	$	8.28
1" Meter	2.5	5.52	$	13.80
1½" Meter	5	5.52	$	27.60
2" Meter	8	5.52	$	44.15
3" Meter	15	5.52	$	82.79
4" Meter	25	5.52	$	137.98
6" Meter	50	5.52	$	275.95

TABLE A
Conversion Factor Table (Based on a 20-year Loan)

Column A Annual Interest	Column B Annual Payment Conversion Factor	Column C Annual Interest Payment Conversion Factor	Column D Annual Principal Payment Conversion Factor
3.50%	0.0696	0.0344	0.0352
3.75%	0.0711	0.0369	0.0342
4.00%	0.0727	0.0394	0.0333
4.25%	0.0743	0.0419	0.0324
4.50%	0.0759	0.0444	0.0316
4.75%	0.0775	0.0468	0.0307
5.00%	0.0792	0.0493	0.0299
5.25%	0.0809	0.0518	0.0291
5.50%	0.0825	0.0543	0.0283
5.75%	0.0843	0.0568	0.0275
6.00%	0.0860	0.0593	0.0267
6.25%	0.0877	0.0618	0.0259
6.50%	0.0895	0.0643	0.0252
6.75%	0.0912	0.0668	0.0245
7.00%	0.0930	0.0692	0.0238
7.25%	0.0948	0.0717	0.0231
7.50%	0.0967	0.0742	0.0224
7.75%	0.0985	0.0767	0.0218
8.00%	0.1004	0.0792	0.0211

Typical Bill Analysis

Schedule DRE-9, which is similar to Schedule DRE-5, shows the effect of the potential arsenic surcharge on the typical 5/8 inch residential customer's bill. Bear in mind that the arsenic surcharge amount is added to Staff's already recommended monthly minimum increase for 5/8 inch residential customers of $12.00 as shown in Schedule DRE-5.

The arsenic surcharge that Staff calculated using a hypothetical $40,000 WIFA loan would increase the typical residential bill with a median usage of 3,404 gallons from $18.04 to $28.34 for an increase of $10.30 or 57.1 percent.

Conclusion

Staff concludes that the construction of an arsenic treatment system is necessary for Blue Hills to comply with the EPA's revised drinking water standard that requires reducing the arsenic level in drinking water to 10 ppb.

Staff further concludes that the Company will need a WIFA loan up to the total of $40,000 to purchase an arsenic treatment system to comply with the EPA revised drinking water standard.

Staff Recommendations

Staff recommends approval of the Staff proposed rates and charges as shown in Schedule DRE-4. In addition to collection of its regular rates and charges, the Company may collect from its customers a proportionate share of any privilege, sales, or use tax as provided for in A.A.C. R14-2-409.D.

Staff further recommends that the Company be ordered to file with Docket Control a tariff schedule of its new rates and charges within 30 days after the effective date of the Decision in this proceeding.

Staff further recommends that Blue Hills adopt Staff's allocation methodology for shared expenses.

Staff further recommends that the Commission administratively close Docket No. W-02056A-03-0490 and remove the appropriate area from Wilhoit's service territory as shown on the Commission's CC&N maps.

Staff further recommends that Wilhoit, be ordered to maintain separate revenues, expenses, and rate bases for each of the Wilhoit water systems and Dells, and additionally provide separate balance sheets for each water system, and as a compliance item in this docket, file separate annual reports with the Commission.

Staff further recommends that any new rates approved in this Docket not go into effect until after an agreement between Wilhoit and the Yavapai County Treasurer's office is executed for payment of all its delinquent property taxes on its utility property in Yavapai County and filed with Docket Control.

Staff further recommends that the Company begin using depreciation rates by individual NARUC category as delineated on Table B in Section G of the attached Engineering Report.

Staff further recommends that the Company monitor its system and submit the gallons pumped and sold to determine the actual water loss for one full year. The results of this monitoring and reporting should be docketed as a compliance item in this case within 13 months of the effective date of the order issued in this proceeding. If the reported water loss for the period is greater than 10 percent, the Company shall prepare a report containing a detailed analysis and plan to reduce water loss to 10 percent or less. If the Company believes it is not cost effective to reduce water loss to less than 10 percent, it should submit a detailed cost benefit analysis to support its opinion. In no case shall the Company allow water loss to be greater than 15 percent. The water loss reduction report or the detailed analysis, whichever is submitted, shall be docketed as a compliance item within 13 months of the effective date of the order issued in this proceeding.

Staff further recommends that Wilhoit be required to report its customer count by system in future submittals of its Commission Annual Reports.

Staff further recommends that the Company file with Docket Control, as a compliance item in this docket by December 31, 2008, a letter from Arizona Department of Water Resources indicating that the Company's water use and monitoring requirements have been resolved.

Staff further recommends approval of Staff's Service Line and Meter Installation Charges as delineated in Table C in Section H of the attached Engineering Report.

Staff further recommends that the Company file a curtailment tariff in the form found on the Commission's website at www.azcc.gov/divisions/utilities/forms/Curtailment-Std.pdf. This tariff shall be docketed as a compliance item in this case within 45 days of the effective date of an order in this proceeding for review and certification by Staff.

Staff further recommends that the Company file with Docket Control, as a compliance item in this docket, the monthly revenues from its standpipe service. Staff recommends that this filing be done on a quarterly basis beginning 90 days after the Decision in the current rate increase application and should continue until further notice from the Commission.

Staff further recommends the Company maintain records of its standpipe service operations in compliance with the NARUC USOA.

Staff further recommends Blue Hills be authorized to incur long-term debt in the form of a WIFA loan up to the amount of $40,000. Staff makes this recommendation with the understanding that the Commission will subsequently also consider an arsenic removal surcharge to enable the Company to meet its principal and interest obligations on the WIFA loan, and incremental income taxes on the surcharge.

Staff further recommends that Blue Hills file before the Commission an arsenic removal surcharge tariff application that would enable the Company to meet its principal and interest obligations on the WIFA loan, and income taxes on the surcharge.

Staff further recommends that the Company follow the same methodology presented in this Report and as shown in Schedules DRE-6, DRE-7, and DRE-8 to calculate the additional revenue needed to meet its interest, principal, and additional income tax obligations on the WIFA loan using actual loan amounts and use the result to develop its arsenic removal surcharge tariff application. The increase in revenue calculation should be included in the arsenic removal surcharge tariff application.

Staff further recommends ordering Blue Hills to file with Docket Control copies of its calculation of revenue requirement for principal and interest obligations on the WIFA loan and incremental income taxes on the surcharge within 60 days after the loan agreement is signed by both WIFA and the Company.

Staff further recommends ordering Blue Hills to file with Docket Control copies of all executed financing documents within 60 days after the loan agreement is signed.

Staff further recommends that all of the Wilhoit systems and Dells be ordered to file rate cases within five years of the effective date of this Decision.

Staff further recommends that the Company submit the ADEQ Certificate of Approval of Construction for the arsenic treatment system by December 31, 2008.

Staff further recommends authorizing the Company to execute any documents necessary to effectuate the authorizations granted.

Wilhoit Water Company, Inc. - Blue Hills #3
Docket No. W-02065A-07-0313
Test Year Ended: December 31, 2006

Schedule DRE-1

SUMMARY OF FILING

	-- Present Rates --		-- Proposed Rates --	
	Company as Filed	Staff as Adjusted	Company as Filed	Staff as Adjusted
Revenues:				
Metered Water Revenue	$17,458	$17,458	$31,403	$22,750
Unmetered Water Revenue	0	3,492	0	3,492
Other Water Revenues	0	0	0	0
Total Operating Revenue	$17,458	**$20,950**	$31,403	**$26,242**
Operating Expenses:				
Operation and Maintenance	$26,740	$20,114	$26,740	$20,114
Depreciation	0	55	0	55
Property & Other Taxes	1,355	1,055	1,355	1,055
Income Tax	0	50	0	1,050
Total Operating Expense	$28,095	**$21,274**	$28,095	**$22,273**
Operating Income/(Loss)	($10,637)	**($324)**	$3,308	**$3,968**
Rate Base O.C.L.D.	$1,250	$5,108	$1,250	$5,108
Rate of Return - O.C.L.D.	N/M	N/M	264.67%	77.69%
Operating Margin	N/M	N/M	10.53%	15.12%

NOTE: 1. Operating Margin represents the proportion of funds available to pay interest and other below the line or non-ratemaking expenses

Wilhoit Water Company, Inc. - Blue Hills #3
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RATE BASE

	---------- Original Cost ----------			
	Company	Adjustment		Staff
Plant in Service	$44,186	$1,638	A	$45,824
Less:				
Accum. Depreciation	42,936	41	B	42,977
Net Plant	$1,250	$1,597		**$2,847**
Less:				
Plant Advances	$0	$0		$0
Accumulated Deferred Income Taxes	0	0		0
Total Advances	$0	$0		$0
Contributions Gross	$0	$0		$0
Less:				
Amortization of CIAC	0	0		0
Net CIAC	$0	$0		$0
Total Deductions	$0	$0		**$0**
Plus:				
1/24 Power	$0	$127	C	$127
1/8 Operation & Maint.	0	2,134	D	2,134
Inventory	0	0		0
Prepayments	0	0		0
Total Additions	$0	$2,261		**$2,261**
Rate Base	**$1,250**	**$3,858**		**$5,108**

Explanation of Adjustment:
- A - See Schedule 2, Page 2, a
- B - See Schedule 2, Page 5
- C - See Schedule 2, Page 6
- D - See Schedule 2, Page 6

Wilhoit Water Company, Inc. - Blue Hills #3
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PLANT ADJUSTMENT

	Company Exhibit	Adjustment		Staff Adjusted
301 Organization	$0	$0		$0
302 Franchises	0	0		0
303 Land & Land Rights	1,250	0		1,250
304 Structures & Improvements	1,200	1,638	A	2,838
307 Wells & Springs	4,238	0		4,238
311 Pumping Equipment	11,927	0		11,927
320 Water Treatment Equipment	609	0		609
330 Distribution Reservoirs & Stan	2,843	0		2,843
331 Transmission & Distribution M	14,296	0		14,296
333 Services	4,309	0		4,309
334 Meters & Meter Installations	3,421	0		3,421
335 Hydrants	0	0		0
336 Backflow Prevention Devices	0	0		0
339 Other Plant and Misc. Equipm	0	0		0
340 Office Furniture & Equipment	91	0		91
341 Transportation Equipment	0	0		0
343 Tools Shop & Garage Equipm	0	0		0
344 Laboratory Equipment	0	0		0
345 Power Operated Equipment	0	0		0
346 Communication Equipment	0	0		0
347 Miscellaneous Equipment	0	0		0
348 Other Tangible Plant	0	0		0
105 C.W.I.P.	0	0		0
TOTALS	$44,186	$1,638		**$45,824**

Explanation of Adjustment:
a - See Schedule 2, Page 3

Wilhoit Water Company, Inc. - Blue Hills #3
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STAFF PLANT ADJUSTMENTS

A -	STRUCTURES & IMPROVEMENTS - Per Company	$1,200	
	Per Staff	2,838	$1,638

To properly reflect account
provided in response to a data request as follows:

In 2006, the Company put a fence around a water tank that the Company expensed in its rate application, Staff has capitalized this cost

$	1,200	Ending balance in last rate case
$	1,638	2006 Capitalization of installation of fence around water tank
$	2,838	Staff Account Balance

ACCUMULATED DEPRECIATION ADJUSTMENT

	Amount	
Accumulated Depreciation - Per Company	$42,936	
Accumulated Depreciation - Per Staff	42,977	B
Total Adjustment	**$41**	

Explanation of Adjustment:

B - To properly reflect the half-year depreciation expense taken on the capitalized cost to installed fence around water tank applying the 5% composite depreciation rate established in Decision No. 58102

Plant in Service	$45,824	
Less: Non Depreciable Plant	1,250	
Fully Depreciated Plant	42,936	
Depreciable Plant		$1,638
Times: Existing Composite Depreciation Rate		5.00%
Full Year Depreciation Expense		$82
Less: Half-Year Depreciation		41
Credit to Accumulated Depreciation		$41

STAFF RATE BASE ADJUSTMENTS

E	-	WORKING CAPITAL (1/24 PURCHASED PWR & WTR) - Per Company	$0	
		Per Staff	127	$127
		To reflect Staff's calculation of cash working capital based upon Staff's recommendations for purchased power and purchased water		
F	-	WORKING CAPITAL (1/8 OPERATION & MAINT EXP) - Per Company	$ -	
		Per Staff	2,134	$2,134
		To reflect Staff's calculation of cash working capital based upon Staff's recommendations for operation and maintenance expense (excluding purchased power and purchased water expenses)		

Wilhoit Water Company, Inc. - Blue Hills #3
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STATEMENT OF OPERATING INCOME

	Company Exhibit	Staff Adjustments		Staff Adjusted
Revenues:				
461 Metered Water Revenue	$17,458	$0		$17,458
460 Unmetered Water Revenue	0	3,492	A	3,492
474 Other Water Revenues	0	0		0
Total Operating Revenue	$17,458	$3,492		**$20,950**
Operating Expenses:				
601 Salaries and Wages	$9,778	($2,106)	B	$7,672
610 Purchased Water	0	0		0
615 Purchased Power	3,039	0		3,039
618 Chemicals	0	0		0
620 Repairs and Maintenance	7,133	(2,358)	C	4,775
621 Office Supplies & Expense	703	(252)	D	451
630 Outside Services	0	408	E	408
635 Water Testing	1,853	(408)	F	1,445
641 Rents	1,400	250	G	1,650
650 Transportation Expenses	0	0		0
657 Insurance - General Liability	661	(87)	H	574
659 Insurance - Health and Life	0	0		0
666 Regulatory Commisssion Expense - Rate Case	0	0		0
675 Miscellaneous Expense	2,173	(2,073)	I	100
403 Depreciation Expense	0	55	J	55
408 Taxes Other Than Income	1,355	(1,355)	K	0
408.11 Property Taxes	0	1,055	L	1,055
409 Income Tax	0	50	M	50
Total Operating Expenses	$28,095	($6,822)		**$21,274**
OPERATING INCOME/(LOSS)	**($10,637)**	**$10,313**		**($324)**
Other Income/(Expense):				
419 Interest and Dividend Income	$0	$0		$0
421 Non-Utility Income	0	0		0
427 Interest Expense	0	0		0
4XX Reserve/Replacement Fund Deposit	0	0		0
426 Miscellaneous Non-Utility Expense	0	0		0
Total Other Income/(Expense)	$0	$0		$0
NET INCOME/(LOSS)	**($10,637)**	**$10,313**		**($324)**

STAFF ADJUSTMENTS

A -	UNMETERED WATER REVENUE - Per Company		$0	
	Per Staff		3,492	$3,492

To reflect the standpipe sales that the Company does not have records for. Staff computed sales at 20% of metered revenue

Test year metered revenue	$17,458
Rate to compute standpipe sales	20%
Staff Balance, Unmetered Revenue	$3,492

B -	SALARIES AND WAGES - Per Company		$9,778	
	Per Staff		7,672	($2,106)

To reflect Staff's computation of Salaries & Wages based on number of customers by Company

Total Salaries and Wages for all Companies $44,231

Salaries and Wages					
Number of Customers by Company					
Allocation Amount	Dells	Thunderbird	YMHE	Blue Hills	Total
	67	128	110	64	369
	18.16%	34.69%	29.81%	17.34%	100.00%
$ 44,231	$ 8,031	$ 15,343	$ 13,185	$ 7,672	$ 44,231

Staff balance, Salaries and Wages $ 7,672

Wilhoit Water Company, Inc. - Blue Hills #3
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STAFF ADJUSTMENTS (Cont.)

C -	REPAIRS AND MAINTENANCE - Per Company	$7,133	
	Per Staff	4,775	($2,358)

To reflect Staff's computation of Repairs and Maintenance based on number of customers by Company

Calculation of Repairs & Maintenance		
Allocated Shared Expenses	$	310.18
Total Non-Allocable Direct Expenses	$	4,464.78
Staff balance, Repairs & Maintenance	$	4,774.96

Repairs and Maintenance					
		Amount Before Allocation	No. of Customers Allocation %		Allocated Amount
Dells	$	1,788.39	18.16%	$	324.72
Thunderbird	$	1,788.39	34.69%	$	620.36
YMHE	$	1,788.39	29.81%	$	533.12
Blue Hills	$	1,788.39	17.34%	$	310.18
			1.000000000		1,788

Repairs and Maintenance		Amount Before Allocation
Hughes	$	1,740.89
Arizona Blue Stake, Inc.	$	47.50
Total Allocable Expenses	$	1,788.39

Non-Allocable (Direct) Expenses		
Prescott Pump Service	$	1,812.94
Hughes	$	526.69
Equipment Plus	$	225.00
Ernie Dodd	$	1,900.15
Total Direct Expenses	$	4,464.78

Wilhoit Water Company, Inc. - Blue Hills #3
Docket No. W-02065A-07-0313
Test Year Ended: December 31, 2006

STAFF ADJUSTMENTS (Cont.)

D -	OFFICE SUPPLIES & EXPENSE - Per Company	$703	
	Per Staff	451	($252)

To reflect Staff's computation of Office Supplies & Expense based on Staff's computation of reasonable expenses and number of customers allocation

Calculation of Office Supplies & Expense		
Total Direct billed Postage	$	314.88
Allocated Shared Expenses	$	136.41
Staff balance, Office Supplies & Maintenance	$	451.29

Office Supplies & Expense					
	Amount Before Allocation		No. of Customers Allocation %	Allocated Amount	
Dells	$	786.51	18.16%	$	142.81
Thunderbird	$	786.51	34.69%	$	272.83
YMHE	$	786.51	29.81%	$	234.46
Blue Hills	$	786.51	17.34%	$	136.41
			1.000000000		786.51

	Office Supplies & Expense				
	Unit Cost		Units per Year	Amount Before Allocation	
Paper 10/RM 5,000 sheets				$	32.97
Ink Cartridges					
Black	$	27.49	4	$	109.96
Color	$	67.97	4	$	271.88
Post-its	$	15.29	4	$	61.16
Highlighters	$	11.39	4	$	45.56
Rubber Bands	$	10.49	4	$	41.96
Pencils	$	11.96	4	$	47.84
Shredder				$	39.98
Glue Stick				$	10.29
Envelopes (500 box)	$	19.99	4	$	79.96
Tape				$	17.99
Pens	$	6.74	4	$	26.96
Total Allocable Expenses				$	786.51

Direct Billed Postage

	Dells		Thunderbird		YHME		Blue Hills		Total
No. of Customers		67		128		110		64	369
Number of Billings		12		12		12		12	12
Total no. of bills s		804		1,536		1,320		768	4,428
Postage rate		0.41		0.41		0.41		0.41	0.41
Total Postage	$	329.64	$	629.76	$	541.20	$	314.88	$ 1,815.48

STAFF ADJUSTMENTS (Cont.)

E -	OUTSIDE SERVICES - Per Company	$0	
	Per Staff	408	$408

To reflect Staff's computation of Outside Services based on
Staff's moving expenses previously listed in water testing expense

F -	WATER TESTING - Per Company	$1,853	
	Per Staff	1,445	($408)

To reflect Staff's computation of Water Testing based on Staff's
moving some expenses previously listed in water testing expense
to Outside Services

G -	RENTS - Per Company	$1,400	
	Per Staff	1,650	$250

To reflect Staff's computation of Rents Expense based on
an equal percentage split amongst 4 companies

Rents					
Equal Percentage to each company					
		Amount Before Allocation	Allocation Percentage		Allocated Amount
Dells	$	6,600.00	25%	$	1,650.00
Thunderbird	$	6,600.00	25%	$	1,650.00
YMHE	$	6,600.00	25%	$	1,650.00
Blue Hills	$	6,600.00	25%	$	1,650.00
			1.000000	$	6,600.00
Staff balance, Rents				$	1,650

H -	INSURANCE - GENERAL LIABILITY - Per Company	$661	
	Per Staff	574	($87)

To reflect Staff's computation of Insurance - General Liability based on
an equal percentage split amongst 4 companies

Insurance - General Liability					
Number of Customers by Company					
		Amount Before Allocation	No. of Customers Allocation %		Allocated Amount
Dells	$	3,307.00	18.16%	$	600.46
Thunderbird	$	3,307.00	34.69%	$	1,147.14
YMHE	$	3,307.00	29.81%	$	985.83
Blue Hills	$	3,307.00	17.34%	$	573.57
			1.000000000	$	3,307.00
Staff balance, Insurance - General Liability				$	574

STAFF ADJUSTMENTS (Cont.)

I -	MISCELLANEOUS EXPENSE - Per Company	$2,173	
	Per Staff	100	($2,073)

To reflect Staff's calculation of Miscellaneous Expense based on information submitted by the Company, and calculation of the allocated portion of the miscellaneous expense using number of customers allocation

Miscellaneous Expense			
	Amount Before Allocation	Equal Percentage Allocation %	Allocated Amount
Dells	$ 398.80	25.00%	$ 99.70
Thunderbird	$ 398.80	25.00%	$ 99.70
YMHE	$ 398.80	25.00%	$ 99.70
Blue Hills	$ 398.80	25.00%	$ 99.70
		1.000000000	398.80

Miscellaneous Expense	Amount Before Allocation
Water Utilities Association of Arizona	$ 125.00
Martin & Bell, LLC	$ 273.80
Total Allocable Expenses	$ 398.80

Staff balance, Miscellaneous Expense	$ 100

Wilhoit Water Company, Inc. - Blue Hills #3
Docket No. W-02065A-07-0313
Test Year Ended: December 31, 2006

STAFF ADJUSTMENTS (Cont.)

J -	DEPRECIATION - Per Company	$0	
	Per Staff	55	$55

Explanation of Adjustment:

Pro Forma Annual Depreciation Expense:

DESCRIPTION	PLANT In SERVICE Per Staff	NonDepreciable or Fully Depreciated PLANT	DEPRECIABLE PLANT (Col A - Col B)	DEPRECIATION RATE	DEPRECIATION EXPENSE (Col C x Col D)
Organization	$ -	$ -	$ -	0.00%	$ -
Franchises	$ -	$ -	$ -	0.00%	$ -
Land & Land Rights	$ 1,250	$ 1,250	$ -	0.00%	$ -
Structures & Improvem	$ 2,838	$ 1,200	$ 1,638	3.33%	$ 55
Wells & Springs	$ 4,238	$ 4,238	$ -	3.33%	$ -
Pumping Equipment	$ 11,927	$ 11,927	$ -	20.00%	$ -
Water Treatment Equip	$ 609	$ 609	$ -	0.00%	$ -
Distribution Reservoirs	$ 2,843	$ 2,843	$ -	0.00%	$ -
Transmission & Distrib	$ 14,296	$ 14,296	$ -	2.22%	$ -
Services	$ 4,309	$ 4,309	$ -	5.00%	$ -
Meters & Meter Installa	$ 3,421	$ 3,421	$ -	2.00%	$ -
Hydrants	$ -	$ -	$ -	3.33%	$ -
Backflow Prevention D	$ -	$ -	$ -	8.33%	$ -
Other Plant and Misc. I	$ -	$ -	$ -	0.00%	$ -
Office Furniture & Equi	$ 91	$ 91	$ -	0.00%	$ -
Transportation Equipm	$ -	$ -	$ -	0.00%	$ -
Tools Shop & Garage I	$ -	$ -	$ -	0.00%	$ -
Laboratory Equipment	$ -	$ -	$ -	0.00%	$ -
Power Operated Equip	$ -	$ -	$ -	0.00%	$ -
Communication Equipr	$ -	$ -	$ -	0.00%	$ -
Miscellaneous Equipm	$ -	$ -	$ -	0.00%	$ -
Other Tangible Plant	$ -	$ -	$ -	0.00%	$ -
Total	$ 45,824	$ 44,186	$ 1,638		$ 55

Depreciation Expense Before Amortization of CIAC:	$ 55
Amortization of CIAC	$ -
Test Year Depreciation Expense - Staff:	$ 55
Depreciation Expense - Company:	$0
Staff's Total Adjustment:	$ 55

Pro Forma Annual Depreciation Expense:

Plant in Service	$45,824
Less: Non Depreciable Plant	1,250
Fully Depreciated Plant	42,936
Depreciable Plant	$1,638
Times: Staff Proposed Depreciation Rate	3.33%
Pro Forma Annual Depreciation Expense	**$55**

STAFF ADJUSTMENTS (Cont.)

K -	TAXES OTHER THAN INCOME - Per Company	$1,355	
	Per Staff	0	($1,355)
	To reflect removal of sales taxes included in operating expense		
L -	TAXES OTHER THAN INCOME - Per Company	$0	
	Per Staff	1,055	$1,055
	To reflect property taxes for the 2006 test year		
M -	INCOME TAX - Per Company	$0	
	Per Staff	50	$50
	To reflect Staff's computation of income tax expense given Staff's adjustments to operating revenue and operating expenses		

Wilhoit Water Company, Inc. - Blue Hills #3
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Test Year Ended: December 31, 2006

Schedule DRE-4

RATE DESIGN

	Present	-Proposed Rates-	
Monthly Usage Charge	Rates	Company	Staff
5/8" x 3/4" Meter	$8.00	$10.00	$12.00
3/4" Meter	8.00	10.00	$12.00
1" Meter	18.00	22.50	$30.00
1½" Meter	40.00	50.00	$60.00
2" Meter	64.00	80.00	$96.00
3" Meter	120.00	150.00	$192.00
4" Meter	200.00	250.00	$300.00
5" Meter	300.00	375.00	$450.00
6" Meter	400.00	500.00	$600.00
Gallons Included in Minimum	0	0	0
Per 1,000 Gallons for 0 to 6,000 Gallons	$2.95	$6.65	N/A
Per 1,000 Gallons for Gallons in Excess of 6,000	$3.78	$9.30	N/A
Per 1,000 Gallons for 0 to 3,000 Gallons	N/A	N/A	$3.00
Per 1,000 Gallons for 3,001 to 10,000	N/A	N/A	$4.50
Per 1,000 Gallons for Gallons in Excess of 10,000	N/A	N/A	$5.40
Bulk Haulers per 1000	N/A	N/A	$5.40
Service Line and Meter Installation Charges			
5/8" x 3/4" Meter	$265.00	$520.00	$520.00
3/4" Meter	295.00	600.00	600.00
1" Meter	345.00	690.00	690.00
1½" Meter	520.00	935.00	935.00
2" Meter	725.00	1,595.00	1,595.00
3" Meter	925.00	2,275.00	2,275.00
4" Meter	1,550.00	3,520.00	3,520.00
6" Meter	3,725.00	6,275.00	6,275.00
Service Charges			
Establishment	$30.00	$100.00	$30.00
Establishment (After Hours)	0.00	0.00	0.00
Reconnection (Delinquent)	30.00	100.00	30.00
Meter Test (If Correct)	50.00	150.00	50.00
Deposit	0.00	*	*
Deposit Interest	0.00%	*	*
Re-Establishment (Within 12 Months)	0.00	**	**
NSF Check	15.00	35.00	30.00
Deferred Payment (per annum)	6.00%	6.00%	6.00%
Meter Re-Read (If Correct)	15.00	35.00	15.00
Late Fee	0.00	10.00	***
Monthly Service Charge for Fire Sprinkler			
4" or Smaller	NA	NA	****
6"	NA	NA	****
8"	NA	NA	****
10"	NA	NA	****
Larger than 10"	NA	NA	****

* Per Commission Rules (R14-2-403.B)
** Months off system times the minimum (R14-2-403.D)
*** 1.5% of unpaid monthly balance.
**** 1.00% of Monthly Minimum for a Comparable Sized Meter Connection, but no less than $5.00 per month. The Service Charge for Fire Sprinklers is only applicable for service lines seperate and distinct from the primary water service line.

Wilhoit Water Company, Inc. - Blue Hills #3
Docket No. W-02065A-07-0313
Test Year Ended: December 31, 2006

TYPICAL BILL ANALYSIS
General Service 5/8 X 3/4 - Inch Meter

Average Number of Customers: 64

Company Proposed	Gallons	Present Rates	Proposed Rates	Dollar Increase	Percent Increase
Average Usage	4,639	$21.68	$40.85	$19.17	88.4%
Median Usage	3,404	$18.04	$32.64	$14.60	80.9%
Staff Recommend					
Average Usage	4,639	$21.68	$28.37	$6.69	30.9%
Median Usage	3,404	$18.04	$22.82	$4.78	26.5%

Present & Proposed Rates (Without Taxes)
General Service 5/8 X 3/4 - Inch Meter

Gallons Consumption	Present Rates	Company Proposed Rates	% Increase	Staff Proposed Rates	% Increase
0	$8.00	$10.00	25.0%	$12.00	50.0%
1,000	10.95	16.65	52.1%	15.00	37.0%
2,000	13.90	23.30	67.6%	18.00	29.5%
3,000	16.85	29.95	77.7%	21.00	24.6%
4,000	19.80	36.60	84.8%	25.50	28.8%
5,000	22.75	43.25	90.1%	30.00	31.9%
6,000	25.70	49.90	94.2%	34.50	34.2%
7,000	29.48	59.20	100.8%	39.00	32.3%
8,000	33.26	68.50	106.0%	43.50	30.8%
9,000	37.04	77.80	110.0%	48.00	29.6%
10,000	40.82	87.10	113.4%	52.50	28.6%
15,000	59.72	133.60	123.7%	79.50	33.1%
20,000	78.62	180.10	129.1%	106.50	35.5%
25,000	97.52	226.60	132.4%	133.50	36.9%
50,000	192.02	459.10	139.1%	268.50	39.8%
75,000	286.52	691.60	141.4%	403.50	40.8%
100,000	381.02	924.10	142.5%	538.50	41.3%
125,000	475.52	1,156.60	143.2%	673.50	41.6%
150,000	570.02	1,389.10	143.7%	808.50	41.8%
175,000	664.52	1,621.60	144.0%	943.50	42.0%
200,000	759.02	1,854.10	144.3%	1,078.50	42.1%

Wilhoit Water Company, Inc. - Blue Hills #3 Schedule DRE-6
Docket No. W-02065A-07-0313
Test Year Ended: December 31, 2006

FINANCIAL ANALYSIS

Selected Financial Data
Arsenic Surcharge

Line No.		[A] Staff Recommended Permanent Rates Without Loan	[B] Arsenic Treatment System $40,000 Loan at 8.00 Percent Interest Adjustments	[C] Staff Recommended Ratges with Arsenic Surcharge, Loan Prin & Interest, and Income taxes
1	INCOME STATEMENT			
	Operating Revenue			
2	Metered Water Revenue	$ 22,750	$ -	$ 22,750
3	Arsenic Surcharge	$ -	4,239	4,239
4	Unmetered Water Revenue	$ 3,492	$ -	3,492
5	Other Water Revenues	$ -	$ -	$ -
6	**Total Operating Rev:**	$ 26,242	$ 4,239	$ 30,480
	Operating Expenses			
7	Salaries and Wages	$ 7,672	$ -	$ 7,672
8	Purchased Water	$ -	$ -	$ -
9	Purchased Power	$ 3,039	$ -	$ 3,039
10	Repairs and Maintenance	$ 4,775	$ -	$ 4,775
11	Office Supplies and Expense	$ 451	$ -	$ 451
12	Outside Services	$ 408	$ -	$ 408
13	Water Testing	$ 1,445	$ -	$ 1,445
14	Rents	$ 1,650	$ -	$ 1,650
15	Insurance - General Liability	$ 574	$ -	$ 574
16	Miscellaneous Expense	$ 100	$ -	$ 100
17	Depreciation Expense	$ 55	$ -	$ 55
18	Taxes Other Than Income	$ -	$ -	$ -
19	Property Taxes	$ 1,055	$ -	$ 1,055
20	Income Tax	$ 1,050	$ 224	$ 1,274
21	**Total Operating Expense**	$ 22,273	$ 224	$ 22,497
22	**Operating Income**	$ 3,968	$ 4,015	$ 7,983
23	Interest Income	$ -	$ -	$ -
24	Interest Expense	$ -	$ 3,169	$ 3,169
25	Interest-Customer Deposits	$ -	$ -	$ -
26	**Total Other Interest Expense**	$ -	$ 3,169	$ 3,169
27	**Net Income**	$ 3,968	$ 845	$ 4,814
28	Principal Repayment	$ -	$ 845	$ 845
	TIER			
30	[L 18 + L 20] ÷ L 22	N/A		2.92
	DSC			
31	[L 16 + L 17 + L 20] ÷ [L 22 + L 26]	N/A		2.32

Wilhoit Water Company, Inc. - Blue Hills #3
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Test Year Ended: December 31, 2006

Schedule DRE-7

Line No.	CALCULATION OF ADDITIONAL REVENUE NEEDED FOR ARSENIC SURCHARGE FOR PRINCIPAL, INTEREST, AND INCOME TAXES TO PRESERVE CASH FLOW		
1			
2	Annual Principal Payment on Loan	$	845
3	Multiplied by: Gross Revenue Conversion Factor		1.265
4	**Additional Revenue Needed for Principal Payment [L2 x L3]**	$	1,069
5			
6	Additional Revenue Needed for Principal Payment (from L 4)	$	1,069
7	Less: Annual Principal Payment on Loan	$	845
8	**Additional Revenue Needed for Income Taxes [L7 - L6]**	$	224
9			
10	Annual Principal Payment on Loan (from L2)	$	845
11	Annual Interest Payment on Loan	$	3,169
12	Annual Principal and Interest Payments (L10 + L11)	$	4,015
13	Plus: Additional Revenue Needed for Income Taxes (from L6)	$	224
14	**Total Additional Revenue Needed for Principal, Interest, & Income Taxes [L12 + L13]**	$	4,239

Wilhoit Water Company, Inc. - Blue Hills #3
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Schedule DRE-8

SURCHARGE AMOUNTS

Line No.							
1	Equivalent Annual Bills (768) = Number of Customers 64 times 12 months						
2							
3							
4	Arsenic Surcharge - as determined by Arsenic Removal Surcharge Mechanism (Loan Amount $40,000)						
5	Total Increase in Revenue	$ 4,239					
6	Equivalent Annual Bills	768					
7							
8	Surcharge Amount $	5.52					
9							
10	Pro forma Effects on monthly bill						
11	5/8"x 3/4" Meter	1	x	$	5.52	=	$ 5.52
12	3/4" Meter	1.5	x	$	5.52	=	$ 8.28
13	1" Meter	2.5	x	$	5.52	=	$ 13.80
14	1½" Meter	5	x	$	5.52	=	$ 27.60
15	2" Meter	8	x	$	5.52	=	$ 44.15
16	3" Meter	15	x	$	5.52	=	$ 82.79
17	4" Meter	25	x	$	5.52	=	$ 137.98
18	6" Meter	50	x	$	5.52	=	$ 275.95

Total Direct Expenses

Wilhoit Water Company, Inc. - Blue Hills #3
Docket No. W-02065A-07-0313
Test Year Ended: December 31, 2006

TYPICAL BILL ANALYSIS

General Service 5/8 X 3/4 - Inch Meter
With Arsenic Removal Surcharge

Average Number of Customers: 64

Company Proposed	Gallons	Present Rates	Proposed Rates	Dollar Increase	Percent Increase
Average Usage	4,639	$21.68	$40.85	$19.17	88.4%
Median Usage	3,404	$18.04	$32.64	$14.60	80.9%
Staff Recommend					
Average Usage	4,639	$21.68	$33.89	$12.21	56.3%
Median Usage	3,404	$18.04	$28.34	$10.30	57.1%

Present & Proposed Rates (Without Taxes)
General Service 5/8 X 3/4 - Inch Meter

Gallons Consumption	Present Rates	Company Proposed Rates	% Increase	Staff Proposed Rates	% Increase
0	$8.00	$10.00	25.0%	$17.52	119.0%
1,000	10.95	16.65	52.1%	20.52	87.4%
2,000	13.90	23.30	67.6%	23.52	69.2%
3,000	16.85	29.95	77.7%	26.52	57.4%
4,000	19.80	36.60	84.8%	31.02	56.7%
5,000	22.75	43.25	90.1%	35.52	56.1%
6,000	25.70	49.90	94.2%	40.02	55.7%
7,000	29.48	59.20	100.8%	44.52	51.0%
8,000	33.26	68.50	106.0%	49.02	47.4%
9,000	37.04	77.80	110.0%	53.52	44.5%
10,000	40.82	87.10	113.4%	58.02	42.1%
15,000	59.72	133.60	123.7%	85.02	42.4%
20,000	78.62	180.10	129.1%	112.02	42.5%
25,000	97.52	226.60	132.4%	139.02	42.6%
50,000	192.02	459.10	139.1%	274.02	42.7%
75,000	286.52	691.60	141.4%	409.02	42.8%
100,000	381.02	924.10	142.5%	544.02	42.8%
125,000	475.52	1,156.60	143.2%	679.02	42.8%
150,000	570.02	1,389.10	143.7%	814.02	42.8%
175,000	664.52	1,621.60	144.0%	949.02	42.8%
200,000	759.02	1,854.10	144.3%	1,084.02	42.8%

Engineering Report for Wilhoit Water Company, Inc. – Blue Hills #3 System

Docket No. W-02065A-07-0313 (Rates)

By: Marlin Scott, Jr.,
Utilities Engineer

October 16, 2007

CONCLUSIONS

A. Wilhoit Water Company, Inc. – Blue Hills #3 System's ("Company") current well and storage capacities could adequately serve its current customer base and reasonable growth.

B. The Arizona Department of Environmental Quality ("ADEQ") reported no deficiencies and has determined that the Company's system, PWS #13-055 is currently delivering water that meets the water quality standards required by Arizona Administrative Code, Title 18, Chapter 4.

C. The Company has an approved backflow prevention tariff that became effective on February 22, 2004.

RECOMMENDATIONS

1. Staff recommends that the Company monitor the system and submit the gallons pumped and sold to determine the actual water loss for one full year. The results of this monitoring and reporting should be docketed as a compliance item in this case within 13 months of the effective date of the order issued in this proceeding. If the reported water loss for the period is greater than 10%, the Company shall prepare a report containing a detailed analysis and plan to reduce water loss to 10% or less. If the Company believes it is not cost effective to reduce water loss to less than 10%, it should submit a detailed cost benefit analysis to support its opinion. In no case shall the Company allow water loss to be greater than 15%. The water loss reduction report or the detailed analysis, whichever is submitted, shall be docketed as a compliance item within 13 months of the effective date of the order issued in this proceeding.

2. Staff recommends that the Company be required to report its customer count by system in future submittal of Commission Annual Reports.

3. Staff recommends an annual water testing expense of $1,445 be used for purposes of this application and further recommends that the remaining $408 of the reported $1,853 be classified as part of the water operator's fee

4. Staff recommends that Company submit the ADEQ Certificate of Approval of Construction for the arsenic treatment system by December 31, 2008.

5. The Company is located in the Prescott Active Management Area. Staff recommends that the Company file with Docket Control, as a compliance item in this docket by December 31, 2008, a letter from Arizona Department of Water Resources indicating that the Company's water use and monitoring requirements have been resolved.

6. Staff recommends that the Company use Staff's depreciation rates delineated in Table B.

7. Staff recommends approval of Staff's Service Line and Meter Installation Charges as delineated in Table C.

8. Staff recommends that the Company file a curtailment tariff in the form found on the Commission's website at www.azcc.gov/divisions/utilities/forms/Curtailment-Std.pdf. This tariff shall be docketed as a compliance item in this case within 45 days of the effective date of an order in this proceeding for review and certification by Staff.

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PAGE

A. LOCATION OF COMPANY

Wilhoit Water Company, Inc. – Blue Hills #3 System ("Company") serves a community in Dewey. Figure 1 shows the location of the Company within Yavapai County and Figure 2 shows the certificated area covering 1/32 square-mile or 20 acres.

B. DESCRIPTION OF THE WATER SYSTEM

The water system was field inspected on September 17, 2007, by Marlin Scott, Jr., Staff Utilities Engineer, in the accompaniment of Jim West, Consultant for the Company. The current system consists of two wells, one storage tank, booster system and a distribution system serving approximately 55 customers and a coin-operated standpipe service. All the pumping facilities are located at one site.

In the mid 1990's, a gasoline spill occurred across the road from the wells/pumping site. Due to this spill, ADEQ ordered the responsible party, Blue Hills Market, to clean-up the spill and further ordered treatment equipment be installed for the water company. This treatment equipment, activated charcoal filters, was placed into operation in 2002 and is currently being operated and maintained by Zelen Environmental on behalf of the Blue Hills Market.

A system schematic is shown as Figure 3 and a detailed plant facility listing is as follows:

Table 1. Pumping Site

Plant Items	Well #1 (55-622750)	Well #2 (55-622751)
Casing Size	6-inch	6-inch
Casing Depth **	178 ft.	35 ft.
Submersible Pump	3-Hp	1/2-Hp
Pumping Rate	30 GPM	10 GPM
Meter Size	1-1/2-inch	
Storage Tank	12,500 gallon	
Booster Pumps	3-Hp, 2 each	
Captive Air Tanks	120 gallons, 4 each	
Chlorination	Liquid	
Chain Link Fencing	50 ft. by 70 ft. around entire site	

** Note: According to the ADWR Imaged Records Database.

Table 2. Water Mains #

Diameter	Material	Length
3-inch	-	-
4-inch	ACP	3,845 ft.
6-inch	ACP	3,150 ft.
	Total:	6,995 ft.

Note: According to Staff's prior Engineering Report in 1992.

Table 3. Customer Meters

Size	Quantity
5/8 x 3/4-inch	55
3/4-inch	-
1- inch	-
1-1/2-inch	-
2-inch	-
Total:	55

Table 4. Structures

Structures
Standpipe – coin operated system

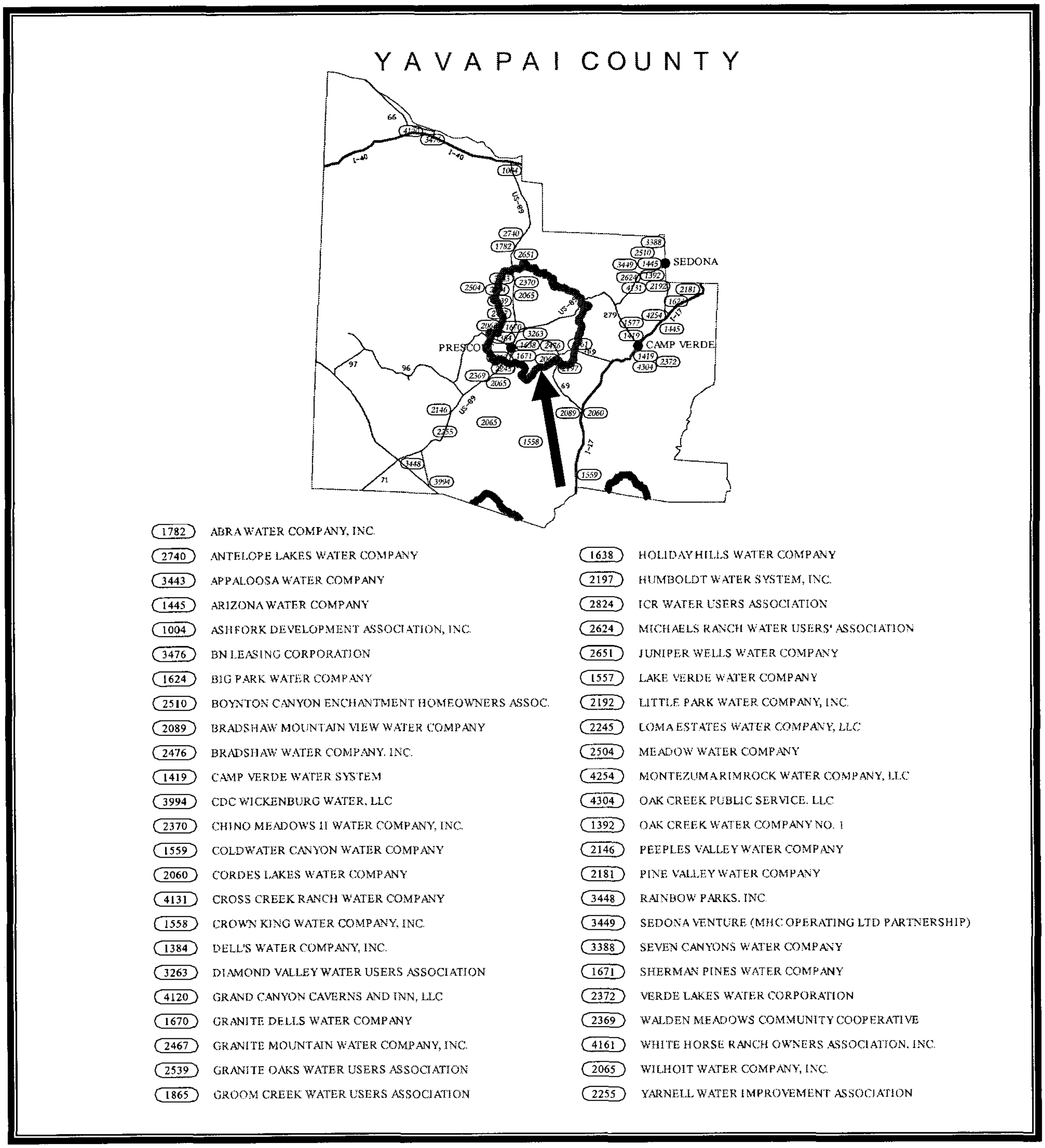

Figure 1. Yavapai County Map

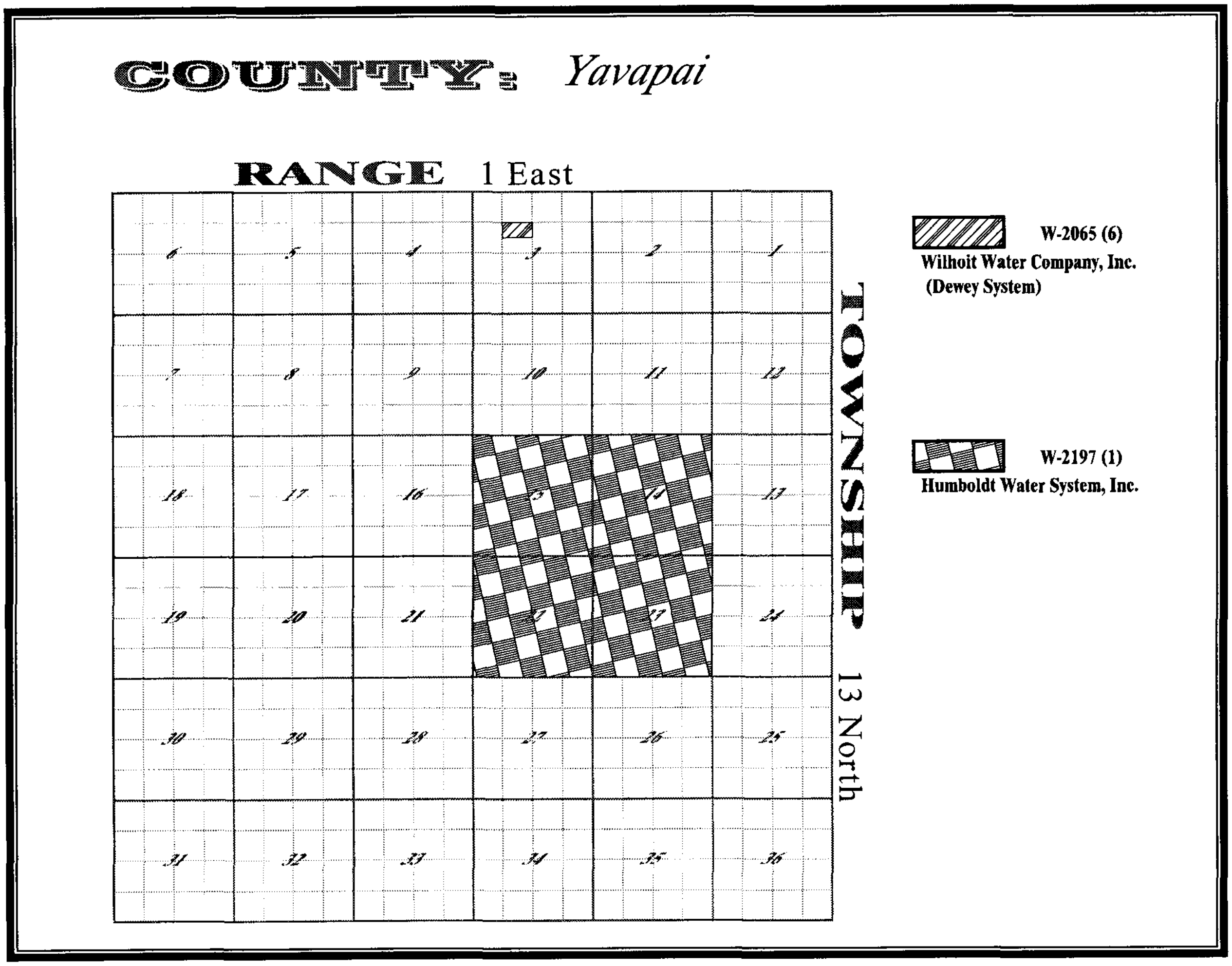

Figure 2. Certificated Area

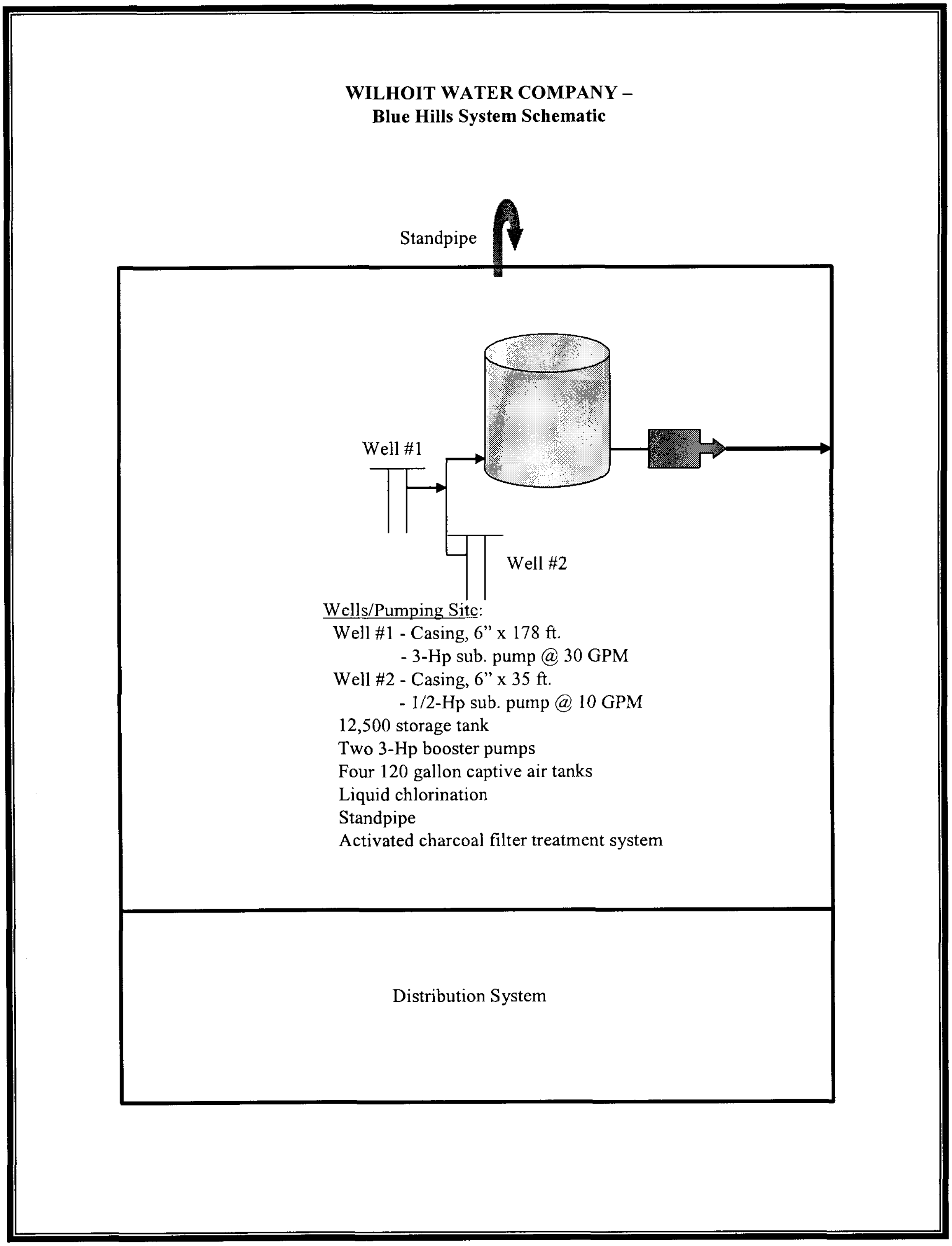

Figure 3. System Schematic

C. WATER USE

Water Sold

Figure 4 represents the water consumption data provided by the Company in its water use data sheet. Customer consumption experienced a high monthly water use of 223 gallons per day ("GPD") per connection in May and a low monthly water use of 90 GPD per connection in March for an average monthly use of 153 GPD per connection.

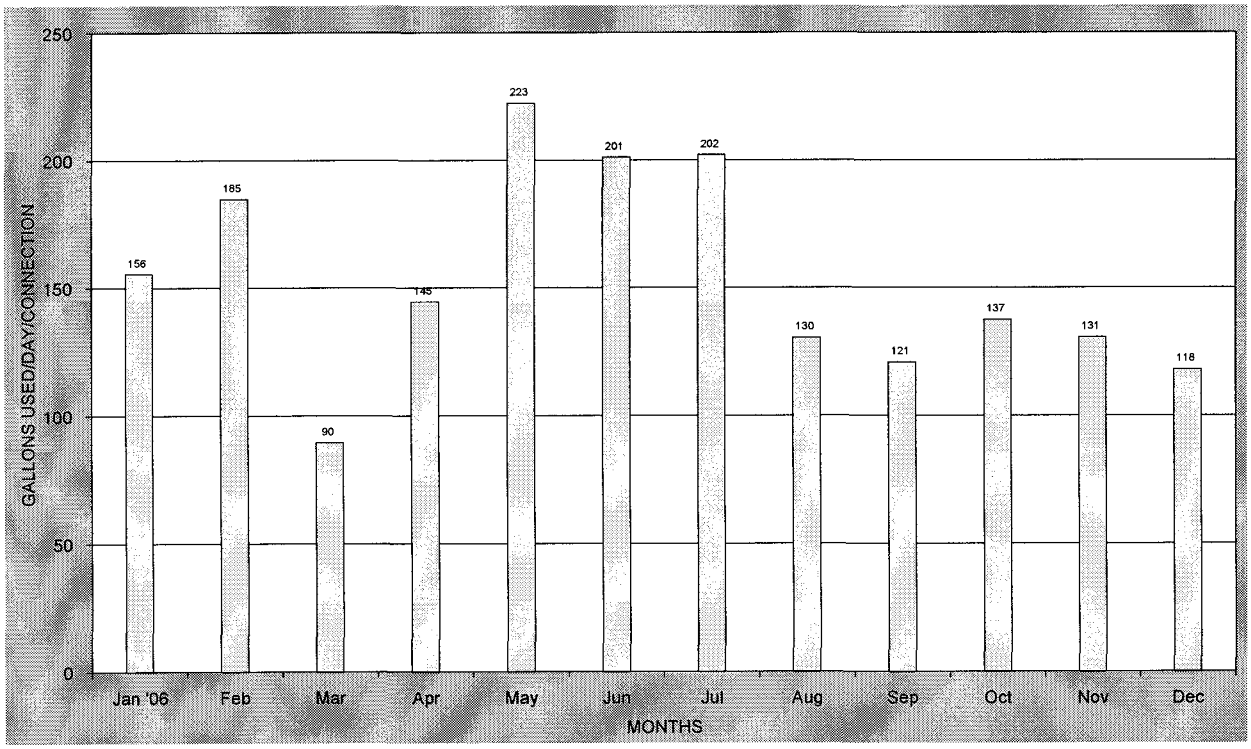

Figure 4. Water Use

Non-Account Water

Non-account water should be 10% or less. The Company reported 3,572,301 gallons of water sold and did not report the number of gallons pumped during the test year. Although the wells share a 1-1/2-inch meter, the Company is not recording its gallons pumped. In prior years as shown in their Annual Reports, the Company has been reporting the same amount of gallons sold as gallons pumped. Based on the unknown "actual" gallons pumped, the water loss percent cannot be determined at this time.

Staff recommends that the Company monitor the system and submit the gallons pumped and sold to determine the actual water loss for one full year. The results of this monitoring and reporting should be docketed as a compliance item in this case within 13 months of the effective date of the order issued in this proceeding. If the reported water loss for the period is greater than 10%, the Company shall prepare a report containing a detailed analysis and plan to reduce water loss to 10% or less. If the Company believes it is not cost effective to reduce water loss to less than 10%, it should submit a detailed cost benefit analysis to support its opinion. In no case shall the Company allow water loss to be greater than 15%. The water loss reduction report or the detailed analysis, whichever is submitted, shall be docketed as a compliance item within 13 months of the effective date of the order issued in this proceeding.

System Analysis

The system's current two source well capacity totaling 40 GPM and 12,500 gallons of storage tank capacity could adequately serve approximately 100 service connections. The system currently has 55 service connections and one standpipe service. Therefore, this system can adequately serve its current customer base and reasonable growth.

D. GROWTH

In the Company's Annual Reports, it did not separate the customer count for each of its three independent water systems, but instead, reported its entire customer base as one. Therefore, Staff cannot determine possible growth for this system. Staff recommends that the Company be required to report its customer count by system in future submittal of Commission Annual Reports.

E. ARIZONA DEPARTMENT OF ENVIRONMENTAL QUALITY ("ADEQ") COMPLIANCE

Compliance

According to an ADEQ Compliance Status Report, dated April 30, 2007, that was submitted with the rate application; ADEQ reported no deficiencies and has determined that the Company's system, PWS #13-055 is currently delivering water that meets the water quality standards required by Arizona Administrative Code, Title 18, Chapter 4.

Water Testing and Operator's Fee Expenses

The Company is subject to mandatory participation in the Monitoring Assistance Program ("MAP"). Starting January 1, 2002, water companies paid a fixed $250 per year fee, plus an additional fee of $2.57 per service connection, regardless of meter size for participation in MAP. Participation in the MAP program is mandatory for water systems, which serve less than 10,000 persons (approximately 3,300 service connections).

The Company reported its water testing expense at $1,853 during the test year by combining water testing costs and water operator's fees. Staff has reviewed these expenses and has recalculated the annual expense by adding the omitted monitoring requirements for lead & copper and Disinfection/Disinfection By-Product ("D/DBP"). Annual D/DBP monitoring applies to any public water system that adds a halogenated disinfectant during the treatment process. The Company chlorinates its wells and therefore, is required to monitor for D/DBP. Staff has also made additional adjustments that are shown in Table A below for Staff's adjusted annual water testing expense of $1,445.

Table A. Water Testing Cost

Monitoring (Tests per 3 years, unless noted.)	Cost per test	No. of tests	Annual Cost
Total coliform – monthly	$65	12	$780
Inorganics – Priority Pollutants	MAP	MAP	MAP
Radiochemical – per 4 years	MAP	MAP	MAP
Phase II and V:			
Nitrate – annual	$55	1	$55
Nitrite – once per period	MAP	MAP	MAP
Asbestos – per 9 years	MAP	MAP	MAP
MAP – IOCs, SOCs, & VOCs ##	MAP	MAP	** $381
Lead & Copper – per 3 years - Sampling & shipping samples	$45 $75	5 1	$75 $25
D/DBP:			
TTHM/HH5 – per 3 years - Sampling & shipping samples	$335 $50	1 1	$112 $17
Total			**$1,445**

Note: ADEQ - MAP invoice for the 2006 Calendar Year is $381.07.

Staff recommends an annual water testing expense of $1,445 be used for purposes of this application and further recommends that the remaining $408 of the reported $1,853 be classified as part of the water operator's fee.

Arsenic

According to the ADEQ Monitoring Assistance Program analysis report for 2007, the Company's composite arsenic level from its two well was reported at 18 parts per billion ("ppb"). Based on this arsenic level, the Company indicated it is currently seeking a bid from Adedge Technologies for engineering, construction, and installation of an arsenic treatment system.

Staff recommends that Company submit the ADEQ Certificate of Approval of Construction for the arsenic treatment system by December 31, 2008.

F. ARIZONA DEPARTMENT OF WATER RESOURCES ("ADWR") COMPLIANCE

The Company is located in the Prescott Active Management Area ("AMA"). Since the Company uses less than 250 acre-feet of water per year, it is considered a small provider by ADWR and is not subject to the gallons per capita per day limit and conservation rules. The Company is only required to monitor and report water use.

In response to Staff's request for a compliance status, ADWR provided a copy of its Advisory letter to Wilhoit Water Company dated October 11, 2007. According to the letter, the Company is not in compliance with ADWR requirements for calendar year 2006, based on ADWR's audit of the Company's 2006 Annual Withdrawal and User Report. In addition, it states that the Company shall provide conformation of repair or installation of new meters for all its wells to ADWR by December 11, 2007. The Company's 2007 Annual Withdrawal and User Report will also have to include the partial meter readings for the fourth quarter of 2007.

Staff recommends that the Company file with Docket Control, as a compliance item in this docket by December 31, 2008, a letter from ADWR indicating that the Company's water use and monitoring requirements have been resolved.

G. DEPRECIATION RATES

The Company has been using a depreciation rate of 5.00% in every National Association of Regulatory Utility Commissioners ("NARUC") plant category. In recent orders, the Commission has been shifting away from the use of composite rates in favor of individual depreciation rates by NARUC category. (For example, a uniform 5% composite rate would not really be appropriate for either vehicles or transmission mains and instead, different specific retirement rates should be used.)

Staff has developed typical and customary depreciation rates within a range of anticipated equipment life. These rates are presented in Table B and it is recommended that the Company use depreciation rates by individual NARUC category on a going-forward basis.

Table B. Depreciation Rates

NARUC Acct. No.	Depreciable Plant	Average Service Life (Years)	Annual Accrual Rate (%)
304	Structures & Improvements	30	3.33
305	Collecting & Impounding Reservoirs	40	2.50
306	Lake, River, Canal Intakes	40	2.50
307	Wells & Springs	30	3.33
308	Infiltration Galleries	15	6.67
309	Raw Water Supply Mains	50	2.00
310	Power Generation Equipment	20	5.00
311	Pumping Equipment	8	12.5
320	Water Treatment Equipment		
320.1	Water Treatment Plants	30	3.33
320.2	Solution Chemical Feeders	5	20.0
330	Distribution Reservoirs & Standpipes		
330.1	Storage Tanks	45	2.22
330.2	Pressure Tanks	20	5.00
331	Transmission & Distribution Mains	50	2.00
333	Services	30	3.33
334	Meters	12	8.33
335	Hydrants	50	2.00
336	Backflow Prevention Devices	15	6.67
339	Other Plant & Misc Equipment	15	6.67
340	Office Furniture & Equipment	15	6.67
340.1	Computers & Software	5	20.00
341	Transportation Equipment	5	20.00
342	Stores Equipment	25	4.00
343	Tools, Shop & Garage Equipment	20	5.00
344	Laboratory Equipment	10	10.00
345	Power Operated Equipment	20	5.00
346	Communication Equipment	10	10.00
347	Miscellaneous Equipment	10	10.00
348	Other Tangible Plant	----	----

NOTES:

1. These depreciation rates represent average expected rates. Water companies may experience different rates due to variations in construction, environment, or the physical and chemical characteristics of the water.

2. Acct. 348, Other Tangible Plant may vary from 5% to 50%. The depreciation rate would be set in accordance with the specific capital items in this account.

H. OTHER ISSUES

1. Service Line and Meter Installation Charges

The Company has requested changes in its service line and meter installation charges. These charges are refundable advances and the Company has requested "total" charges that are similar to Staff's customary range of charges. Since the Company may at times install meters on existing service lines, it would be appropriate for some customers to only be charged for the meter installation. Therefore, Staff recommends approval of the "total" charges as shown in Table C below, with separate installation charges for the service line and meter installations. Staff also would recommend the deletion of the 5-inch meter installation charge due to the fact that 5-inch meters do not exist.

Table C. Service Line and Meter Installation Charges

Meter Size	Company Current Charges	Recommended Service Line Charges	Recommended Meter Charges	Recommend Total Charges
5/8 x 3/4-inch	$265	$385	$135	$520
3/4-inch	$295	$385	$215	$600
1-inch	$345	$435	$255	$690
1-1/2-inch	$520	$470	$465	$935
2-inch	$725	$630	$965	$1,595
3-inch	$925	$805	$1,470	$2,275
4-inch	$1,550	$1,170	$2,350	$3,520
5-inch	$2,638	N/A	N/A	N/A
6-inch	$3,725	$1,730	$4,545	$6,275

2. Curtailment Tariff

The Company does not have an approved curtailment tariff. Staff recommends that the Company file a curtailment tariff in the form found on the Commission's website at www.azcc.gov/divisions/utilities/forms/Curtailment-Std.pdf. This tariff shall be docketed as a compliance item in this case within 45 days of the effective date of an order in this proceeding for review and certification by Staff.

3. **Backflow Prevention Tariff**

The Company has an approved backflow prevention tariff that became effective on February 22, 2004.