

COMMISSIONERS
MIKE GLEASON - Chairman
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
KRISTIN K. MAYES
GARY PIERCE



0000078559

ARIZONA CORPORATION COMMISSION

ORIGINAL

DATE: NOVEMBER 9, 2007

DOCKET NO: W-20541A-06-0308

TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Marc E. Stern. The recommendation has been filed in the form of an Order on:

CEDAR GROVE WATER, INC.
(RATES)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and ten (10) copies of the exceptions with the Commission's Docket Control at the address listed below by **4:00** p.m. on or before:

NOVEMBER 19, 2007

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

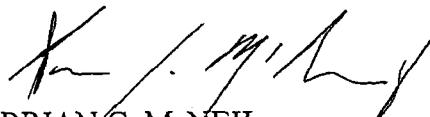
NOVEMBER 27, 2007 and NOVEMBER 28, 2007

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

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AZ CORP COMMISSION
DOCKET CONTROL


BRIAN C. McNEIL
EXECUTIVE DIRECTOR

Arizona Corporation Commission
DOCKETED

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1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 COMMISSIONERS

3 MIKE GLEASON - Chairman
4 WILLIAM A. MUNDELL
5 JEFF HATCH-MILLER
6 KRISTIN K. MAYES
7 GARY PIERCE

8 IN THE MATTER OF THE APPLICATION OF
9 CEDAR GROVE WATER, INC. FOR
10 APPROVAL OF A PERMANENT RATE
11 INCREASE.

DOCKET NO. W-20541A-06-0308

DECISION NO. _____

12 ORDER

13 Open Meeting
14 November 27 and 28, 2007
15 Phoenix, Arizona

16 **BY THE COMMISSION:**

17 On May 2, 2006, Mark Grapp d/b/a Cedar Grove Water Company ("CGW") filed with the
18 Arizona Corporation Commission ("Commission") an application for a permanent increase in CGW's
19 water rates and charges. Subsequent to the filings of CGW's application, notice was provided to
20 CGW's customers by first class U.S. mail.

21 On June 1, 2006, pursuant to A.A.C. R14-2-103, the Commission's Utilities Division
22 ("Staff") issued a Notice of Insufficiency ("Notice") with respect to the Company's application.
23 After subsequent data filings by the Company, Staff on July 18, November 14 and December 28,
24 2006, issued three more Notices.

25 On March 12, 2007, Staff issued a Notice of Sufficiency, and classified the Company as a
26 Class D Utility. However, Staff subsequently determined that it required "extensive additional
27 information" to complete its analysis and needed more data from CGW. Staff discussed the problem
28 with CGW and the utility agreed to a suspension of the time frame as set forth in A.A.C. R14-2-103.

Additionally, on March 22, 2007, CGW and Cedar Grove Water, Inc. ("Applicant" or
Company") filed with the Commission an application for the approval of the sale of CGW's assets

1 and transfer of CGW's Certificate of Convenience and Necessity ("Certificate") to the Company.¹

2 On April 25, 2007, in light of the foregoing, Staff filed a Motion for the suspension of the
3 time frame in the proceeding and indicated that the Applicant did not object to the Motion.

4 On May 2, 2007, by Procedural Order, the time frame was suspended until further Order.

5 On October 26, 2007, Staff filed its Staff Report recommending that Staff's proposed rates
6 and charges be approved. No comments or objections were filed by the Company to Staff's
7 recommendations.

8 * * * * *

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

11 **FINDINGS OF FACT**

12 1. Pursuant to authority granted by the Commission, Applicant is an Arizona corporation
13 engaged in the business of providing water service to an area approximately twelve miles northeast of
14 Show Low in Apache County, Arizona.

15 2. Applicant's present rates and charges for water were approved in Decision No. 63673
16 (May 24, 2001).

17 3. On May 2, 2006, the Company filed an application requesting authority to increase its
18 rates and charges for water service.

19 4. Applicant provided notice to its customers of its application for a proposed rate
20 increase by first class U.S. mail and, in response thereto, four protests have been received by the
21 Commission.

22 5. On March 12, 2007, Staff filed notice that the Company's rate application had met the
23 Commission's sufficiency requirements pursuant to A.A.C. R14-2-103.

24
25 _____
26 ¹ See Decision No. 69982 (October 30, 2007) in which the Commission approved the application of CGW and the
27 Company for the sale of CGW's assets and transfer of its Certificate to the Company. This Decision describes the manner
28 in which Mr. Mark Grapp personally acquired the assets of CGW in 1992, continued utility operations and ultimately
transferred the assets to the Company, which is an Arizona corporation in good standing and is owned by Mr. Grapp. As
a result of Decision No. 69982, CGW's docket number of W-02597A was extinguished and the utility now operates under
Docket No. W-20541A which is assigned to the Company. Therefore, the docket number originally assigned to the
Company in its rate application of W-02597A-06-0308 has been changed to W-20541A-06-0308 as it appears above.

1 6. On May 2, 2007, by Procedural Order, the time frame was suspended until further
2 Order because Staff needed additional data to further process the Company's application.

3 7. During the test year ended December 31, 2005 ("TY"), Applicant served 283 metered
4 customers who were all served by 5/8" x 3/4" meters.

5 8. Average and median water usage by residential users during the TY were 5,135 and
6 2,883 gallons per month, respectively.

7 9. Staff conducted an investigation of Applicant's proposed rates and charges for water
8 service and filed its Staff Report on the Company's rate application request on October 26, 2007,
9 recommending that Staff's proposed rates and charges be approved. Staff also recommended that the
10 Company's service line and meter installation charges and its other service charges remain at their
11 current levels consistent with Staff's recommendations.

12 10. The water rates and charges for Applicant at present, as proposed in the application,
13 and as recommended by the Staff are as follows:

	<u>Present Rates</u>	<u>Proposed Rates Company</u>	<u>Staff</u>
<u>MONTHLY USAGE CHARGE:</u>			
5/8" x 3/4" Meter	\$ 18.75	\$ 27.50	\$ 20.50
3/4" Meter	28.15	41.25	30.78
1" Meter	46.90	68.75	51.28
1 1/2" Meter	93.75	137.50	102.50
2" Meter	150.00	220.00	164.00
3" Meter	281.25	412.50	307.50
4" Meter	468.75	687.50	512.50
6" Meter	937.50	1,375.00	1,025.00
<u>GALLONAGE CHARGES:</u>			
(per 1,000 gallons)			
0 to 3,000	N/A	N/A	\$ 2.00
3,001 to 9,000	N/A	N/A	\$ 3.25
Over 9,000	N/A	N/A	\$ 4.90
0 to 4,000	\$ 2.50	\$ 3.00	N/A
4,001 to 9,999	\$ 2.50	\$ 3.25	N/A
Over 10,000	\$ 2.50	\$ 3.75	N/A
Bulk Water Rate (per 1,000 Gallons)	\$ 5.00	\$ 6.50	\$ 5.00

SERVICE LINE AND METER INSTALLATION CHARGES:

(Refundable pursuant to A.A.C. R14-2-405)

1				
2	5/8" x 3/4" Meter	\$ 210.00	\$ 0.00	\$ 0.00
	3/4" Meter	245.00	245.00	245.00
3	1" Meter	350.00	350.00	350.00
	1 1/2" Meter	525.00	525.00	525.00
4	2" Meter	700.00	700.00	700.00
	3" Meter	980.00	980.00	980.00
5	4" Meter	1,820.00	1,820.00	1,820.00
6	6" Meter	3,920.00	3,920.00	3,920.00

SERVICE CHARGES:

8	Establishment	\$ 20.00	\$ 25.00	\$ 20.00
9	Establishment (After Hours)	35.00	40.00	35.00
	Reconnection (Delinquent)	20.00	25.00	20.00
10	Meter Test (If Correct)	50.00	50.00	50.00
	Deposit	0.00	0.00	*
11	Deposit Interest	0.00%	0.00%	*
	Reestablishment (Within 12 Months)	0.00	**	**
12	NSF Check	20.00	30.00	20.00
13	Deferred Payment (Per Month)	18.00%	18.00%	18.00%
	Meter Reread (If Correct)	15.00	25.00	15.00
14	Late Fee	18.00%	18.00%	1.50%

MONTHLY SERVICE CHARGE FOR FIRE SPRINKLERS:

17	4" or Smaller	***	***	***
	6"	***	***	***
18	8"	***	***	***
	10:	***	***	***
19	Larger than 10"	***	***	***

- * Per Commission rule A.A.C. R-14-2-403(B).
- ** Months off system times the minimum per Commission rule A.A.C. R14-2-403(D).
- *** 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 separate and distinct from the primary water service line.

11. Pursuant to the Staff Report, Applicant's fair value rate base ("FVRB") is determined to be \$46,587 which is the same as its original cost rate base. The Company's FVRB reflects a \$50,243 decrease by Staff to Applicant's proposed FVRB due in large part to an adjustment to

1 Applicant's plant in service totaling \$26,002 and due to a \$46,403 increase to the Company's
2 accumulated depreciation.

3 12. In the Staff Report, the Applicant is described as one of five companies owned and
4 operated by Mr. Grapp from an office located at 340 N. 9th Street in Show Low, Arizona. Four of the
5 companies are Commission regulated public water companies as follows: Watco, Inc.; Cedar Grove
6 Water, Inc.; A. Peterson Water Company; and Vernon Valley Water, Inc. The fifth company, Cedar
7 Grove Water Management Company, is a management entity.²

8 13. Staff found that Mr. Grapp shares services to manage and operate all five companies.
9 Shared service expenses accounted for approximately 60 percent of the Company's TY expenses.
10 The shared expenses include, but are not limited to the following: employee salaries, including Mr.
11 Grapp's; transportation; office space; office supplies; utilities; computers; computer software;
12 telephones; insurance; and other miscellaneous services.

13 14. Staff reviewed the allocation methodology used by Applicant and found that the
14 Company allocates some expenses based on a single factor (i.e., the number of customers per
15 regulated utility) and allocates other expenses on a 50/50 split between Applicant and Watco, Inc.
16 Since the primary goal of cost allocation is to prevent or limit, as much as possible, any cross-
17 subsidization of customers from one company by customers of another company, the single factor
18 allocation methodology that the Company uses is inappropriate because it always results in the utility
19 company with the largest number of customers (i.e., Applicant) paying the largest amount of the
20 allocated cost regardless of any direct causal relationship between the number of customers and that
21 cost.

22 15. Staff noted that inequities resulted in the areas of the owner's salary allocation, rental
23 allocation, the insurance allocation, transportation allocation and office expenses.

24 16. These inequities led to some subsidization of the customers of Mr. Grapp's two
25 smaller water utilities, A. Peterson Water Company and Vernon Valley Water, Inc., and to some
26 extent his unregulated management company.

27 _____
28 ² Additionally, Mr. Grapp owns a payroll company, Four Star Land Development that processes payroll for the four
regulated companies, but is not located at the same office as the other five companies.

1 17. Staff cited principles contained in the National Association of Regulatory
2 Commissioners ("NARUC") Guideline for Cost Allocations and Affiliate Transactions ("GCAAT").

3 18. Using NARUC's GCAAT, Staff identified four relevant cost drivers of the Company's
4 shared indirect expenses. The equally weighted factors used in calculating the general allocation
5 percentage are as follows: direct labor hours of employees; direct operating expense; number of
6 customers; and net plant.

7 19. Staff's calculation of the four-factor general allocation percentage is shown on
8 Schedule DRE-3 of the Staff Report. Staff states that this methodology produces a more equitable
9 allocation of shared indirect expenses because it more closely follows NARUC's GCAAT of
10 identifying relevant cost drivers and utilizing direct costs which Staff utilized to make adjustments of
11 the Company's TY operating expenses. Staff recommended that the Company use NARUC's
12 GCAAT in the future to determine the Company's indirect shared expenses.

13 20. Staff decreased Applicant's TY operating expenses by \$14,493 primarily due to
14 adjustments caused by applying NARUC's GCAAT to the Company's expense items. The following
15 expenses were substantially reduced by Staff: repairs and maintenance (\$1,986); office supplies and
16 expenses (\$3,882); outside services (\$533); transportation expense (\$5,947); miscellaneous expense
17 (\$1,391); taxes other than income (\$5,206); and depreciation expense (\$2,410). These decreases
18 were somewhat offset by Staff increases to salaries and wages (\$5,450) and water testing (\$1,374).³

19 21. Applicant's present water rates and charges produced adjusted operating revenues of
20 \$103,461 and adjusted operating expenses of \$103,675 which resulted in an operating loss of \$214
21 during the TY.

22 22. The water rates and charges Applicant proposed would produce operating revenues of
23 \$138,461⁴ and adjusted operating expenses of \$103,675 resulting in net operating income of \$34,786.
24 This is a 74.67 percent rate of return on FVRB. Staff notes that the Company has too small a rate
25

26 _____
27 ³ Staff also made an adjustment to below the line expenses by increasing interest expense by \$1,903 to reflect the interest
expense during the TY on long-term debt previously approved in 2001.

28 ⁴ Although the Company proposed this amount of operating revenue in its application, according to Staff, the Company's
proposed rates would actually produce \$144,189 in revenue.

1 base to earn a meaningful rate of return and the Company's net operating income equates to a 25.13
2 percent operating margin based on Applicant's proposed rates.

3 23. The water rates and charges proposed by Staff would produce adjusted operating
4 revenues of \$122,069 and adjusted operating expenses of \$103,675 resulting in net operating income
5 of \$18,394 or a 39.48 percent rate of return on FVRB. Staff notes that it was unable to determine
6 Applicant's revenue requirement by applying a rate of return on the Company's small rate base.
7 Staff's revenue requirement will allow the revenues needed to meet the Company's operating needs.⁵

8 24. Applicant's proposed rate schedule would increase the average monthly customer
9 water bill by 36.7 percent, from \$31.59 to \$43.19, and the median monthly customer water bill by
10 39.3 percent, from \$25.96 to \$36.15.

11 25. Staff's recommended rates would increase the average monthly customer water bill by
12 5.9 percent, from \$31.59 to \$33.44, and the median monthly customer water bill by 1.2 percent, from
13 \$25.96 to \$26.27.

14 26. According to the Engineering Report attached to the Staff Report, Staff was unable to
15 accurately determine water loss or non-account water for the Company in 2004 and 2005, and is
16 therefore recommending that the Company monitor and file, annually hereafter, a report to ensure
17 water loss is below 10 percent for at least three years.

18 27. The Staff engineer's report also recommends that the Company complete within 90
19 days of the effective date of this Decision the following repairs:

- 20
- Correct substandard (loose and/or exposed) wiring at the Well No. 5 well site;
 - Install permanent enclosure needed for booster system at the Transfer Station; and
 - Install permanent enclosure/building and slab needed for well at the Well No. 5 well site.
- 21
- 22

23 28. According to Staff, the Company is in compliance with the Commission's rules and is
24 current in the payment of its sales and property taxes.

25 29. The Company's wells produce water which is well below the new maximum standard
26 allowed for arsenic, and according to documentation from the Arizona Department of Environmental
27

28 ⁵ This equates to a 15.07 percent operating margin.

1 Quality ("ADEQ"), the wells are delivering water which meets the requirements of the Safe Drinking
 2 Water Act.

3 30. The Company has a Curtailment Tariff approved by the Commission.

4 31. Staff is additionally recommending that the Commission order the following:

- 5 • that Applicant notify its customers of the approved water rates and charges and their
 6 effective date by means of an insert in the monthly billing which precedes the month
 7 in which they become effective and file a copy of the notice sent to its customers with
 8 the Commission's Docket Control as a compliance item in this docket;
- 9 • that Applicant file, within 30 days of the effective date of this Decision, with the
 10 Commission's Docket Control, as a compliance item in this docket a copy of the
 11 schedule of its approved rates and charges;
- 12 • that the Company maintain its books and records in accordance with the NARUC
 13 Uniform System of Accounts ("USOA");
- 14 • that the Company adopt and utilize NARUC's GCAAT as described in Findings of
 15 Fact No. 17 above to determine the Company's indirect shared expenses;
- 16 • that the Company file, annually after the effective date of this Decision, yearly reports,
 17 within 30 days of the end of each calendar year, with the Commission's Docket
 18 Control, as a compliance item in this docket, which indicate the quantity of water
 19 pumped and sold each month during the year. In the event the non-account water
 20 level for the Company exceeds 10 percent during a reporting period, the Company
 21 shall report the efforts taken to reduce water loss, such as the number of leaks
 22 repaired. If after three consecutive reports have been filed the Company's non-
 23 account water levels remain below the 10 percent threshold, Staff recommends that the
 24 reporting requirement be eliminated;
- 25 • that the Company file, within 90 days of the effective date of this Decision, with the
 26 Commission's Docket Control, as a compliance item in this docket, documentation
 27 demonstrating that the repairs as specified in Findings of Fact No. 27 have been
 28 completed;
- that the Company adopt the depreciation rates delineated in Exhibit 4 of the
 Engineering Report attached to the Staff Report on a going forward basis; and
- that Applicant, in addition to the collection of its regular rates and charges, collect
 from its customers their proportionate share of any privilege, sales, or use tax as
 provided for in A.A.C. R14-2-409(D).

32. Because an allowance for the property tax expense of Applicant is included in the
 Company's rates and will be collected from its customers, the Commission seeks assurances from the
 Company that any taxes collected from ratepayers have been remitted to the appropriate taxing
 authority. It has come to the Commission's attention that a number of water companies have been
 unwilling or unable to fulfill their obligation to pay the taxes that were collected from ratepayers,

1 some for as many as twenty years. It is reasonable, therefore, that as a preventive measure the
2 Company shall annually file, as part of its annual report, an affidavit with the Utilities Division
3 attesting that the company is current in paying its property taxes in Arizona.

4 33. Under the circumstances, after our review of the application and the Staff Report, we
5 believe Staff's proposed rates are reasonable and should be adopted together with the remainder of
6 Staff's recommendations as stated above.

7 **CONCLUSIONS OF LAW**

8 1. Applicant is a public service corporation within the meaning of Article XV of the
9 Arizona Constitution and A.R.S. §§ 40-250, 40-251, 40-301 and 40-302.

10 2. The Commission has jurisdiction over Applicant and of the subject matter of the
11 applications.

12 3. Notice of the application was provided in the manner prescribed by law.

13 4. Under the circumstances discussed herein, the rates and charges proposed by Staff and
14 authorized hereinafter are just and reasonable.

15 5. Staff's recommendations, as set forth in Findings of Fact No. 31, are reasonable and
16 should be adopted.

17 **ORDER**

18 IT IS THEREFORE ORDERED that the Cedar Grove Water, Inc. is hereby directed to file,
19 with Docket Control, as a compliance item in this docket, on or before November 30, 2007, revised
20 rate schedules setting forth the following rates and charges:

21
22 **MONTHLY USAGE CHARGE:**

23	5/8" x 3/4" Meter	\$ 20.50
	3/4" Meter	30.78
24	1" Meter	51.28
	1 1/2" Meter	102.50
25	2" Meter	164.00
	3" Meter	307.50
26	4" Meter	512.50
	6" Meter	1,025.00

GALLONAGE CHARGES:

(per 1,000 gallons)

0 to 3,000	\$ 2.00
3,001 to 9,000	\$ 3.25
Over 9,000	\$ 4.90

Bulk Water Rate (per 1,000 Gallons)	\$ 5.00
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SERVICE LINE AND METER INSTALLATION CHARGES:

(Refundable pursuant to A.A.C. R14-2-405)

5/8" x 3/4" Meter	\$ 0.00
3/4" Meter	245.00
1" Meter	350.00
1 1/2" Meter	525.00
2" Meter	700.00
3" Meter	980.00
4" Meter	1,820.00
6" Meter	3,920.00

SERVICE CHARGES:

Establishment	\$ 20.00
Establishment (After Hours)	35.00
Reconnection (Delinquent)	20.00
Meter Test (If Correct)	50.00
Deposit	*
Deposit Interest	*
Reestablishment (Within 12 Months)	**
NSF Check	20.00
Deferred Payment (Per Month)	18.00%
Meter Reread (If Correct)	15.00
Late Fee	1.50%

MONTHLY SERVICE CHARGE FOR FIRE SPRINKLERS:

4" or Smaller	***
6"	***
8"	***
10:	***
Larger than 10"	***

* Per Commission rule A.A.C. R-14-2-403(B).

** Months off system times the minimum per Commission rule A.A.C. R14-2-403(D).

*** 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 separate and distinct from the primary water service line.

1 IT IS FURTHER ORDERED that the above rates and charges shall be effective on December
2 1, 2007, for all water service.

3 IT IS FURTHER ORDERED that the Cedar Grove Water, Inc. shall notify its customers of
4 the rates and charges authorized hereinabove and the effective date of same by means of an insert, in
5 a form acceptable to Staff, in the next regular monthly billing and file a copy of the notice when sent
6 to its customers with the Commission's Docket Control as a compliance item in this docket.

7 IT IS FURTHER ORDERED that Cedar Grove Water, Inc. shall comply with each of the
8 recommendations appearing in Findings of Fact No. 31.

9 IT IS FURTHER ORDERED that Cedar Grove Water, Inc. maintain its books and records in
10 compliance with the NARUC USOA.

11 IT IS FURTHER ORDERED that Cedar Grove Water, Inc., in addition to the collection of its
12 regular rates and charges, shall collect from its customers their proportionate share of any privilege,
13 sales, or use tax as provided for in A.A.C. R14-2-409(D).

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

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

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN _____ COMMISSIONER

COMMISSIONER _____ COMMISSIONER _____ COMMISSIONER

IN WITNESS WHEREOF, I, DEAN S. MILLER, Interim Executive Director of the Arizona Corporation Commission, have hereunto set my hand and caused the official seal of the Commission to be affixed at the Capitol, in the City of Phoenix, this ____ day of _____, 2007.

DEAN S. MILLER
INTERIM EXECUTIVE DIRECTOR

DISSENT _____

DISSENT _____

MES:db

1 SERVICE LIST FOR: CEDAR GROVE WATER, INC.

2 DOCKET NOS.: W-20541A-06-0308

3

4 Mark Grapp
5 President and General Manager
6 CEDAR GROVE WATER, INC.
P. O. Box 1270
Show Low, AZ 85902

7 Christopher Kempley, Chief Counsel
8 Legal Division
9 ARIZONA CORPORATION COMMISSION
1200 West Washington Street
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10 Ernest G. Johnson, Director
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