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BEFORE THE ARIZONA CORPORATION COMMISSION

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COMMISSIONERS

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- WILLIAM A. MUNDELL
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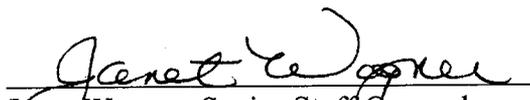
IN THE MATTER OF THE APPLICATION OF
 CHAPARRAL CITY WATER COMPANY FOR A
 DETERMINATION OF THE CURRENT FAIR
 VALUE OF ITS UTILITY PLANT AND
 PROPERTY AND FOR INCREASES IN ITS
 RATES AND CHARGES FOR UTILITY
 SERVICE BASED THEREON.

DOCKET NO. W-02113A-04-0616

NOTICE OF ERRATA

Staff hereby files a notice of errata to correct an error that appears on page 11 of its closing brief, filed on March 5, 2008. A corrected page is attached to this notice.

RESPECTFULLY submitted this 21st day of March, 2008.


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Arizona Corporation Commission
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MAR 21 2008

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Original and thirteen (13) copies of the foregoing were filed this 21st day of March, 2008 with:

Docket Control
 Arizona Corporation Commission
 1200 West Washington Street
 Phoenix, Arizona 85007

Copy of the foregoing mailed this 21st day of March, 2008 to:

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1 modern financial models directly to a FVRB creates redundancies and double counting, thereby
2 leading to excessive and unreasonable rates. The adjustments to the WACC that Staff has
3 recommended appropriately address the mismatch between the WACC and the FVRB.

4
5 **IV. THE EVIDENCE PRESENTED IN THIS CASE PROVIDES AN OPPORTUNITY**
6 **FOR THE COMMISSION TO APPLY ITS EXPERTISE AND DETERMINE AN**
7 **APPROPRIATE FVROR FOR THE COMPANY.**

8 In this case, the Commission has been presented with a number of alternative methods for
9 determining the Company's FVROR. RUCO, for example, adjusted the WACC by removing an
10 inflation factor, thereby arriving at a recommendation of 5.6. Staff's first alternative, which uses a
11 zero cost-rate for the Fair Value Increment, arrives at a recommendation of 6.34 percent. Staff's
12 second alternative, which develops a non-zero cost-rate for the Fair Value Increment, arrives at a
13 recommendation of 6.54 percent.²⁶ In addition, the record also contains testimony related to FERC's
14 method for determining a FVROR. For oil pipelines, FERC adjusts the cost of equity estimate for
15 inflation. Tr. at 203. Applying this kind of adjustment to the WACC in the present case yields a
16 FVROR of 4.28 6.39. Tr. at 162-64.

17 It may be helpful to consider these various recommendations by considering the nature of the
18 inquiry underlying the determination of a FVROR. As Staff witness Parcell stated,

19 [t]his is a process that requires the exercise of judgment. It is therefore
20 more akin to estimating the cost of equity than it is to ascertaining the cost
21 of debt. Furthermore, certain aspects of the process for estimating the cost
22 of equity are relatively well established in financial theory. No such
23 similar parallel exists for determining the fair value rate of return. This is
24 why Staff has proposed two alternative calculations for the fair value rate
25 of return in this proceeding, i.e., to provide the Commission with a sense
26 of the range for the fair value rate of return that is appropriate in this
27 case.²⁷

28 In determining an appropriate FVROR for Chaparral City, the Commission may consider all of the
29 available evidence and may use its expertise to reconcile the evidence and develop a reasonable

26 Staff's second alternative uses 1.25 percent as the cost-rate for the Fair Value Increment. This 1.25 percent is the mid-point of a range wherein the real risk-free rate is the maximum cost-rate for the Fair Value Increment and zero is the minimum cost-rate. Conceptually, the Commission could use any point within that range as the cost-rate for the Fair Value Increment.

27 Exh. S-R6 at 21.