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IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS PARADISE VALLEY WATER DISTRICT	DOCKET NO. W-01303A-05-0405
IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, INC., AN ARIZONA CORPORATION, FOR APPROVAL OF AN AGREEMENT WITH THE PARADISE VALLEY COUNTRY CLUB	DOCKET NO. W-01303A-05-0910 **ARIZONA-AMERICAN WATER COMPANY** **NOTICE OF FILING REBUTTAL TESTIMONY**

Arizona-American Water Company hereby files in the above-referenced matter rebuttal testimony of Thomas M. Broderick.

RESPECTFULLY SUBMITTED on May 6, 2008.

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BEFORE THE ARIZONA CORPORATION COMMISSION

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MIKE GLEASON, Chairman
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REBUTTAL TESTIMONY
OF
THOMAS M. BRODERICK
ON BEHALF OF
ARIZONA-AMERICAN WATER COMPANY
MAY 6, 2008

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OF
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I INTRODUCTION AND QUALIFICATIONS

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND TELEPHONE NUMBER.

A. My name is Thomas M. Broderick. My business address is 19820 N. 7th Street, Suite 201, Phoenix, Arizona 85024, and my business phone is 623-445-2420.

Q. IN WHAT CAPACITY AND BY WHOM ARE YOU EMPLOYED?

A. I am employed by American Water as Director, Rates & Regulation for operations in Arizona, New Mexico and Texas. Arizona-American Water Company ("Arizona-American") is a wholly-owned subsidiary of American Water.

Q. PLEASE DESCRIBE YOUR PRIMARY RESPONSIBILITIES FOR ARIZONA-AMERICAN.

A. I am responsible for water and wastewater rate cases and public utility regulation in Arizona, New Mexico and Texas.

Q. PLEASE DESCRIBE YOUR PROFESSIONAL EXPERIENCE AND EDUCATION.

A. For more than 20 years before joining Arizona-American in 2004, I held various management positions in the electric-utility industry with responsibilities for regulatory and government affairs, corporate economics, planning, load forecasting, finance and budgeting with Arizona Public Service Company, PG&E National Energy Group and Energy Services, and the United States Agency for International Development. I was employed at APS for nearly 14 years as Supervisor, Regulatory Affairs, then Supervisor, Forecasting, and then Manager, Planning. I was designated APS' Chief Economist in the early 1990s. For PG&E National Energy Group, I was Director, Western Region-External Relations. For USAID, I was Senior Energy Advisor to Ukraine.

I have a Masters Degree in Economics from the University of Wisconsin – Madison and a Bachelors Degree in Economics from Arizona State University.

Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THIS COMMISSION?

A. Yes, on many occasions.

II PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS CASE?

A. The purpose of my testimony is to describe action Arizona-American has already taken in response to Commission Staff's April 25, 2008, direct testimony in this proceeding and to explain additional actions that will become necessary if the Commission accepts Staff and RUCO's recommendation to deny the conversion of the existing Public Safety Surcharge to revenue accounting and to deny authorization of an ACRM-like fire flow surcharge capable of a step increase by year-end 2008.

III THE FIRE FLOW FUNDING MECHANISM PROPOSED IN THE RATE DESIGN AGREEMENT ("RDA")

Q. HAVE YOU REVIEWED THE DIRECT TESTIMONIES RECENTLY FILED BY ALL THE PARTIES?

A. Yes.

Q. DO YOU HAVE A RESPONSE?

A. Yes. In their direct testimonies, the Staff and RUCO both oppose the feature of the Rate Design Agreement ("RDA") that converts the existing Public Safety Surcharge ("PSS") to revenue accounting from Contribution in Aid of Construction ("CIAC") accounting. They also oppose the authorization of an ACRM-like surcharge capable of a step increase at year-end 2008. Both the revenue accounting and the step-increase proposed in the RDA are essential components of the RDA from Arizona-American's perspective

because the proceeds from this step increase are necessary in order to begin recovery of the now on-going construction costs of Phase 3 of the Paradise Valley Fire Flow Improvement Project ("FFIP").

Q. WHAT WOULD HAPPEN TO THE FUNDING FOR THE FFIP IF THE COMMISSION REJECTS THE ACRM-LIKE FUNDING MECHANISM PROPOSED IN THE RDA?

A. Under the RDA, only the ACRM-like step increase and the re-set High Block Surcharge ("HBS") provide the contemporaneous funding sources for Phases 3 and 4 of the FFIP. If the Commission rejects the ACRM-like step increase mechanism, it leaves only the HBS as the contemporaneous funding source for Phases 3 and 4 of the FFIP. Under the RDA, the HBS is reduced to $1.00 per 1,000 gallons from $2.15 for residential usage exceeding 80,000 gallons per month and commercial usage exceeding 400,000 gallons per month. The reduced HBS is inadequate to fund Phases 3 and 4 of the FFIP[1].

Q. WHAT ACTION HAS ARIZONA-AMERICAN ALREADY TAKEN AS A RESULT OF STAFF'S APRIL 25, 2008 TESTIMONY?

A. As a direct result of Commission Staff's testimony filed on April 25, 2008, Arizona-American Water suspended the construction of Phase 3B of the FFIP. Phase 3B of the FFIP involves the replacement of 3,300 feet of 6-inch pipe with sixteen-inch pipe along

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[1] Mr. Kiger testified in his direct testimony that the budget for Phase 3 of the FFIP is $3,720,000. He also states that the forecasted proceeds for the reduced HBS are only $772,100 for the anticipated 13 month period from a decision in this docket until a decision in the next Paradise Valley rate case. Mr. Kiger then explained that as of March 30, 2008, we still have $446,906 of Phases 1 and 2 FFIP construction and associated deferrals to pay off. While we anticipate the proceeds from both existing surcharges will be adequate to pay off Phases 1 and 2 costs in the next few months, that still leaves unfunded approximately $3 million of Phase 3 of the FFIP. It also leaves the funding of Phase 4 up in the air until the end of the next rate case.

Lincoln Drive between Tatum and Mountain View Roads, and an additional 1,750 feet of 4-inch pipe with 8-inch pipe on Tatum Boulevard between Lincoln Drive and Joshua Tree Road. The budgeted construction cost for Phase 3B is $2.3 million. The Contractor, Pierson Contracting, had begun advance work relating to the construction of Phase 3B and the actual construction of Phase 3B was scheduled to begin on May 22, 2008, with roadway trenching. Arizona-American has now ceased all work relating to Phase 3B at least until the resolution of this case. The construction of Phase 3B could remain suspended until 2009 (or later) if the Commission does not issue a decision supporting the conversion of the PSS to revenue accounting from CIAC accounting before June 30, 2008.

There are several reasons why, if the construction of Phase 3B is not resumed by June 30, 2008, it will be suspended until 2009 (or later). First, the Town of Paradise Valley ("Town") limits roadway construction to the off-peak summer season when it is less disruptive to traffic. Second, Pierson Contracting's supplier has informed us it will hold our current order for the sixteen-inch pipe only until June 30, 2008. After that date, a new order with higher cost and a later delivery date will make it impossible for Arizona-American to complete the Phase 3B construction by the Town's imposed November 2008 deadline.

Q. PLEASE DESCRIBE PHASE 3A AND ITS PRESENT STATUS.

A. Phase 3A is nearly complete. Phase 3A involves the construction of a twenty-four-inch pipeline one-half mile in length on McDonald Drive between Miller Road and Scottsdale Road in Scottsdale. This pipeline will transmit the increased volumes of water from our treatment plant to a location where future FFIP projects will distribute it further. Phase 3A's current cost estimate is $1.4 million and it is expected to be completed in June 2008 by our contractor, Hunter Contracting. Phase 3A was accelerated and begun late last year

because the City of Scottsdale was already trenching this area for one of its own underground projects. This acceleration resulted in cost savings for Phase 3A of the FFIP. Phase 3A of the FFIP is too far along to be suspended and so it will be completed on schedule. However, if the Commission accepts the RDA without the PSS step increase mechanism, our only option for cost recovery of Phase 3A costs would be as a post-test year plant addition in the new Paradise Valley rate case filed on May 1, 2008. However, even if the Commission authorizes the unrecovered portion of the Phase 3A costs be treated as a post-test year plant addition in the next Paradise Valley rate case, the costs will not go in rates until nearly a year later than under the PSS.

Q. PLEASE DESCRIBE PHASE 4 OF THE FFIP AND ITS PRESENT STATUS?

A. Phase 4 is in design and is budgeted at $3.1 million. The construction of this phase is scheduled to begin and end in 2009. It consists of installing one quarter mile of sixteen-inch pipeline on Lincoln Drive, a booster pump station at Lincoln Drive and Hillside Road, and one-half mile of 8-inch pipeline on Chaparral Road between Scottsdale Road and 68th Street. Phase 4 is likewise now suspended pending the outcome of this proceeding.

Q. IF THE COMMISSION ADOPTS STAFF AND RUCO'S POSITION OPPOSING THE CONVERSION OF THE PSS TO REVENUE ACCOUNTING WITH AN ACRM-LIKE INCREASE, WHEN MIGHT THE CONSTRUCTION OF PHASES 3B AND 4 OF THE FFIP RESUME?

A. On the assumption that the Commission will re-establish the PSS or its equivalent as a revenue surcharge upon the conclusion of the just filed Paradise Valley rate case in September 2009, Phase 3B can resume in 2010 and Phase 4 in 2011, which will push back the in-service dates of those two phases by approximately two years. To reduce the delay of Phase 4, we would consider the possibility of commencing the Phase 4

construction in 2010. Such determination requires further evaluation of our internal resource availability and consultation with the Town about multiple traffic disruptions. Please keep in mind that, under this scenario, the budgets for Phases 3B and 4 will need to be re-examined and the costs will escalate from the current estimates as a result of delay.

Q. DOES ARIZONA-AMERICAN CONTINUE TO SUPPORT THE RDA?

A. We continue to support the RDA as initially proposed by the Town with the minor revisions proposed by Mr. Kiger in his direct testimony. However, we do **not** support the RDA with the revision proposed by the Staff which opposes the conversion of the PSS to revenue accounting and denies authorization to file an ACRM-like step increase in late 2008. The unacceptable risk of the Commission granting the Staff proposed outcome has caused Arizona-American to suspend this discretionary construction.

Q. IF THE COMMISSION APPROVES THE RDA WITH THE MINOR REVISIONS PROPOSED BY MR. KIGER IN HIS DIRECT TESTIMONY BEFORE JUNE 30, 2008, WHAT WOULD HAPPEN TO THE CONSTRUCTION OF PHASES 3B AND 4 OF THE FFIP?

A. Phases 3B and 4 will resume. Phase 3B would be completed about a month later than anticipated - in November 2008. Arizona-American, of course, prefers this scenario.

Q. IF THE COMMISSION DENIES ENTIRELY THE RDA BEFORE JUNE 30, 2008, AND LEAVES THE PSS AND HBS SURCHARGES AT THEIR EXISTING LEVELS AND CIAC ACCOUNTING, WHAT WOULD HAPPEN TO THE CONSTRUCTION OF PHASES 3B AND 4 OF THE FFIP?

A. Phases 3B and 4 will resume. Phase 3B would be completed about a month later than anticipated - in November 2008. This outcome, however, would deny the rate reduction several parties to this case are seeking.

Q. COMMISSION STAFF WITNESS MR. CARLSON STATED THAT THE RDA PROPOSES TO "ELIMINATE" THE PSS. IS THAT TRUE?

A. No. The Section III(B) of the RDA is clear that the PSS will initially be "reset" to $0.00 and "would subsequently be re-established in an 'ACRM' like step increase filings...". For the record, only Mr. Carlson used the word "eliminate"

Q. DOES THAT CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.