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Attorneys for Valley Utilities Water Co., Inc.

BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF VALLEY UTILITIES WATER COMPANY INC. FOR AN INCREASE IN ITS WATER RATES FOR CUSTOMERS WITHN MARICOPA COUNTY, ARIZONA	DOCKET NO. W-01412A-99-0615
IN THE MATTER OF THE APPLICATION OF VALLEY UTILITIES WATER COMPANY INC. FOR AUTHORITY TO ISSUE PROMISSORY NOTE(S) AND OTHER EVIDENCES OF INDEBTEDNESS PAYABLE AT PREIODS OF MORE THAN TWELVE MONTHS AFTER THE DATE OF ISSUANCE	DOCKET NO. W-01412A-00-0023 **NOTICE OF FILING OF REBUTTAL TESTIMONY OF ROBERT L. PRINCE**

Notice is hereby given that on this date, Valley Utilities Water Company, Inc., filed the attached Rebuttal Testimony of Robert L. Prince along with Appendices and Attachments in the above-captioned matter.

RESPECTFULLY SUBMITTED this 13th day of November, 2008.

FENNEMORE CRAIG, P.C.

By: [signature]
Patrick J. Black
Attorneys for Valley Utilities Water Company, Inc.

Arizona Corporation Commission
DOCKETED

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ORIGINAL and **13 copies** of the foregoing
FILED this 13th day of November, 2008 with:

Docket Control
ARIZONA CORPORATION COMMISSION
1200 West Washington Street
Phoenix, AZ 85007

COPY of the foregoing was
MAILED this 13th day of November, 2008 to:

Belinda Martin
Hearing Division
ARIZONA CORPORATION COMMISSION
400 West Congress
Tucson, AZ 85701-1347

COPY of the foregoing was
HANDDELIVERED
this 13th day of November, 2008 to:

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Utilities Division
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By: Gidget Kelsey-Bacon
Gidget Kelsey-Bacon
Secretary to Patrick J. Black

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BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF VALLEY UTILITIES WATER COMPANY INC. FOR AN INCREASE IN ITS WATER RATES FOR CUSTOMERS WITHN MARICOPA COUNTY, ARIZONA	DOCKET NO. W-01412A-99-0615
IN THE MATTER OF THE APPLICATION OF VALLEY UTILITIES WATER COMPANY INC. FOR AUTHORITY TO ISSUE PROMISSORY NOTE(S) AND OTHER EVIDENCES OF INDEBTEDNESS PAYABLE AT PREIODS OF MORE THAN TWELVE MONTHS AFTER THE DATE OF ISSUANCE	DOCKET NO. W-01412A-00-0023

REBUTTAL TESTIMONY OF

ROBERT L. PRINCE

I. INTRODUCTION AND QUALIFICATIONS.

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

A. Robert L. Prince, 6808 N. Dysart Road, Suite 112, Glendale, Arizona 85307. My telephone number is (623) 935-1100.

Q. ARE YOU THE SAME ROBERT PRINCE WHO FILED DIRECT TESTIMONY IN SUPPORT OF VALLEY UTILITIES MOTION IN THESE DOCKET NUMBERS W-01412A-99-0615 AND W-01412A-00-0023?

A. Yes.

II. PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my Rebuttal Testimony is to: (1) incorporate my direct testimony in rebuttal to the Direct Testimony of Staff witness Marvin Milsap, filed on November 3, 2008, (2) to address issues related to the Company's use of excess funds in the Set-Aside account authorized in Decision No. 62908 (September 14, 2000), and (3) to file exhibits that the Company intends to use during the evidentiary hearing scheduled for November 18, 2008.

III. REBUTTAL TESTIMONY

Q. PLEASE DESCRIBE WHY YOU FEEL THAT IT IS NECESSARY TO INCORPORATE YOUR DIRECT TESTIMONY IN REBUTTAL TO STAFF WITNESS MILSAP'S DIRECT TESTIMONY.

A. It appears that Mr. Milsap's Direct Testimony is just a recount of the August 18, 2008 Staff Response filed in this proceeding. Since my Direct Testimony addresses many of the issues raised in that Staff Response, it would be duplicative to file essentially the same response.

Q. IN YOUR DIRECT TESTIMONY, YOU MAKE SEVERAL REFERENCES TO

TWO COMMISSION DECISIONS, DO YOU NOT?

A. Yes. Those would be Decision No. 62908 (September 18, 2000) and Decision No. 68309 (November 14, 2005). While I specifically asked that administrative notice be taken of these two decisions, I believe it will be much easier on all parties to introduce them as exhibits in this proceeding. Therefore, I am attaching these two orders as Exhibits BLP-2 (Decision No. 62908) and BLP-3 (Decision No. 68309).

Q. STAFF MAKES SOME SERIOUS ALLEGATIONS REGARDING THE COMPANY'S NON-COMPLIANCE WITH DECISION NO. 62908. HOW DO YOU RESPOND?

A. I strongly disagree. As I stated in my Direct Testimony, I do not believe that the Company has violated Decision No. 62908 in its maintenance of the Set-Aside Account. The excess funds in the Set-Aside Account were primarily used to pay for Valley Utilities' operating expenses, for maintenance and repair, and for emergency construction required to assure continued and reliable water service to the Company's customers. I have attached a Set-Aside Account Activity breakdown, attached hereto as Exhibit BLP-4.

Q. PLEASE CLARIFY WHAT YOU MEAN WHEN YOU USE THE TERM "EXCESS" FUNDS.

A. In Decision No. 62908, the Commission ordered Valley Utilities to set aside funds equivalent to the annual debt service requirements of the financing granted therein, which would be one-twelfth of the annual debt requirement, on a monthly basis – once the amount of the loan became known to the Company. Until then, Valley Utilities was to set-aside $6.35 from each bill per month in an interest bearing account to be used for the purpose of servicing the debt authorized in that decision. By September 2003, the Company was aware that it would likely receive a WIFA loan in the amount of $52,350 – an amount less than what had already been collected and placed into the Set-Aside account. At that point, the Company view the amount of money over $52,350 as "excess" funds, which otherwise would have gone towards paying Valley Utilities' operating expenses, maintenance and repair, and capital improvements.

Q. BUT MR. PRINCE, IT APPEARS THAT EVEN THOUGH VALLEY UTILITIES WITHDREW "EXCESS" FUNDS FROM ITS SET-ASIDE ACCOUNT TO PAY FOR THESE TYPES OF EXPENSES, THE COMPANY NONETHELESS MADE AN EFFORT TO DEPOSIT SUCH FUNDS BACK INTO THE ACCOUNT. CAN YOU PLEASE EXPLAIN WHY?

A. First, let me clarify that funds paid back into the Set-Aside account after September 2003 were not generated by specifically setting aside $6.35 from each customer's bill – that requirement was no longer applicable. The funds paid back into the Set-Aside account were generated from any "excess" revenue the Company might have in any given month. The reason we made efforts to deposit funds back into the Set-Aside account was simply because the account accrued interest, and was therefore a good vehicle to save for future needs. Unfortunately, the harsh reality of running a small water system is that it involves continual operation, maintenance, repairs and capital improvements. Excess funds over the known amount of $52,350 were withdrawn to allow the Company to continue providing water utility service to its customers.

Q. DO YOU BELIEVE THAT USING EXCESS FUNDS IN THE SET-ASIDE ACCOUNT RESULTED IN ANY HARM TO VALLEY UTILITIES' CUSTOMERS?

A. No. In fact, I believe that without being able to make these sometime extraordinary expenditures from the excess funds in the Set-Aside account, customers would have suffered a reduction in water quality and supply. I would note that Staff has not suggested in previous filings, filed in this proceeding, that the Company's customers suffered.

Q. SO, EVEN IF VALLEY UTILITIES HAD VIOLATED COMMISSION DECISION NO. 62908 AS STAFF SUGGESTS, IT IS MORE FORM OVER SUBSTANCE,

WOULD YOU AGREE?

A. I agree. Staff appears to conclude that withdrawing any funds from the Set-Aside Account, except to pay for debt service on the financing approved in Decision No. 62908, would have been in violation of a Commission order – even those excess funds above the known amount of the loan authorized in Decision No. 62908. I do not really understand this position given that the Commission's primary concern over financing in Decision No. 62908 was to avoid a situation where the Company would not be able to pay the monthly debt service, which is ironically the scenario Valley Utilities is currently trying to avoid.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes.

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EXHIBIT

BLP - 2

Arizona Corporation Commission
DOCKETED

SEP 1 8 2000

DOCKETED BY JM

BEFORE THE ARIZONA CORPORATION COMMISSION

CARL J. KUNASEK
Chairman
JIM IRVIN
Commissioner
WILLIAM A. MUNDELL
Commissioner

IN THE MATTER OF THE APPLICATION OF VALLEY UTILITIES WATER COMPANY, INC. FOR AN INCREASE IN ITS WATER RATES FOR CUSTOMERS WITHIN MARICOPA COUNTY	DOCKET NO. W-01412A-99-0615 DECISION NO. 62908
IN THE MATTER OF THE APPLICATION OF VALLEY UTILITIES WATER COMPANY, INC. FOR AUTHORITY TO ISSUE PROMISSORY NOTE(S) AND OTHER EVIDENCES OF INDEBTEDNESS PAYABLE AT PERIODS OF MORE THAN TWELVE MONTHS AFTER THE DATE OF ISSUANCE	DOCKET NO. W-01412A-00-0023 **OPINION AND ORDER**

DATE OF HEARING:	August 3, 2000
PLACE OF HEARING:	Phoenix, Arizona
PRESIDING OFFICER:	Stephen Gibelli
APPEARANCES:	Richard L. Sallquist, SALLQUIST AND DRUMMOND, P.C., on behalf of the Applicant
	Teena Wolfe, Staff Attorney, Legal Division, on behalf of the Utilities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

On October 27, 1999 and as amended on November 23, 1999, Valley Utilities Water Company, Inc. ("Applicant" or "Company" or "Valley") filed with the Arizona Corporation Commission ("Commission") an application for a rate increase.

On January 11, 2000, the Company filed an application for approval of financing in the amount of $741,755.

On January 19, 2000, the Commission's Utilities Division Staff ("Staff") filed a letter notifying the Company that its application met the sufficiency requirements outlined in A.A.C. R14-2-103 and classifying the Company as a Class C utility.

On January 21, 2000, a Procedural Order was issued which scheduled the hearing for July 28, 2000.

After a request by the Company on January 28, 2000 to extend the hearing date, a Procedural Order was issued on February 3, 2000 setting the hearing for August 3, 2000.

On April 7, 2000, Staff filed a Motion to Consolidate since it believes that the issues in these dockets are substantially related.

On April 11, 2000, the Company filed a Response to Staff's Motion indicating that they had no objection to consolidating the two matters.

On April 13, 2000, the Company filed an Affidavit of Mailing indicating that it mailed notice of its application for an increase in rates to its customers on February 28, 2000.

On May 24, 2000, the matters were consolidated by Procedural Order.

On June 2, 2000, Staff filed its Staff Report.

On June 8, 2000, the Company filed an Affidavit of Mailing indicating that it mailed notice of its financing application to its customers on May 30, 2000.

On June 30, 2000, the Company filed its rebuttal testimony.

On July 14, 2000, Staff filed its surrebuttal testimony.

On July 20, 2000, a petition signed by 136 residents in the Company's service territory was filed opposing the rate increase, as well the notice given by the Company which was provided only in English.

On July 21, 2000, the Company filed its rejoinder testimony.

On August 3, 2000, at the Commission's offices in Phoenix, Arizona, a hearing on the matter was held and public comment was taken.

DISCUSSION

Introduction

Valley is a Class C water utility company that provides public utility water service to Arizona customers. The Company was granted a Certificate of Convenience and Necessity in Decision No. 54274, dated December 20, 1984, to provide service to an area located approximately five miles west of Glendale, Arizona in Maricopa County. This system provides service to about 610 customers during the 1998 Test Year. The Company's current rates were established in Decision No. 56604, dated August 24, 1989.

The Staff Report indicates that the Company is in compliance with the Arizona Department of Water Resources ("ADWR") and had minor deficiencies with the Maricopa County Environmental Services Department ("MCESD"). The MCESD found minor deficiencies in the Operations and Maintenance requirements for this system. These deficiencies included no Emergency Operation plan, no Microbiological Site Sampling Plan, no Backflow Prevention Program, cracks in the slab at the Wellsite and no screen on the storage tank overflow. However, during Staff's field inspection, the Company demonstrated to Staff that these deficiencies were corrected.

The Company is currently delivering water that has no maximum contaminant level violations and meets the quality standards of the Safe Drinking Water Act. Staff also concluded that the Company is in compliance with all of its monitoring and reporting requirements.

Based on TY results, as adjusted by Staff, Valley suffered an operating loss of $50,904 on negative Original Cost Rate Base ("OCRB") of $292,898 resulting in no rate of return. In its rate application, Valley proposed rates that would yield a revenue level of $432,301, which would result in an operating income of $46,065, for an operating margin of 10.66 percent and a Debt Service Coverage ("DSC") ratio of 1.52. Staff recommended a revenue level of $432,301, resulting in an adjusted operating income of $48,754, for an operating margin of 11.28 percent and a DSC ratio of 2.11.

Rate Base

The Company's application utilized a rate base of negative $310,005. Staff's recommended rate base is negative $292,898 as a result of a few adjustments to the Company's application.

Staff's first set of adjustments affecting rate base were to Plant in Service. Staff is recommending a Plant in Service decrease of $11,490, from the Company proposed $1,597,758 to the Staff recommended Plant in Service of $1,586,268. Staff's first adjustment decreased Plant in Service by $12,263 based on the difference between the Company's plant accounts beginning balance of $1,005,370 versus Staff's beginning balance of $993,107 as approved in Decision No. 56604, dated August 24, 1989. Staff also made some reclassifications of items to account for the t decrease of $11,490 to $1,586,268.

Staff's second set of adjustments affecting rate base were to the Accumulated Depreciation balance. Staff's calculation for the balance of Accumulated Depreciation account totaled $945,030, versus the Company's balance of $972,905. Staff began with the $354,325 Accumulated Depreciation balance approved in the last rate case, added the depreciation expense amounts for the ensuing years and removed retirements in calculating the Test Year-end Accumulated Depreciation balance of $945,030.

Staff's final adjustment affecting rate base was an increase to the Operation and Maintenance portion of the Working Capital Allowance by $723 based on the Company's proposed amounts and Staff's adjustments to Operating Expenses.

The Company rate base schedule indicates that the Company currently has a negative rate base of $310,005. Any formal cost of capital calculation would result in a zero or negative rate of return on the Company's "investment." Therefore, Staff based its recommended rate of return on the Water Infrastructure Financing Authority ("WIFA") DSC minimum ratio of 1.20. This ratio indicates that for every dollar of debt approved in financing, the Company has $1.20 available to service the debt after operating expenses.

Revenue and Operating Expenses

Staff made no adjustments to the Operating Revenue section of the Company's application for a rate increase. Both the Company and Staff utilized an Operating Revenue figure of $325,084.

However, Staff reduced the Company's total operating expenses by $10,248 as a result of several adjustments.

Staff first and second adjustments were reclassifications. The first adjustment had the effect of reducing the Repair and Maintenance account by $1,412, from $18,445 to the Staff recommended amount of $17,033. Staff's second adjustment increased the Water Testing expenses by $4,157 to the Staff recommended level of $4,157.

Staff's third adjustment decreased Rents by $2,400 from the Company's $38,400 to Staff's recommendation of $36,000 to reflect the costs shown in the rental agreement.

Staff's fourth adjustment decreased Depreciation expense by $10,752. This adjustment is the result of the Company's use of a five percent depreciation rate versus the individual rates recommended by Engineering Staff. Staff utilized individual depreciation rates on a going-forward basis to calculate the pro forma depreciation expense and applied the five percent depreciation rate up through the Test Year.

Staff's fifth adjustment increased Property Tax expense by $810 to reflect the Company's most recently received tax bill.

Staff's sixth adjustment increased Income Tax expense by $1,292 from negative $1,242 to $50. The Company had included a negative tax based on the recorded loss. Staff then adjusted the amount to the required State minimum tax fee of $50.

Staff's seventh adjustment decreased Miscellaneous expense by $1,943 from the Company amount of $14,674 to the Staff recommended $12,731. Staff determined that the Company had included the expense of personal long distance phone calls in the Test Year expense. After a discussion between the parties, both Staff and the Company agreed that they should be excluded from the cost of service.

Staff's final adjustment increased Interest expense by $27,968 from negative $23 to $27,945, to pro forma the interest expense associated with the long-term debt for which Staff is recommending approval.

Staff's adjustments to revenues and operating expenses, as reflected in the Staff Report, are reasonable and should be adopted.

Revenue Requirement and Rate Design

Both Staff and the Company agree on a Total Operating Revenue figure of $432,301. However, the Staff Report offered a rate design different from that proposed by the Company in its application.

The Company currently charges 5/8 X 3/4 inch meter customers a monthly minimum of $8.50 with usage charges of $1.40 per thousand gallons up to 40,000 gallons usage, and $1.68 per thousand gallons for usage over 40,000 gallons. In its application, the Company proposed a minimum cha of $9.60 for 5/8 X 3/4 inch meter customers, with a charge of $1.85 per thousand gallons usage up to 30,000 gallons, and $2.30 per thousand gallons for usage over 30,000 gallons.

The Staff Report also proposed a minimum charge of $9.60 for 5/8 X 3/4 inch meter customers, but with a charge of $1.80 per thousand gallons usage up to 25,000 gallons, and $2.20 per thousand gallons for usage over 25,000 gallons. The Staff Report also proposed different rates for every meter size than those rates proposed by the Company in its application.

In its Rebuttal testimony, the Company stipulated to Staff's proposed revenue requirement, as well as Staff's proposed rates and rate design.

The Company, in its application, and Staff, in its Staff Report, had slightly different proposals regarding the Service Line and Meter Installation Charges. However, in the Rejoinder testimony of Robert Prince, the Company amended its proposed Service Line and Meter Installation Charges in Exhibit B. The Company based its charges on the Commission Engineering Division's publication of their estimated cost of Service Line and Meter Installation Charges which Staff believes to be appropriate for regulated companies. At the hearing, Staff agreed to these charges as proposed in the Company's Exhibit B.

Financing Request

On January 11, 2000, the Company filed an application for approval of long-term debt in the amount of $452,080 from WIFA and $289,675 from Robert L. Prince, President and CEO of Valley, and Barbara K. Prince, Secretary and Treasurer of Valley.

The purpose of the proposed WIFA debt is to provide funds to replace a water storage tank, replace a booster pump, replace lines and valves, install new fire hydrants, and make other improvements to the systems. The proposed Prince loan is for improvements to the system for vehicles and for certain Central Arizona Project water allocation fees.

Staff is recommending approval of the WIFA loan, but not the Prince loan. The Company currently has no long-term debt, but the Company's capital structure reflects negative equity of $264,404. Staff believes that the proposed WIFA loan is necessary to make needed improvements to the system and is consistent with sound financial practice. Staff Engineering has determined that the improvements are appropriate and the cost estimates are reasonable.

Staff believes that approval of the Prince loan would be further detrimental to the capital structure of the Company. Staff recommends that the proposed Prince loan of $289,675 should not be approved and that Company shareholders finance the remaining projects with equity.

At the hearing, the Company had no objection to Staff's recommendations regarding the proposed WIFA and Prince loans.

<u>Other Issues</u>

Staff recommended in its Report, that $6.35 per bill per month be escrowed in a separate, interest bearing bank account to be used solely for the purpose of servicing the WIFA financing requested in this case. While the Company agrees with the escrowing concept, it proposed an approach slightly different from Staff. The Company proposed in the Rebuttal testimony of Mr. Dan Niedlinger that a fixed total dollar amount that matches the debt service requirements on WIFA borrowings be deposited monthly in a separate, interest bearing account. Actual debt service requirements cannot be determined until the proposed financing is finalized and approved by WIFA. In the Surrebuttal testimony of Mr. Brian Bozzo, Staff concurred with the Company's proposal. Staff stated that the Company's proposal is efficient since it would put aside exactly the amount of funds necessary for the repayment of the WIFA loan on a monthly basis.

The Company's proposal is more efficient and accurate and will prevent excess funds in the escrow account. The Company's proposal regarding the payback of the WIFA loan takes the more reasonable approach and should be adopted. However, the debt service requirement is not known at this time. Therefore, it is reasonable for the Company to set aside $6.35 per bill per month in a separate, interest bearing account to be used solely for the purposed of servicing the WIFA financing, until the debt service requirement is known when the proposed financing is finalized and approved by WIFA.

Staff indicated in its Report that the Company was not following the National Association of Regulatory Commissioners ("NARUC") system of accounts. However, Mr. Dan L. Niedlinger in his

Rebuttal testimony on behalf of the Company, indicated that the Company is currently maintaining books and records in accordance with NARUC. Furthermore, Exhibit A of Mr. Robert L. Prince's Rejoinder testimony displays the Company's general ledger which shows that the Company is in compliance with NARUC standards. At the hearing, Mr. Brian Bozzo testified on behalf of Staff that the Company is in compliance with NARUC standards and practices.

Staff also recommends that in addition to the collection of its regular rates and charges, the Company should collect from its customers their proportionate share of any Privilege, Sales, or Use Tax where appropriate, as provided for in A.A.C. R14-2-608.D.3.

Staff further recommends that the Company be ordered to file a revised tariff amending the uninterruptible service verbiage to comply with Arizona Administrative Code and Decision No. 56604. Staff recommends that this revised Tariff be submitted within 30 days of a Commission decision in this matter to the Utilities Division Director for approval.

* * * * * * * * * *

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

FINDINGS OF FACT

1. Valley is an Arizona Corporation that was granted a Certificate of Convenience and Necessity in Decision No. 54274, dated December 20, 1984, to provide service to an area located approximately five miles west of Glendale, Arizona in Maricopa County.

2. Valley is a Class C water utility company that provides public utility water service to Arizona customers.

3. Valley's system provided service to about 610 customers during the 1998 Test Year.

4. The Company's current rates were established in Decision No. 56604, dated August 24, 1989.

5. On October 7, 1999 and as amended on November 23, 1999, Valley filed with the Commission an application for a rate increase.

6. On January 11, 2000, the Company filed an application for approval of financing in

the amount of $741,755.

7. On January 19, 2000, the Commission's Utilities Division Staff filed a letter notifying the Company that its application met the sufficiency requirements outlined in A.A.C. R14-2-103 and classifying the Company as a Class C utility.

8. After a request by the Company on January 28, 2000 to extend the hearing date, a Procedural Order was issued on February 3, 2000 setting the hearing for August 3, 2000.

9. On April 13, 2000, the Company filed an Affidavit of Mailing indicating that it mailed notice of its application for an increase in rates to its customers on February 28, 2000.

10. On May 24, 2000, the matters were consolidated by Procedural Order.

11. On June 2, 2000, Staff filed its Staff Report. The Staff Report recommended:

a) approval of its proposed rates and charges;

b) that the Company collect from its customers their proportionate share of any Privilege, Sales, or Use Tax where appropriate, as provided for in A.A.C. R14-2-608.D.3;

c) that Valley be ordered to maintain its books and records in accordance with the NARUC Uniform System of Accounts foı water utilities;

d) that the Company be ordered to file a revised tariff amending the uninterruptible service verbiage to comply with Arizona Administrative Code and Decision No. 56604. This tariff should be submitted within 30 days of a Commission decision in this matter to the Utilities Division Director for approval;

e) that $6.35 per bill, per month be set aside in a separate, interest bearing bank account to be used solely for the purpose of servicing the WIFA loan, and;

f) that the WIFA loan in the amount of $452,080 be approved and the Prince loan in the amount of $289,675 be denied.

12. On June 8, 2000, the Company filed an Affidavit of Mailing indicating that it mailed notice of its financing application to its customers on May 30, 2000.

13. On July 20, 2000, a petition signed by 136 residents in the Company's service territory

was filed opposing the rate increase as well the notice given by the Company since it was provi only in English and many residents of the area only speak Spanish.

14. On August 3, 2000, at the Commission's offices in Phoenix, Arizona, a hearing on the matter was held.

15. In its rate application, Valley proposed rates that would yield a revenue level of $432,301, which would generate an operating income of $46,065, for an operating margin of 10.66 percent and a DSC ratio of 1.52.

16. Staff recommended a revenue level of $432,301, which would result in an adjusted operating income of $48,754, for an operating margin of 11.28 percent and a DSC ratio of 2.11.

17. In its Rebuttal and Rejoinder testimony, Valley concurs with Staff's recommended revenue requirement, proposed rates, and rate design.

18. Valley's present and proposed rates and charges, as well as Staff's proposed rates and charges are as follows:

	Present Rates	Proposed Rates Company	Proposed Rates Staff
Monthly Usage Charges			
5/8" x 3/4" Meter	$8.50	$9.60	$9.60
3/4" Meter	N/A	13.00	14.50
1" Meter	17.00	21.00	24.00
1 1/2" Meter	31.00	40.00	48.00
2" Meter	49.00	64.00	77.00
3" Meter	60.00	79.00	144.00
4" Meter	80.00	105.00	240.00
6" Meter	125.00	170.00	480.00
Gallons in Minimum	1,000	0	0
Charge per 1,000 gallons:			
First 40,000 gallons of usage	$1.40		
All usage over 40,000 gallons	$1.68		
First 30,000 gallons of usage		$1.85	
All usage over 30,000 gallons		$2.30	
First 25,000 gallons of usage			$1.80
All usage over 25,000 gallons			$2.20

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DECISION NO. 62908

<u>Service Line and Meter Installation Charges</u>			
5/8" x 3/4" Meter	$150.00	$375.00	$375.00
3/4" Meter	170.00	450.00	435.00
1" Meter	210.00	500.00	510.00
1 1/2" Meter	350.00	700.00	740.00
2" Meter Turbo	500.00	1,250.00	1,300.00
3" Meter Turbo	875.00	1,800.00	1,855.00
4" Meter Turbo	1,550.00	2,750.00	2,870.00
6" Meter Turbo	3,200.00	6,700.00	5,375.00
<u>Service Charges</u>			
Establishment	$25.00	$30.00	$30.00
Establishment (After Hours)	40.00	55.00	45.00
Reconnection (Delinquent)	30.00	40.00	40.00
Meter Test (If Correct)	30.00	30.00	30.00
Deposit	*	*	*
Deposit Interest	*	*	*
Re-Establishment (Within 12 Months)	**	**	**
NSF Check	20.00	30.00	25.00
Deferred Payment	1.5%	1.5%	1.5%
Meter Re-Read (If Correct)	10.00	10.00	10.00

* Per Commission Rules (R14-2-403.B)
** Months off system times the minimum (R14-2-403.D).

12. Valley's fair value rate base ("FVRB") as indicated by the Staff Report, is determined to be negative $292,898. The Company's FVRB is the same as its OCRB.

13. Valley's current rates and charges, as adjusted by Staff, produced water revenues of $308,109 in the TY and resulted in an operating loss of $50,904.

14. Staff's adjustments to revenues and expenses, as reflected in the Staff Report, are reasonable.

15. The rates proposed by Staff, and subsequently accepted by the Company, would increase the median 5/8" x 3/4" meter bill by 31.3 percent from $17.31 to $22.73, and the average 5/8" x 3/4" meter bill by 30.8% from $20.73 to $27.13.

16. Staff's recommended rates and charges are just and reasonable.

17. The Company filed an application for approval of long-term debt in the amount of $452,080 from WIFA and $289,675 from Robert L. Prince, President and CEO of Valley, and Barbara K. Prince, Secretary and Treasurer of Valley.

18. The purpose of the proposed WIFA debt is to provide funds to replace a water storage tank, replace a booster pump, replace lines and valves, install new fire hydrants, and make other improvements to the systems.

19. The proposed Prince loan is for improvements to the system for vehicles and for certain Central Arizona Project water allocation fees.

20. Staff is recommending approval of the WIFA loan.

21. Staff Engineering has determined that the improvements are appropriate and the cost estimates are reasonable.

22. Staff recommends that the proposed Prince loan of $289,675 should not be approved since the Company has a negative equity of $264,404 and approval of the Prince loan would be detrimental to the Company's capital structure.

23. Staff recommended that the Company shareholders finance the remaining projects with equity.

24. At the hearing, the Company had no objection to Staff's recommendations regarding the proposed WIFA and Prince loans.

25. Staff proposed that $6.35 per bill, per month be set aside in a separate, interest bearing account to be used to service the WIFA loan.

26. The Company proposed that rather than set aside a fixed dollar amount per bill in the escrow account, it should set aside the amount of funds equivalent to the annual debt service requirements of the WIFA loan and set aside one-twelfth on a monthly basis.

27. The Company's proposal will offer the more accurate set aside amount, is more practical, and should be adopted.

28. Staff has indicated that the Company is current on all of its property and sales taxes.

29. The Company is in compliance with the Arizona Department of Water Resources ("ADWR").

30. The MCESD found minor deficiencies in the Operations and Maintenance requirements for this system. These deficiencies included no Emergency Operation plan, no

Microbiological Site Sampling Plan, no Backflow Prevention Program, cracks in the slab at the Wellsite and no screen on the storage tank overflow. However, during Staff's field inspection, the Company noted that these deficiencies were corrected.

31. Valley is currently delivering water that meets the quality standards of the Safe Drinking Water Act.

32. Valley is in compliance with all of its monitoring and reporting requirements.

CONCLUSIONS OF LAW

1. Valley is a public service corporation within the meaning of Article XV of the Arizona Corporation Commission and A.R.S. Sections 40-250, 40-251, 40-301, 40-302 and 40-303.

2. The Commission has jurisdiction over Valley and of the subject matter of the applications.

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

4. The rates and charges authorized hereafter are just and reasonable and should be approved without a hearing.

5. The financing approved herein is for lawful purposes, within Valley's corporate powers, is compatible with the public interest, with sound financial practices, with proper performance by Valley of service as a public service corporation, and will not impair Valley's ability tc perform that service.

6. The financing approved herein is for the purposes stated in the application and is reasonably necessary for those purposes, and such purposes are not, wholly or in part, reasonably chargeable to operating expenses or to income.

ORDER

IT IS THEREFORE ORDERED that Valley Utilities Water Company, Inc. shall file on or before September 29, 2000, the following schedule of rates and charges:

MONTHLY USAGE CHARGES

5/8" x 3/4" Meter	$9.60
3/4" Meter	14.50
1" Meter	24.00
1 ½" Meter	48.00
2" Meter	77.00
3" Meter	144.00
4" Meter	240.00
6" Meter	480.00

Charge per 1,000 Gallons:	
Usage from 1 – 25,000 gallons	$1.80
Usage over 25,000 gallons	$2.20

SERVICE LINE AND METER INSTALLATION CHARGES
(Refundable Pursuant to A.A.C. R14-2-405(B))

5/8" x 3/4" Meter	$455.00
3/4" Meter	515.00
1" Meter	590.00
1 1/2" Meter	820.00
2" Turbine Meter	1,380.00
2" Compound Meter	2,010.00
3" Turbine Meter	1,935.00
3" Compound Meter	2,650.00
4" Turbine Meter	3,030.00
4" Compound Meter	3,835.00
6" Turbine Meter	5,535.00
6" Compound Meter	7,130.00

SERVICE CHARGES

Establishment	$30.00
Establishment (After Hours)	45.00
Reconnection (Delinquent)	40.00
Meter Test (If Correct)	30.00
Deposit	*
Deposit Interest	*
Re-Establishment (Within 12 Months)	**
NSF Check	25.00
Deferred Payment (Per Month)	1.5%
Meter Re-Read (If Correct)	10.00

* Per Commission Rules (R14-2-403.B).
** Months off system times the minimum (R14-2-403.D).

IT IS FURTHER ORDERED the aforementioned rates shall become effective as of October 1, 2000.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall notify its customers of the rates and charges authorized herein and the effective date of same by means of an insert in its next regular monthly billing.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file with the Commission within 60 days from the effective date of this Decision a copy of the notice it sends to its customers of the new rates and charges.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall collect from its customers their proportionate share of any Privilege, Sales, or Use Tax where appropriate, as provided for in A.A.C. R14-2-608.D.3.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file a revised tariff amending the uninterruptible service verbiage from Sheet No. 16, Items C and D, to comply with Decision No. 56604. This revised tariff must be filed within 30 days of a Commission decision in this matter for approval by the Utilities Division Director.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc.'s request for approval of the WIFA loan in the amount of $452,080 is hereby approved.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall set aside the amount of funds equivalent to the annual debt service requirements of the WIFA loan and set aside one-twelfth on a monthly basis when the amount of the debt service requirement becomes known to the Company. Until such time as that amount is known, the Company shall set aside $6.35 per bill per month in a separate, interest bearing account to be used solely for the purpose of servicing the WIFA financing.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall submit information detailing the amount of the debt service requirement on the WIFA loan to the Utilities Division Director within 60 days of a Decision in this matter.

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. . .

. . .

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc.'s request approval of the Prince loan in the amount of $289,675 is hereby denied.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. is hereby authorized to engage in any transactions and to execute any documents necessary to effectuate the authorization granted hereinabove.

IT IS FURTHER ORDERED that such authority is expressly contingent upon Valley Utilities Water Company, Inc.'s use of the proceeds for the purposes set forth in its application.

IT IS FURTHER ORDERED that approval of the financing set forth hereinabove does not constitute or imply approval or disapproval by the Commission of any particular expenditure of the proceeds derived thereby for purposes of establishing just and reasonable rates.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file copies of all executed financing documents setting forth the terms of the financing, within 30 days of the obtaining such financing

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

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN	COMMISSIONER	COMMISSIONER

IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive Secretary 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 8th day of SEPT, 2000.

for

BRIAN C. McNEIL
EXECUTIVE SECRETARY

DISSENT ______________
SG:bbs

DECISION NO. 62908

SERVICE LIST FOR: Valley Utilities Water Company, Inc.

DOCKET NOS. W-01412A-99-0615 and W-01412B-00-0023

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DECISION NO. 68908

EXHIBIT

BLP – 3

BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission
DOCKETED

NOV 14 2005

DOCKETED BY

<u>COMMISSIONERS</u>

JEFF HATCH-MILLER, Chairman
WILLIAM A. MUNDELL
MARC SPITZER
MIKE GLEASON
KRISTIN K. MAYES

IN THE MATTER OF THE APPLICATION OF VALLEY UTILITIES WATER COMPANY, INC. FOR AN INCREASE IN ITS WATER RATES FOR CUSTOMERS WITHIN MARICOPA COUNTY, ARIZONA.	DOCKET NO. W-01412A-04-0736
IN THE MATTER OF THE APPLICATION OF VALLEY UTILITIES WATER COMPANY, INC. FOR AUTHORITY TO ISSUE PROMISSORY NOTE(S) AND OTHER EVIDENCES OF INDEBTEDNESS PAYABLE AT PERIODS OF MORE THAN TWELVE MONTHS AFTER THE DATE OF ISSUANCE.	DOCKET NO. W-01412A-04-0849 DECISION NO. 68309 **<u>OPINION AND ORDER</u>**

DATE OF PRE-HEARING CONFERENCE:	July 11, 2005
DATE OF HEARING:	July 14, 2005
PLACE OF HEARING:	Phoenix, Arizona
ADMINISTRATIVE LAW JUDGE:	Teena Wolfe
APPEARANCES:	Richard L. Sallquist, SALLQUIST, DRUMMOND & O'CONNOR, on behalf of Valley Utilities Water Company, Inc.; and David Ronald, Staff Attorney, Legal Division, on behalf of the Utilities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

On October 7, 2004, Valley Utilities Water Company, Inc. ("Valley", "Applicant" or "Company") filed an application with the Arizona Corporation Commission ("Commission") for an increase in its water rates for customers within Maricopa County, Arizona.

On November 5, 2005, the Commission's Utilities Division Staff ("Staff") issued a Letter of Deficiency indicating that Valley's application had not met the sufficiency requirements.

On November 12, 2004, Staff filed a Letter of Sufficiency indicating that Valley's application met the sufficiency requirements outlined in A.A.C. R14-2-103.

On November 26, 2004, Valley filed an application for approval for the issuance of promissory note(s) and other evidences of indebtedness in the original amount of up to $1,926,100.

On December 7, 2004, by Procedural Order, a hearing was set in the rate case for July 14, 2005.

Valley caused notice of its financing application to be published in the *Record Reporter* on December 20, 2005.

By Procedural Order issued March 23, 2005, the rate application and financing application matters were consolidated in accordance with the Company's request filed on March 17, 2005.

On April 1, 2005, an Affidavit of Mailing was filed indicating notice of the hearing was provided to all customers by first class mail as ordered in the Commission's Procedural Order dated December 7, 2004.

Intervention was granted to K. Robert Janis, TC Crownover, and James Shade.

A hearing was held as scheduled before a duly authorized Administrative Law Judge of the Commission on July 14, 2005. Public comment was taken at the commencement of the hearing. The Company and Staff appeared and presented evidence. Following the hearing, the parties filed closing briefs and the consolidated matters were taken under advisement pending the submission of a Recommended Opinion and Order to the Commission.

DISCUSSION

Valley is a Class C water utility that provided public utility water service to approximately 1,210 customers during the test year ended December 31, 2003.[1] The Company's current rates were set by the Commission in Decision No. 62908 (September 18, 2000), using a test year ending December 31, 1998. In the rate application, the Company proposed a two step rate increase and a 10 percent operating margin for each step. According to Valley, the Company has negative equity, so a meaningful cost of capital cannot be determined. Under Step 1, a 10 percent operating margin would require an increase of approximately 12.2 percent over the adjusted test year and annualized

[1] If the Company's requested surcharge mechanism to service proposed debt is approved, Valley would become a Class B utility (Tr. at 115).

revenues, or $101,800. Step 2 would also include a 10 percent operating margin ($403,000 increase), and an adjuster mechanism for recovery of arsenic treatment operating costs.[2] According to the application, during the Test Year ended December 31, 2003 ("TY"), the Company had an adjusted operating income of $13,138 (Exhibit A-1, Schedule C-1 Step 1).

Rate Base

The Company's TY rate base as filed was ($540,689) (Exhibit A-1, Application Schedule A-1 Step 1). The Company requested a waiver of the reconstruction cost new less depreciation ("RCND") schedule filing requirement and requested that its original cost rate base ("OCRB") be used as its fair value rate base ("FVRB").

Staff made two adjustments to rate base, resulting in a net increase of $885, for a FVRB of ($539,804). The first adjustment reflects capitalization of an erroneously recorded expense and the second adjustment increased Cash Working Capital. (Exhibit S-2, Rogers Direct, p 9). The Company accepted Staff's proposed adjustments, but calculated a different Cash Working Capital amount, resulting in a slightly different rate base of ($543,488) (Exhibit A-4, Bourassa Rejoinder p 5).

We agree with the adjustments made by Staff to the Company's rate base, and find that the Company's OCRB is ($539,804). Because the Company did not file RCND schedules, its FVRB is the same as its OCRB.

Revenue and Operating Expense

Staff and the Company agree that TY revenues were $827,565. The Company proposed TY expenses of $814,427. Staff made a number of adjustments to TY expense, including: a reduction in lawn service costs to reflect only that portion attributable to the Company's offices, which are located within the shareholder's domicile; an increase in water testing expenses to reflect a normalized amount; a reduction in transportation expense to remove a non-arm's length transaction involving a vehicle leased from the shareholder and the inclusion of two years' registration fees; a reduction in miscellaneous expense to remove a non-recurring recruitment expense; a reduction in directors' fees to remove "catch up" and advances in fees; a reduction in miscellaneous expense to remove long

[2] In its rebuttal testimony, the Company dropped its request for a two step increase, and instead proposed a surcharge mechanism for recovery of the arsenic treatment operating and maintenance costs (Exhibit A-3, Bourassa Rebuttal p 2).

distance personal telephone calls,[3] costs to acquire a new sign, the cost of which Staff added to rate base, gym membership expenses, and sponsorship in a high school fundraiser; and an increase in depreciation expense, property tax expense, and income tax expense (Exhibit S-2, Rogers Direct, pp 11-18, and Schedule DRR-7).

The Company accepted all of Staff's expense adjustments (Exhibit A-3, Bourassa Rebuttal, p 6). Staff's adjusted TY operating expense is $814,662, for a TY operating income of $12,903. In its rebuttal testimony, the Company dropped its request for a two step increase, and instead proposed a surcharge mechanism for recovery of the arsenic treatment operating and maintenance costs (Exhibit A-3, Bourassa Rebuttal, p 2).

Because the Company's adjusted FVRB is negative $539,804, a rate of return calculation is not meaningful. Staff recommended that the Commission authorize a 10 percent operating margin, or $957,511. This represents a $129,946, or 15.70 percent, revenue increase from $827,565 to $957,511. We agree that because the Company's FVRB is negative, it is appropriate to use an operating margin to set fair and reasonable rates. We are, however, concerned that this Company continues to operate the utility in such a way that although equity is not being invested, ratepayers are required to generate cash sufficient to show an operating income.[4] We agree with Staff's recommendation, discussed below, to require the Company to implement a plan to improve its equity position.

<u>Rate Design</u>

The Company's current rate design consists of customer charges that vary by meter size, with no gallons included. All but the 3 inch meters for commercial construction have a two tier structure, with a commodity rate of $1.80 per 1,000 gallons up to 25,000 gallons, and $2.20 per 1,000 gallons greater than 25,000.

The Company's proposed rate design applies a uniform percentage increase to all monthly minimums and changes from a two tier commodity rate to a three tier rate for all customer classes

[3] The Company requested rate recovery of these personal telecommunications expenses in its application despite the fact that the Commission specifically disallowed similar expenses in the Company's prior rate proceeding (*see* Decision No. 62908 p 5).

[4] The Company's FVRB in its last rate case was negative $292,898 (*see* Decision No. 62908 p 11).

with the exception of construction water, to assist in conservation. The breakover points graduate by meter size, with the first tier rate of $1.98, the second tier at $2.42, and the third tier at $2.662 per 1,000 gallons. According to the Company, customers using larger quantities of water will experience a higher increase due to the three tier rate design.

Staff proposed an inverted tier rate structure that includes three tiers for residential 5/8 x 3/4-inch meters and residential 3/4-inch meters, and two tiers for all others. With the residential meters, the first tier breakover point is 3,000 gallons and the second tier breakover point is 10,000 gallons. Other breakover points vary by meter size. The Company objected to Staff's recommendation, stating that the residential first tier is a "lifeline or low income" rate and that, according to the American Water Works Association ("AWWA") should only be offered to residential customers who meet certain eligibility requirements; "should not be considered unless the local cost of water service is high compared to other similar water utilities or where a significant percentage of residential customers are believed to be unable to afford water service" and should not be used in areas where there are water shortages (Exhibit A-2, Kozoman Rebuttal, pp 4-5). The Company speculates that Staff's recommended rate design may lead existing 1-inch meter customers to demand a downsizing of meter sizes, which the Company believes would cause revenue and O&M impacts, in addition to destabilization of cash flows, and which the Company believes would require monitoring to prevent what it terms "over-revving" of the smaller meters (Exhibit A-3 Prince Rebuttal, p 2). The Company acknowledged that it has not performed a cost of service study and that it is not facing water supply shortages, although it is in the Phoenix Active Management Area ("AMA").

Staff points out that the concerns asserted by Mr. Prince are also present with the Company's proposed rate design (Exhibit S-3, Rogers Surrebuttal, p 4). Staff asserts that its recommended rate design acknowledges water use patterns by meter size and in total to encourage efficient consumption, and that the Commission has recently issued decisions that adopted Staff's recommended rate design consisting of an inverted three tier rate design for residential 5/8-inch and 3/4-inch meter customers and an inverted two tier structure for all other meter sizes and customers.

We agree that Staff's recommended rate design will promote conservation by sending appropriate price signals to all customers, and find that it also addresses the goals of efficient water use, affordability, fairness, simplicity, and revenue stability. We will therefore adopt it.

Arsenic Removal/Financing Request

The U.S. Environmental Protection Agency ("EPA") has reduced the arsenic maximum contaminant level ("MCL") in drinking water from 50 parts per billion ("ppb") to 10 ppb, with a compliance date of January 23, 2006. The Company's six wells have arsenic concentrations between 7 and 13 ppb. The Company is seeking a loan from the Water Infrastructure Finance Authority of Arizona ("WIFA") to purchase and construct water treatment facilities for arsenic removal. In Decision No. 67669 (March 9, 2005), the Commission approved an Arsenic Impact Fee Tariff for the Company to help pay for debt service and/or principal on the requested WIFA loan, with the hook-up fees[5] to be treated as contributions in aid of construction ("CIAC"), and to be refunded if they are not used to pay for arsenic treatment facilities. The Company hired a consulting firm to conduct an arsenic treatment study using the treatment model methods presented in the Arizona Department of Environmental Quality's ("ADEQ") Arsenic Master Plan guidelines. A pilot study was conducted at three of the Company's wells and a final study report was completed in May 2004. The study recommended using absorption media treatment with a total treatment system cost of $1,926,100 for treatment of five of Valley's six wells. According to Staff's testimony, the Company evaluated other options such as blending and drilling new wells or deepening existing wells, but due to the high arsenic concentration and its fluctuation in the area, the Company concluded that treating the water source was the only available solution. Staff concluded that the arsenic treatment facilities are appropriate and the estimated capital costs and O&M costs are reasonable for purposes of the financing request (Exhibit S-1, Scott Direct, p *ii*).

The terms of the proposed $1,926,100 WIFA loan is 20 years, with a maximum interest rate of prime plus 200 basis points and a debt service coverage ("DSC") of at least 1.2. Payment of the loan begins six months after WIFA provides the monies to the Company, and monthly payments on the loan include both principal and interest. Staff analyzed the requested financing and testified that the Company's capital structure is composed of 100 percent negative equity, and if the financing is

[5] The approved hook-up fee is $1,100 for all new 5/8 x 3/4-inch service connections, graduated for larger meter sizes.

approved, the capital structure would be 6.3 percent short-term debt, 121.1 percent long-term debt, and 27.3 percent negative equity. According to Staff, the pro forma effect on the Company's financial ratios of obtaining the $1,926,100 WIFA loan at an interest rate of 5.0 percent and implementation of Staff's recommended rates is a Times Interest Earned Ration ("TIER") of 1.58 and a DSC of 1.86. Staff determined that an annual surcharge of approximately $185,247 would be necessary for the Company to maintain its pre-loan cash flow. Staff testified that the proposed loan "exacerbates the Company's negative equity with a debt burden, an undesirable event" (Exhibit S-2, Rogers Direct, p 26). However, Staff concluded that there are no other known options to finance the purchase/construction of the arsenic removal equipment required to comply with the EPA MCL. Staff believes that a mitigating factor is that the pro forma DSC and TIER indicate that the Company would have adequate earnings and cash flow to meet all obligations. Staff concluded that the purchase and/or construction of the arsenic removal equipment is necessary for the Company to comply with the federal rule; and that its recommended rates, which are intended to provide an operating margin that will allow the Company to attain a positive equity position, are insufficient to meet additional debt service obligations of the proposed WIFA debt.

In regard to the Company's financing request, Staff recommended:

- that the loan be approved on the terms and conditions described in the application, with the understanding that the Commission will subsequently consider an arsenic removal surcharge to enable the Company to meet its principal and interest obligations on the WIFA loan, and the incremental income taxes on the surcharge;
- that the Company be authorized to execute any documents necessary to effectuate the authorization granted;
- that the Company be ordered to provide to the Utilities Division Compliance Section copies of all executed financing documents within 60 days after the loan agreement is signed; and
- that the Company be ordered not to use any portion of the loan to pay for incurred operating or other expenses.

In relation to its recommendation regarding future Commission consideration of an arsenic removal surcharge, Staff recommended that the Company be required to:

- file in Docket Control an arsenic removal surcharge tariff application that will allow the Company to meet its principal and interest obligations on the proposed WIFA loan and income taxes on the surcharge;
- follow the same methodology set forth in Table A to the Staff testimony, to calculate the incremental revenue needed to meet the interest, principal and incremental income tax obligations on the WIFA loan, using actual loan amounts and use the result to develop its arsenic removal surcharge tariff application, which would also include the required increase in revenue calculation; and
- 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.

These Staff recommendations are reasonable and will be adopted.

Funds Set Aside Pursuant to Decision No. 62908

Decision No. 62908 set rates for the Company and approved a WIFA loan in the amount of $452,080. It also ordered the Company to "set aside the amount of funds equivalent to the annual debt service requirements of the WIFA loan and set aside one-twelfth on a monthly basis when the amount of the debt service requirement becomes known to the Company. Until such time as that amount is known, the Company shall set aside $6.35 per bill per month in a separate, interest bearing account to be used solely for the purpose of servicing the WIFA financing." It further ordered the Company to "submit information detailing the amount of debt service requirement on the WIFA loan to the Utilities Division Director within 60 days of a Decision in this matter (Decision No. 62908, p 15). The Company complied with the filing requirement on January 30, 2003, after several extensions had been granted by the Commission, but never filed copies of executed documents indicating that the Company ever obtained the approved financing. According to a compliance filing in that docket, the Company has been setting aside the required monthly amount in a segregated, interest-bearing account to be used solely for the purpose of servicing the WIFA financing (Letter from counsel for Valley to Patrick Williams dated January 4, 2002). The Company has not incurred the WIFA debt approved in Decision No. 62908, but has collected funds intended to pay that debt. The existing balance of the collected debt-service funds must either be refunded or applied to WIFA debt. Because the Company is again requesting WIFA financing, and is requesting imposition of a surcharge to pay the debt service, it would be reasonable and efficient to apply the existing balance of the collected funds to service the new WIFA debt. Under the circumstances, it is reasonable to cancel the prior WIFA financing authority, and require the Company to use the collected fund balance to service the arsenic remediation-related long-term debt authorized herein. We will therefore require the Company to file, in addition to the arsenic removal surcharge tariff application recommended by Staff, a report detailing the balance of the funds collected for debt service as authorized by Decision No. 62908, and the extent to which the application of the collected funds to debt service will offset the amount of, or the need for, an arsenic removal surcharge.

AOMRSM Request

The Company proposed an Arsenic Operating and Maintenance Recovery Surcharge Mechanism ("AOMRSM"). The Company estimates that the arsenic treatment costs will total $216,600 for the first full year of operation. Under the Company's proposal, the cost per 1,000 gallons would be determined by dividing the actual arsenic O&M costs for the year by the annual gallons sold, and a balancing account would be maintained. Each year, the Company would provide Staff a detailed calculation of the surcharge as well as provide an accounting of the amount collected during the year. According to the Company's estimations, the AOMSM charge per 1,000 gallons would be $0.84, and the impact on an average 5/8-inch customer bill would be $7.77, for a combined estimated increase of 42.94 percent over present rates. The Company estimates that the total impact of the ARSM and the AOMRSM on such a customer's monthly bill would be $14.23, for a combined increase of 67.55 percent (Exhibit A-3, Bourassa Rebuttal, p 14). Based on its estimates, the Company claims that if both surcharges are not adopted, it will experience net losses (*see* Exhibit A-4, Bourassa Rejoinder, Exhibit 3).

Staff recommended that the Company's proposed AOMRSM be disallowed and that the Company file a rate case application after a period of time, so that actual operation and maintenance costs can be determined and the appropriate rates established. Staff testified that while the costs proposed by the Company may be a reasonable estimate, they are projected costs, and to authorize estimated costs to be recovered at some future time, before they are known and measurable, would not allow Staff the opportunity to ascertain with any degree of confidence, the reasonableness of the charges and whether they are accounted for correctly (Exhibit S-3, Rogers Surrebuttal, p 6). Staff further testified that the Commission has consistently found that operation and maintenance costs associated with arsenic removal should be segregated and tracked for a period of time, and that a rate case should be filed once the actual costs become known and measurable.

We agree with Staff for several reasons. First, it would not be reasonable to require the Company's customers to pay a surcharge for O&M costs when the costs have only been estimated, and have not been subject to audit in order to determine their reasonableness and whether they are accounted for correctly. This problem is exemplified by the fact that the calculations presented in the Company's testimony overstate the effect of the Company's own estimates due to an apparent computation error involving the double-counting of interest expense. Valley presented calculations estimating net losses it will incur if its requested surcharges are not granted. The estimation calculations subtracted interest expense twice, which resulted in an understatement of cash flows to the tune of $94,988 (*see* Exhibit A-4, Bourassa Rejoinder, Exhibit 3). Correcting this error on the Company's exhibit would result in estimated positive cash flows of $55,150, instead of the Company's negative $39,838 estimated net operating loss.

Second, Decision No. 67669 has already approved a $1,100 Arsenic Impact Fee Tariff for the Company to help pay for debt service and/or principal on the requested WIFA loan.

Third, this Decision approves the concept of a surcharge to pay the debt service on the arsenic remediation-related WIFA loan once the amount of the debt service is determined and orders the Company to file an application for that surcharge. Approval of the AOMRSM in addition to the WIFA debt-service surcharge would therefore result in the Company's existing customers paying two surcharges, with new customers paying a hook-up fee in addition to the two surcharges.[6]

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[6] As an alternative to Staff's recommendation to deny the AOMRSM, Staff stated that if the Company were to fund the needed arsenic remediation plant with equity contributions instead of debt, Staff could agree in concept to permitting a

Fourth, we are approving rates herein that are based on an operating margin instead of a return on equity, in order to prevent operating losses, as discussed at page 4 above, due to the Company's ongoing negative equity position. As discussed below, we are requiring the Company to develop, submit and implement a plan to increase its equity position, because the Company has been operated in such a way that its negative equity position has continued to deteriorate, despite the fact that over a period of years, this Commission has authorized returns that provided the Company with an opportunity to increase its equity position (*see* Tr. p 112).

For these reasons, we will not approve the Company's proposed AOMRSM, but will instead consider actual operation and maintenance costs in a future rate filing, where rates can be established based on known and measurable actual costs.

<u>Shareholder/Company Transactions</u>

Staff recommended that the Company be ordered to make all reasonable efforts to institute operating policies that would remove any and all transactions between the Company and its owners that are not arm's length transactions. Based on the evidence presented in this proceeding, this is a reasonable recommendation, and it will be adopted. We will expect Staff to carefully scrutinize the Company's books in the Company's next rate case, and bring to the Commission's attention any instances of transactions between the Company and its shareholder that are not arm's length, including but not limited to the payment of personal expenses from water utility revenues, along with recommendations for appropriate Commission action.

<u>Equity Position</u>

Staff recommended that the Company be required to institute a plan that would produce a positive equity position by December 31, 2010, such plan to be filed with Docket Control within 90 days from the date of the Commission's Decision. The Company's FVRB in its last rate case was negative $292,898 (*see* Decision No. 62908, p 11), and in this case, has deteriorated further, to negative $539,804. As stated at page 4 above, we are concerned that this Company continues to operate the utility in such a way that although equity is not being invested, ratepayers are required to

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surcharge to collect the Company's first year of arsenic-related O&M costs (Tr. at 91). However, the Company made no indication at the hearing that it planned to make such an equity infusion.

generate cash sufficient to show an operating income. Staff's concerns are legitimate, and its recommendation provides a reasonable means of ameliorating the problem. We will therefore adopt Staff's recommendation. We will also direct Staff to bring to the attention of the Commission in the Company's next rate case all evidence of any inappropriate lease arrangements between the shareholder and the Company, or any other inappropriate practices that contribute to the deterioration rather than to the building of the Company's equity. The Company should be on notice that questionable expenses will be subject to disallowance in future rate proceedings.

Additional Staff Recommendations

Staff also recommended that the Company's proposed service line and meter installation charges be adopted, and that the Company use the depreciation rates in Exhibit MSJ-A, Table I-1, found in Hearing Exhibit S-1. Staff also recommended that the Company be required to file a curtailment tariff conforming to the sample tariff in Exhibit MSJ-A, Attachment K-1, found in Hearing Exhibit S-1, within 45 days after the effective date of this Decision with Docket Control, as a compliance item for Staff review and certification. These recommendations are reasonable and will be adopted.

* * * * * * * * * *

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

FINDINGS OF FACT

1. Valley is an Arizona Corporation that was granted a Certificate of Convenience and Necessity in Decision No. 54274, dated December 20, 1984, to provide service to an area located approximately five miles west of Glendale, Arizona in Maricopa County. Valley provides water utility service to approximately 1,210 customers in Maricopa County, Arizona.

2. On October 7, 2004, Valley Utilities filed an application for a rate increase for its water customers comprised of a two-step phase-in rate increase based on a test year ("TY") ending December 31, 2003. The rate application requested an operating margin of 10 percent in order to have adequate debt service coverages for a loan from WIFA to fund improvements related to arsenic removal capital improvements.

3. On November 5, 2004, Staff filed a letter informing the Company that its application had not met the sufficiency requirements outlined in A.A.C. R14-2-103.

4. Also on November 5, 2005, Valley filed a compliance status report from ADEQ.

5. On November 12, 2004, Staff filed a Letter of Sufficiency.

6. On November 26, 2004, Valley Utilities filed an application for authority to issue promissory notes and evidences of indebtedness of up to $1,926,100 to finance the purchase or construction of a plant and the equipment necessary to treat and remove arsenic from its water supply.

7. On December 7, 2004, by Procedural Order, a hearing was scheduled on Valley's rate application.

8. On January 4, 2005, Valley docketed an Affidavit of Publication certifying that it caused notice of its financing application to be published in the *Record Reporter* on December 20, 2005.

9. On March 17, 2005, the Company filed a Motion to Consolidate the financing application with the rate application for purposes of hearing, which was granted by Procedural Order issued March 23, 2005.

10. On April 1, 2005, pursuant to the Commission's Procedural Order of December 7, 2004, the Company filed an Affidavit of Mailing indicating that notice of the rate application and hearing was mailed to all customers of record in the Company's February billings.

11. Public comment was filed on April 12, 2005 and July 14, 2005, objecting to the Company's proposed rate increase.

12. On May 2, 2005, TC Crownover, James Shade and K. Robert Janis filed requests to intervene.

13. On May 2, 2005, William Clark, on behalf of Litchfield Vista View III Homeowners Association, filed a request to intervene.

14. On May 10, 2005, by Procedural Order, K. Robert Janis, TC Crownover, James Shade and William Clark were granted intervention.

15. On May 11, 2005, Staff filed its Direct Testimony.

16. On May 13, 2005, Valley filed Objections to the Procedural Order Regarding Intervention. Valley did not object to the intervention of K. Robert Janis, but stated that the intervention requests of TC Crownover, James Shade and William Clark were untimely. Valley further objected to Mr. Clark's intervention on the grounds that he is not a customer of Valley and therefore has no interest in these proceedings. Mr. Clark did not appear at the hearing to respond to the Company's objections. The May 10, 2005 Procedural Order was therefore amended at the hearing to state that Mr. Clark's intervention request is denied due to his failure to show that he would be directly and substantially affected by the outcome of this proceeding.

17. The Company and Staff docketed pre-filed testimony in accordance with the requirements of the rate case Procedural Order.

18. The hearing was held as scheduled on July 14, 2005. Mr. Charles Prokow, Ms. Almira Martinez, and Mr. Michael Fent appeared and provided public comment for the record in opposition to the level of rate increase requested by the Company. The Company and Staff appeared and presented testimony and cross-examined witnesses. Intervenor Ms. TC Crownover appeared on her own behalf and provided public comment, and also filed written public comment in the docket on the date of the hearing.[7]

19. On August 25, 2005, the Company and Staff filed Closing Briefs, and the consolidated matters were taken under advisement.

20. The rates and charges for Valley at present, as proposed in the rate application, and as recommended by Staff are as follows:

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[7] It became known at the hearing that Ms. Crownover herself is not a customer of the Company.

	Present Rates	Co. Phase One	Co. Phase Two	Staff
MONTHLY USAGE CHARGE:*				
5/8" x ¾" Meter	$ 9.60	$ 10.37	$ 14.16	$ 11.24
¾" Meter	14.50	15.66	21.38	16.87
1" Meter	24.00	25.92	35.38	28.10
1 ½" Meter	48.00	51.85	70.78	56.21
2" Meter	77.00	83.18	113.54	89.94
3" Meter	144.00	155.55	212.33	179.87
4" Meter	240.00	259.25	353.88	281.05
6" Meter	480.00	518.50	707.75	562.10
Construction Water	144.00		212.33	179.87
COMMODITY CHARGES:*				
All Meters				
1,000 to 25,000 Gallons	$ 1.80			
25,001 gallons and over	2.20			
Construction Water	2.60	2.86	4.25	$ 3.02
5/8" Meter				
1 – 8,000 gallons		1.98	2.94	
8,001 – 12,000 gallons		2.42	3.60	
12,001 gallons and over		2.662	3.9580	
3/4" Meter				
1 – 12,000 gallons		1.98	2.94	
12,001 to 18,000 gallons		2.42	3.60	
18,001 gallons and over		2.662	3.9580	
1" Meter				
1 to 20,000 gallons		1.98	2.94	
20,001 to 30,000 gallons		2.42	3.60	
30,001 gallons and over		2.662	3.9580	
1 1/2" Meter				
1 – 40,000 gallons		1.98	2.94	
40,001 to 60,800 gallons		2.42	3.60	
60,801 gallons and over		2.662	3.9580	
2" Meter				
1 – 64,000 gallons		1.98	2.94	
64,001 to 96,000 gallons		2.42	3.60	
96,001 gallons and over		2.662	3.9580	

3" Meter			
1 to 128,000 gallons	$ 1.98	$ 2.94	
128,001 to 192,000 gallons	2.42	3.60	
192,001 gallons and over	2.662	3.9580	
4" Meter			
1 to 200,000 gallons	1.98	2.94	
200,001 to 300,000 gallons	2.42	3.60	
300,001 gallons and over	2.662	3.9580	
6" Meter			
1 to 400,000 gallons	1.98	2.94	
400,001 to 600,000 gallons	2.42	3.60	
600,001 gallons and over	2.662	3.9580	
5/8" x 3/4" Meter - Residential			
1 to 3,000 gallons			$ 1.50
3,001 to 10,000 gallons			2.31
10,001 gallons and over			2.53
5/8" x 3/4" Meter - Commercial			
1 to 18,000 gallons			2.31
18,001 gallons and over			2.58
3/4" Meter – Residential			
1 to 3,000 gallons			1.50
3,001 to 10,000 gallons			2.31
10,001 gallons and over			2.53
3/4" Meter – Commercial			
1 to 18,000 gallons			2.31
18,001 gallons and over			2.58
1" Meter			
1 to 50,359 gallons			2.31
50,360 gallons and over			2.53
1 1/2" Meter			
1 to 126,054 gallons			2.31
126,055 gallons and over			2.53
2" Meter			
1 to 151,256 gallons			2.31
151,257 gallons and over			2.53

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<u>3" Meter</u>	
1 to 403,274 gallons	$ 2.31
403,275 gallons and over	2.53
<u>4" Meter</u>	
1 to 453,722 gallons	2.31
453,723 gallons and over	2.53
<u>6" Meter</u>	
1 to 1,260,313 gallons	2.31
1,260,314 gallons and over	2.53

*In addition to the collection of regular rates, the utility will collect from its customers a proportionate share of any privilege, sales, use and franchise tax per Commission Rule R14-2-409.D.5.

<u>SERVICE LINE AND METER INSTALLATION CHARGES</u>:**
(Refundable pursuant to A.A.C. R14-2-405)

	Present Meter and Service Line Installation Charge	Proposed Service Line Inst. Charge Co.	Proposed Meter Inst. Charge Co.	Total Proposed Charge Co.	Total Proposed Inst. Charge Staff
5/8 x ¾ Inch	$ 455.00	$385.00	135.00	$ 520.00	$ 520.00
3/4 Inch	515.00	385.00	215.00	600.00	600.00
1 Inch	590.00	435.00	255.00	690.00	690.00
1 ½ Inch	820.00	470.00	465.00	935.00	935.00
2 Inch/Turbine	1,380.00	630.00	965.00	1,595.00	1,595.00
2 Inch/Compound	2,010.00	630.00	1,690.00	2,320.00	2,320.00
3 Inch/Turbine	1,935.00	805.00	1,470.00	2,275.00	2,275.00
3 Inch/Compound	2,650.00	845.00	2,265.00	3,520.00	3.520.00
4 Inch/Turbine	3,030.00	1,170.00	2,350.00	3,520.00	3,520.00
4 Inch/Compound	3,835.00	1,230.00	3,245.00	4,475.00	4,475.00
6 Inch/Turbine	3,535.00	1,730.00	4,545.00	6,275.00	6,275.00
6 Inch/Compound	7,130.00	1,770.00	6,280.00	8,050.00	8,050.00
8 Inch	At Cost	At Cost	At Cost	At Cost	At Cost
10 Inch	At Cost	At Cost	At Cost	At Cost	At Cost
12 Inch	At Cost	At Cost	At Cost	At Cost	At Cost

** All advances and/or contributions are to include labor, materials, overheads, and applicable taxes, including gross-up taxes for income taxes, if applicable. As meters and service lines are now taxable income for income purposes, the Company shall collect income taxes on the meter and service line charges. Any tax collected will be refunded each year that the meter deposit is refunded.

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SERVICE CHARGES:	Present Rates	Proposed Rates Company	Staff
Establishment	$ 30.00	$ 30.00	$ 30.00
Establishment (After Hours)	45.00	45.00	45.00
Reconnection (Delinquent) (b)	40.00	40.00	40.00
Reconnection (Delinquent and After Hours) (b)	$ 40.00	$ 40.00	$ 40.00
Meter Test	30.00	30.00	30.00
Deposit Requirement	(a)	(a)	(a)
Deposit Interest	6%	6%	6%
Reestablishment (Within 12 Months)	(b)	(b)	(b)
Reestablishment (After Hours)	(b)	(b)	(b)
NSF Check (per Rule R14-2-409.F)	25.00	25.00	25.00
Deferred Payment, Per Month	1.50%	1.50%	1.50%
Meter Reread (per Rule R14-2-408.C)	10.00	10.00	10.00
Charge of Moving Customer Meter – Customer Requested	Cost	Cost	Cost
After hours service charge	25.00	25.00	25.00

(a) Residential – two times the average bill. Non-Residential – two and one-half times the average bill.

(b) Per Rule R14-2-403.D.

21. Valley's present rates and charges produced adjusted TY operating revenues of $827,565 and adjusted TY operating expenses of $814,662, for a TY operating income of $12,903.

22. The Company's OCRB is ($539,804). The Company did not file RCND schedules. The Company's FVRB is therefore determined to be ($539,804).

23. Because the Company's adjusted FVRB is negative $539,804, a rate of return calculation is not meaningful. Based on the unique circumstances of this case, it is appropriate to use an operating margin to set fair and reasonable rates, and to allow a 10 percent operating margin, for revenues of $957,511. This represents a $129,946, or 15.70 percent, revenue increase from $827,565 to $957,511. In the Company's next rate filing, if the Company again requests use of an operating margin in lieu of a rate of return calculation, consideration will be given to the strength of the Company's efforts to improve its equity position.

24. Average and median usage during the TY for the Company's 593 3/4-inch meter

residential customers were 10,134 and 7,500 gallons per month, respectively; and average and median usage during the TY for the Company's 256 5/8 x 3/4-inch meter residential customers were 9,251 and 6,500 gallons per month, respectively.

25. The rate schedule adopted herein will increase the average residential 5/8 x 3/4-inch meter customer's monthly bill by $3.93, from $30.18 to $34.11, or 14.97 percent, and the median 5/8 x 3/4-inch meter customer's monthly bill by $2.53, from $23.83 to $26.36, or 11.86 percent. The average residential 3/4-inch meter customer's monthly bill will increase by $5.14, from $37.88 to $43.02, or 15.69 percent, and the median residential 3/4-inch meter customer's monthly bill will increase by $3.76, from $31.76 to $35.52, or 13.45 percent.

26. The Company proposes three-tier rates for all customer classes with the exception of construction water, and disagrees with Staff's rate design, which provides three-tiers only for residential customers and two tiers for all other customers. The Company believes that Staff's proposed first-tier rates are equivalent to a "lifeline" rate, which it asserts should only be offered to residential customers who meet certain eligibility requirements. The Company speculates that Staff's recommended rate design may lead existing 1-inch meter customers to demand a downsizing of meter sizes, leading to revenue and O&M impacts and destabilization of cash flows. However, no cost of service study was performed, and Staff testified that the Company's concerns regarding possible meter downsizing may also exist with the Company's recommendation.

27. Staff's recommended rate design acknowledges water use patterns by meter size and in total to encourage efficient consumption. The inverted three tier rate design for residential 5/8-inch and 3/4-inch meter customers and an inverted two tier structure for all other meter sizes and customers as proposed by Staff is reasonable and will be adopted because it will promote conservation by sending appropriate price signals to all customers; and because it addresses the goals of efficient water use, affordability, fairness, simplicity, and revenue stability.

28. Valley's system consists of six wells, five storage tanks, four booster stations, and a distribution system, with a source capacity of 1,060 gallons per minute ("GPM") and storage capacity of 1,060,000 gallons. According to Staff, the existing system has adequate production and storage capacity to serve the present customer base and reasonable growth.

29. Staff reviewed the arsenic treatment facilities Valley proposed in the financing application. Based on its analysis, Staff's engineering section concluded that the proposed arsenic treatment facilities to be financed are appropriate, and recommended that the Company's estimated capital costs and O&M costs be used for purposes of processing the financing request.

30. Under the circumstances of this case, it is reasonable to approve the Company's financing request on the terms and conditions described in the application, with the proceeds to be used solely for capital expenditures, and not operating or other expenses, and to require the Company to file, as recommended by Staff, an arsenic removal surcharge tariff application for subsequent approval of a surcharge that will allow Valley to meet its principal and interest obligations on the amount of the WIFA loan and income taxes on the surcharges.

31. For the reasons described herein, it is not in the public interest to approve in this Decision the Company's request for a surcharge to service the financing for which authority is requested in this proceeding.

32. The debt authority granted in Decision No. 62908 was never utilized and should be cancelled. It is reasonable to require that the funds the Company has collected for the sole purpose of servicing the WIFA debt approved in Decision No. 62908 be applied to service the WIFA debt for which authority is requested in this proceeding.

33. The Company should be required to file with Docket Control, within 30 days, a report that provides detailed information regarding the balance of the funds the Company has collected for the sole purpose of servicing the WIFA debt approved in Decision No. 62908, which debt was never issued. The report should also include an analysis of the extent to which the application of the collected funds to service the debt approved in this proceeding will offset the amount of, or the need for, a surcharge to service the WIFA loan for arsenic removal capital projects.

34. In relation to the WIFA financing approved herein, it is reasonable to require the Company to follow the methodology set forth in Table A-DRR attached to Hearing Exhibit S-2, to calculate the incremental revenue needed to meet the interest, principal and incremental income tax obligations on the WIFA loan, using actual loan amounts and use the result to develop its arsenic removal surcharge tariff application, which would also include the required increase in revenue

calculation. The Company shall also include in its revenue increase calculation the offsets provided by the application of the previously-collected funds pursuant to Decision No. 62908 to service the debt, and the offsets provided by hook-up fees collected pursuant to Decision No. 67669 (March 9, 2005), which approved an Arsenic Impact Fee Tariff for the Company to help pay for debt service and/or principal on the requested WIFA loan; and shall file 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.

35. Based on the evidence in this proceeding, it is reasonable to require the Company to make all reasonable efforts to institute operating policies to remove any and all transactions between the Company and its owners that are not arm's length transactions. It is also reasonable to require Staff to carefully scrutinize the Company's books in the Company's next rate case, and bring to the Commission's attention any instances of transactions between the Company and its shareholder that are not arm's length, including but not limited to improper lease arrangements and payment of personal expenses, along with recommendations for appropriate Commission action.

36. It is reasonable to require the Company to develop and institute a plan that would produce a positive equity position by December 31, 2010, and to file a copy of the plan as a compliance item in this docket within 90 days. It is also reasonable to require Staff to bring to the attention of the Commission in the Company's next rate case all evidence of any inappropriate lease arrangements between the shareholder and the Company, or any other inappropriate practices, that contribute to the deterioration rather than to the building of the Company's equity.

37. It is not in the public interest to grant the Company's proposed AOMRSM.

38. It is reasonable to require the Company to file a curtailment tariff as recommended by Staff within 45 days with Docket Control, as a compliance item for Staff review and certification.

39. The Company's proposed service line and meter installation charges are reasonable and should be adopted.

40. Staff testified that the Company has no outstanding compliance issues with the Commission.

41. Staff testified that Valley's TY water loss is 1.96 percent, within acceptable limits.

42. Staff testified that the Company is currently delivering water that meets water quality standards required by the Arizona Administrative Code, Title 18, Chapter 4.

43. The Company is located within the Arizona Department of Water Resources' ("ADWR") Phoenix AMA. Staff testified that the Company is in compliance with the AMA reporting and conservation requirements

44. Because an allowance for the property tax expense of Valley Utilities 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, some for as many as twenty years. It is reasonable, therefore, that as a preventive measure Valley Utilities should 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.

CONCLUSIONS OF LAW

1. Valley is a public service corporation within the meaning of Article XV of the Arizona Corporation Commission and A.R.S. Sections 40-250, 40-251, 40-301, 40-302 and 40-303.

2. The Commission has jurisdiction over Valley and of the subject matter of the applications.

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

4. The rates and charges authorized herein are just and reasonable and should be approved without a hearing.

5. The financing approved herein is for lawful purposes, within Valley's corporate powers, is compatible with the public interest, with sound financial practices, with proper performance by Valley of service as a public service corporation, and will not impair Valley's ability to perform that service.

6. The financing approved herein is for the purposes stated in the application and is reasonably necessary for those purposes, and such purposes are not, wholly or in part, reasonably chargeable to operating expenses or to income.

ORDER

IT IS THEREFORE ORDERED that Valley Utilities Water Company Inc. shall file with the Commission's Docket Control Center, as a compliance item in this docket, on or before November 30, 2005, the following schedule of rates and charges:

MONTHLY USAGE CHARGE:

5/8" x ¾" Meter	$ 11.24
¾" Meter	16.87
1" Meter	28.10
1 ½" Meter	56.21
2" Meter	89.94
3" Meter	179.87
4" Meter	281.05
6" Meter	562.10
Construction Water	179.87

COMMODITY CHARGES:*

Construction Water	3.02
5/8" x 3/4" Residential Meter	
1 to 3,000 gallons	1.50
3,001 to 10,000 gallons	2.31
10,001 gallons and over	2.53
5/8" x 3/4" Meter - Commercial	
1 to 18,000 gallons	2.31
18,001 gallons and over	2.58
3/4" Meter - Residential	
1 to 3,000 gallons	1.50
3,001 to 10,000 gallons	2.31
10,001 gallons and over	2.53
3/4" Meter - Commercial	
1 to 18,000 gallons	2.31
18,001 gallons and over	2.58
1" Meter	
1 to 50,359 gallons	2.31
50,360 gallons and over	2.53
1 1/2" Meter	
1 to 126,054 gallons	2.31
126,055 gallons and over	2.53

2" Meter	
1 to 151,256 gallons	$ 2.31
151,257 gallons and over	2.53
3" Meter	
1 to 403,274 gallons	2.31
403,275 gallons and over	2.53
4" Meter	
1 to 453,722 gallons	2.31
453,723 gallons and over	2.53
6" Meter	
1 to 1,260,313 gallons	2.31
1,260,314 gallons and over	2.53

*In addition to the collection of regular rates, the utility will collect from its customers a proportionate share of any privilege, sales, use and franchise tax per Commission Rule R14-2-409.D.5.

SERVICE LINE AND METER INSTALLATION CHARGES: **
(Refundable pursuant to A.A.C. R14-2-405)

	Service Line Inst. Charge	Meter Inst. Charge	Total Inst. Charge
5/8 x ¾ Inch	$ 385.00	$ 135.00	$ 520.00
3/4 Inch	385.00	215.00	600.00
1 Inch	435.00	255.00	690.00
1 ½ Inch	470.00	465.00	935.00
2 Inch/Turbine	630.00	965.00	1,595.00
2 Inch/Compound	630.00	1,690.00	2,320.00
3 Inch/Turbine	805.00	1,470.00	2,275.00
3 Inch/Compound	845.00	2,265.00	3,520.00
4 Inch/Turbine	1,170.00	2,350.00	3,520.00
4 Inch/Compound	1,230.00	3,245.00	4,475.00
6 Inch/Turbine	1,730.00	4,545.00	6,275.00
6 Inch/Compound	1,770.00	6,280.00	8,050.00
8 Inch	At Cost	At Cost	At Cost
10 Inch	At Cost	At Cost	At Cost
12 Inch	At Cost	At Cost	At Cost

** All advances and/or contributions are to include labor, materials, overheads, and applicable taxes, including gross-up taxes for income taxes, if applicable. As meters and service lines are now taxable income for income purposes, the Company shall collect income taxes on the meter and service line charges. Any tax collected will be refunded each year that the meter deposit is refunded.

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SERVICE CHARGES:

Establishment	$ 30.00
Establishment (After Hours)	45.00
Reconnection (Delinquent) (b)	40.00
Reconnection (Delinquent and After Hours) (b)	40.00
Meter Test (If Correct)	30.00
Deposit Requirement	(a)
Deposit Interest	6%
Reestablishment (Within 12 Months)	(b)
Reestablishment (After Hours)	(b)
NSF Check (per Rule R14-2-409.F)	25.00
Deferred Payment, Per Month	1.50%
Meter Reread (per Rule R14-2-408.C)	10.00
Charge of Moving Customer Meter – Customer Requested	Cost
After hours service charge	25.00

(a) Residential – two times the average bill.
Non-Residential - two and one-half times the average bill.
(b) Per Rule R14-2-403.D.

Monthly Service Charge for Fire Sprinkler: ***

*** 1% of Monthly Minimum for a Comparable Size 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.

IT IS FURTHER ORDERED that the above rates and charges shall be effective for all service provided on and after December 1, 2005.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall notify its customers of the revised rates and charges authorized herein, and their effective date, in a form acceptable to the Commission's Utilities Division Staff, by means of an insert in its next regularly scheduled billing.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file with the Commission's Docket Control, as a compliance item in this docket, a copy of the notice it sends to its customers within 60 days of the effective date of this Decision.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc.'s request for approval of the WIFA loan in the amount of $1,926,100 is hereby approved.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. is hereby authorized to engage in any transactions and to execute any documents necessary to effectuate the authorization granted hereinabove.

IT IS FURTHER ORDERED that such authority is expressly contingent upon Valley Utilities Water Company, Inc.'s use of the proceeds for the purposes set forth in its application.

IT IS FURTHER ORDERED that approval of the financing set forth hereinabove does not constitute or imply approval or disapproval by the Commission of any particular expenditure of the proceeds derived thereby for purposes of establishing just and reasonable rates.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file copies of all executed financing documents setting forth the terms of the financing, within 30 days of the obtaining such financing.

IT IS FURTHER ORDERED that the financing authority granted to Valley Utilities Water Company, Inc. in Decision No. 62908 but which was never utilized, is hereby cancelled.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. file with Docket Control, as a compliance item in this docket, within 30 days of this Decision, a report that provides detailed information regarding the balance of the funds the Company has collected for the sole purpose of servicing the WIFA debt approved in Decision No. 62908, which debt was never issued. The report shall also include an analysis of the extent to which application of the collected funds to service the debt approved in this proceeding will offset the amount of, or the need for, a surcharge to service the financing approved herein.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file with Docket Control an application for approval of an arsenic removal surcharge tariff if a surcharge is necessary to allow Valley Utilities Water Company, Inc. to meet its principal and interest obligations on the amount of the WIFA loan and income taxes on the surcharges.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall file with Docket

Control, as a compliance item in this docket, 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. The revenue calculation shall include the effects of 1) the application of the previously-collected funds referenced in the previous Ordering Paragraph to service the debt authorized herein, and 2) hook-up fees collected pursuant to Decision No. 67669 (March 9, 2005), which approved an Arsenic Impact Fee Tariff for the Company to help pay for debt service and/or principal on the requested WIFA loan.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall institute operating policies to remove any and all transactions between the Company and its owners that are not arm's length transactions.

IT IS FURTHER ORDERED that the Commission's Utilities Division Staff shall carefully scrutinize Valley Utilities Water Company, Inc.'s books in its next rate case, and bring to the Commission's attention any instances of transactions between the Valley Utilities Water Company, Inc. and its shareholder that are not arm's length, including but not limited to improper lease arrangements and payment of personal expenses, along with recommendations for appropriate Commission action.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc. shall develop and institute a plan to produce a positive equity position by December 31, 2010, and shall file a copy of the plan, with the Commission's Docket Control, as a compliance item in this docket within 90 days.

IT IS FURTHER ORDERED that in Valley Utilities Water Company, Inc.'s next rate proceeding, the Commission's Utilities Division Staff shall bring to the attention of the Commission all evidence of any inappropriate practices that contribute to the deterioration of, rather than to the building of, equity.

IT IS FURTHER ORDERED that Valley Utilities Water Company, Inc.'s request for an Arsenic Operating and Maintenance Recovery Surcharge Mechanism is hereby denied.

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IT IS FURTHER ORDERED that Valley Utilities Water Company, 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, BRIAN C. McNEIL, 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 14th day of NOV., 2005.

BRIAN C. McNEIL
EXECUTIVE DIRECTOR

DISSENT ____________________

DISSENT ____________________

EXHIBIT

BLP – 4

Valley Utilities Water Co., Inc.

Set Aside Breakdown

DATE	DEPOSIT AMOUNT	AMOUNT WITHDRAWN	REASON	BALANCE
12/5/2000	4032.25		Nov. 00	4032.25
12/31/2000	5.19		Int.	4037.44
1/31/2001	5.97		Int.	4043.41
2/28/2001	4.65		Int.	4048.06
3/31/2001	5.12		Int.	4053.18
4/30/2001	4.82		Int.	4058
5/31/2001	4.27		Int.	4062.27
6/27/2001	24580.85		Dec. 00 - May 01 (6 mos.)	28643.12
6/30/2001	9.05		Int.	28652.17
7/31/2001	42.34		Int.	28694.51
8/31/2001	42.29		Int.	28736.8
9/5/2001	4115		July. 01	32851.8
9/30/2001	38.75		Int.	32890.55
10/31/2001	34.64		Int.	32925.19
11/1/2001	4178.3		Sept. 01	37103.49
11/30/2001	34.86		Int.	37138.35
12/20/2001	4502.15		Nov. 01	41640.5
12/31/2001	32.03		Int.	41672.53
1/18/2002	4578.35		Dec. 01	46250.88
1/31/2002	33.42		Int.	46284.3
2/14/2002	4768.85		Jan. 02	51053.15
2/28/2002	35.8		Int.	51088.95
3/20/2002	5022.85		Feb. 02	56111.8
3/31/2002	41.95		Int.	56153.75
4/15/2002	5105.4		Mar. 02	61259.15
4/30/2002	51.45		Int.	61310.6
5/30/2002	5416.55		Apr. 02	66727.15
5/31/2002	52.35		Int.	66779.5
6/26/2002	5746.75		May. 02	72526.25
6/30/2002	51.68		Int.	72577.93
7/31/2002	65.6		Int.	72643.53
8/22/2002	6203.95		July. 02	78847.48
8/31/2002	59.27		Int.	78906.75
9/11/2002	6286.5		Aug. 02	85193.25
9/30/2002	63.24		Int.	85256.49
10/21/2002	6375.4		Sept. 02	91631.89
10/31/2002	66.72		Int.	91698.61
11/25/2002	6375.4		Oct. 02	98074.01
11/30/2002	57.53		Int.	98131.54
12/31/2002	64.49		Int.	98196.03
1/30/2003	6578.6		Nov. 02	104774.63
1/30/2003	6642.1		Dec. 02	111416.73
1/31/2003	63.06		Int.	111479.79
2/28/2003	64.11		Int.	111543.9
3/19/2003	6889.75		Feb. 03	118433.65
3/31/2003	72.86		Int.	118506.51

Valley Utilities Water Co., Inc.

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DATE	DEPOSIT AMOUNT	AMOUNT WITHDRAWN	REASON	BALANCE
4/25/2003	6985		Mar. 03	125491.51
4/30/2003	73.88		Int.	125565.39
5/21/2003	7270.75		Apr. 03	132836.14
5/30/2003	78.86		Int.	132915
6/12/2003	7454.9		May. 03	140369.9
6/30/2003	87.54		Int.	140457.44
7/15/2003	7531.1		June. 03	147988.54
7/31/2003	87.84		Int.	148076.38
8/8/2003	7620		July. 03	155696.38
8/29/2003	79.01		Int.	155775.39
9/10/2003	7600.95		Aug. 03	163376.34
9/30/2003	90.31		Int.	163466.65
10/9/2003		10000	Operating expense short (payroll)	153466.65
10/15/2003		12000	Operating expense short (LX paybacks)	141466.65
10/31/2003	76.29		Int.	141542.94
11/12/2003	7543.8		Oct. 03	149086.74
11/17/2003		10000	Operating expense short (accounts payable)	139086.74
11/28/2003	60.97		Int.	139147.71
12/8/2003	4200		Dec. 03	143347.71
12/31/2003	70.67		Int.	143418.38
1/30/2004	64.79		Int.	143483.17
2/27/2004	12.96		Int.	143496.13
4/2/2004		20000	Operating expense short (accounts payable)	123496.13
5/2/2004		5000	Operating expense short (payroll)	118496.13
5/12/2004	2500		Transfer of operating funds	120996.13
5/12/2004		510	Wifa project engineering invoice	120486.13
6/9/2004		2871.49	Wifa project engineering invoice	117614.64
9/8/2004	5845.37		Transfer of operating funds	123460.01
9/30/2004	5845.37		Transfer of operating funds	129305.38
11/1/2004	2500		Transfer of operating funds	131805.38
11/1/2004	5845.37		Transfer of operating funds	137650.75
11/30/2004	77.83		Int.	137728.58
12/10/2004	2922.69		Transfer of operating funds	140651.27
12/31/2004	160.55		Int.	140811.82
1/14/2005		5000	Arsenic Remediation Coalition dues	135811.82
1/31/2005	180.36		Int.	135992.18
2/10/2005		10000	Operating expense short (payroll)	125992.18
2/28/2005	156.56		Int.	126148.74
2/28/2005	2922.69		Transfer of operating funds	129071.43
3/11/2005		10000	Operating expense short (payroll & income taxes)	119071.43
3/28/2005		20000	Operating expense short (insurance & well repair #4 well)	99071.43
3/31/2005	179.32		Int.	99250.75
4/6/2005		10000	Operating expense short (payroll)	89250.75
4/29/2005	127.28		Int.	89378.03
5/31/2005	140.25		Int.	89518.28
6/16/2005	5845.37		Transfer of operating funds	95363.65
6/30/2005	138.72		Int.	95502.37

Valley Utilities Water Co., Inc.

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DATE	DEPOSIT AMOUNT	AMOUNT WITHDR AWN	REASON	BALANCE
7/1/2005		119	Attorney stmt. 12/3/04 for Wifa loan closing	95383.37
7/29/2005	144.17		Int.	95527.54
8/31/2005	171.11		Int.	95698.65
9/29/2005	5845.37		Transfer of operating funds	101544.02
9/30/2005	172.72		Int.	101716.74
10/18/2005		265.58	Wifa project engineering invoice	101451.16
10/31/2005	224.27		Int.	101675.43
11/16/2005		323.75	Wifa project engineering invoice	101351.68
11/30/2005	222.79		Int.	101574.47
12/27/2005		565.35	Wifa project engineering invoice	101009.12
12/27/2005		38.57	Wifa project engineering invoice	100970.55
12/27/2005	1500		Transfer of operating funds	102470.55
12/31/2005	226.1		Int.	102696.65
1/26/2006	5000		Transfer of operating funds	107696.65
1/31/2006	250.36		Int.	107947.01
2/21/2006	3500		Transfer of operating funds	111447.01
2/28/2006	238.14		Int.	111685.15
3/29/2006	3500		Transfer of operating funds	115185.15
3/31/2006	271.26		Int.	115456.41
4/26/2006		51000	Operating expense short (payroll & accounts payable)	64456.41
4/28/2006	214.15		Int.	64670.56
4/28/2006	33.94		Int.	64704.5
5/8/2006		9200	Operating expense short (payroll & accounts payable)	55504.5
5/31/2006	149.99		Int.	55654.49
6/20/2006	10000		Transfer of operating funds	65654.49
6/30/2006	145.83		Int.	65800.32
7/31/2006	170.99		Int.	65971.31
8/31/2006	171.44		Int.	66142.75
9/29/2006	160.79		Int.	66303.54
10/31/2006	177.86		Int.	66481.4
11/30/2006	166.19		Int.	66647.59
12/29/2006	159.37		Int.	66806.96
1/31/2007	183.88		Int.	66990.84
2/28/2007	164.44		Int.	67155.28
3/29/2007	10000		Transfer of operating funds	77155.28
3/30/2007	174.56		Int.	77329.84
4/30/2007	200.95		Int.	77530.79
5/31/2007	201.48		Int.	77732.27
6/14/2007		24579.91	Operating expense short (LPSCO tie in & accounts payable)	53152.36
6/29/2007	149.72		Int.	53302.08
7/31/2007	131.66		Int.	53433.74
7/31/2007		10464.34	Operating expense short (LPSCO tie in)	42969.14
8/31/2007	102.54		Int.	43071.94
9/28/2007	86.55		Int.	43158.49
10/31/2007	91.67		Int.	43250.16
10/31/2007	10000		Transfer of operating funds	53250.16
11/30/2007	95.75		Int.	53345.91

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12/12/2007	6500		Transfer of operating funds	59845.91
12/31/2007	96.19		Int.	59942.1
1/23/2008	6500		Transfer of operating funds	66442.1
1/31/2008	83.09		Int.	66525.19
2/15/2008	6500		Transfer of operating funds	73025.19
2/29/2008	55.64		Int.	73080.83
3/31/2008	54.05		Int.	73134.88
4/30/2008	45.32		Int.	73180.2
5/31/2008	45.35		Int.	73225.55
6/30/2008	46.89		Int.	73272.44
7/31/2008	46.92		Int.	73319.36
8/31/2008	43.9		Int.	73363.26
9/30/2008	48.22		Int.	73411.48