



0000093049

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

BEFORE THE ARIZONA CORPORATION

IN THE MATTER OF THE APPLICATION)
OF CHAPARRAL CITY WATER COMPANY,)
INC., AN ARIZONA CORPORATION,)
FOR A DETERMINATION OF THE FAIR)
VALUE OF ITS UTILITY PLANT AND)
PROPERTY AND FOR INCREASES IN)
ITS RATES AND CHARGES FOR)
UTILITY SERVICE BASED THEREON.)

DOCKET NO.
W-02113A-07-0551

**EVIDENTIARY
HEARING**

At: Phoenix, Arizona
Date: December 10, 2008
Filed: **DEC 31 2008**

RECEIVED
2008 DEC 31 P 2:48
AZ CORP COMMISSION
DOCKET CONTROL

REPORTER'S TRANSCRIPT OF PROCEEDINGS

VOLUME III

Arizona Corporation Commission (Pages 355 through 444)

DOCKETED

DEC 31 2008

DOCKETED BY *[Signature]*

ARIZONA REPORTING SERVICE, INC.
Court Reporting
Suite 502
2200 North Central Avenue
Phoenix, Arizona 85004-1481

ORIGINAL

By: MICHELE E. BALMER
Certified Reporter
Certificate No. 50489

Prepared for:

ACC

**FOR
INTERNAL
&
INTERAGENCY
USE
ONLY**

Pursuant to the contract with Arizona Reporting Service all transcripts are available electronically for internal agency use only.

Do not copy, forward or transmit outside the Arizona Corporation Commission.

1 INDEX TO EXAMINATIONS

2 WITNESSES PAGE

3 MARVIN E. MILLSAP (Continued)

| | | |
|---|--|-----|
| 4 | Cross-Examination by Mr. Shapiro | 374 |
| | Examination by ALJ Wolfe | 406 |
| 5 | Cross-Examination by Ms. Wood | 409 |
| | Further Cross-Examination by Mr. Shapiro | 420 |
| 6 | Redirect Examination by Mr. Van Cleve | 423 |

7

8 THOMAS J. BOURASSA - REBUTTAL

| | | |
|---|---------------------------------|-----|
| 8 | Direct Examination by Mr. James | 428 |
| 9 | Cross-Examination by Ms. Wood | 439 |

10

11

12 INDEX TO EXHIBITS

| 12 | NO. | DESCRIPTION | IDENTIFIED | ADMITTED |
|----|------|--|------------|----------|
| 13 | A-12 | Excerpt of Transcript re Oak Creek Water in Docket No. W-01392A-07 | | |
| 14 | | -0679 | 383 | 390 |
| 15 | A-13 | Chaparral City Data Request 1.54 | 385 | 390 |
| 16 | A-14 | Chaparral City Data Request 1.27 | 395 | 406 |
| 17 | A-15 | Chaparral City Data Request 4.4 | 405 | 406 |
| 18 | | | | |
| 19 | | | | |
| 20 | | | | |
| 21 | | | | |
| 22 | | | | |
| 23 | | | | |
| 24 | | | | |
| 25 | | | | |

1 BE IT REMEMBERED that the above-entitled and
2 numbered matter came on regularly to be heard before the
3 Arizona Corporation Commission, 1200 West Washington
4 Street, Phoenix, Arizona, commencing 9:30 a.m. on the
5 10th day of December, 2008.

6

7 BEFORE: TEENA WOLFE, Administrative Law Judge

8

9 APPEARANCES:

10 For the Arizona Corporation Commission Staff:

11 Ms. Robin Mitchell, Ms. Amanda Ho,
12 and Mr. Wesley Van Cleve
13 Staff Attorneys, Legal Division
14 1200 West Washington Street
15 Phoenix, Arizona 85007

16

For Chaparral City Water Company:

17

FENNEMORE CRAIG

18

By Mr. Norman D. James

Mr. Jay L. Shapiro

19

3003 North Central Avenue, Suite 2600

Phoenix, Arizona 85012

20

21 For the Residential Utility Consumer Office:

22

RESIDENTIAL UTILITY CONSUMER OFFICE

By Ms. Michelle L. Wood

23

1110 West Washington, Suite 220

Phoenix, Arizona 85007

24

25

MICHELE E. BALMER

Certified Reporter

Certificate No. 50489

26

1 ALJ WOLFE: Good morning. I guess we can just go
2 right to it, unless you have a procedural issue.

3 MS. MITCHELL: I do have a procedural issue,
4 Judge Wolfe, thank you.

5 In our filing yesterday, the adoption of the
6 Chaves testimony by Dave Parcell, there's some corrections
7 that need to be made, and I just wanted to alert the
8 parties that Staff would be filing some errata.

9 I won't be able to file it today because
10 Mr. Parcell is testifying in another jurisdiction and he's
11 not in his office, but he will be returning tomorrow. And
12 as soon as, you know, I can get with him to discuss the
13 changes, we will be filing some errata to that testimony,
14 and Staff apologizes if it causes any inconvenience to the
15 parties.

16 ALJ WOLFE: Okay.

17 MR. JAMES: Your Honor, may I?

18 ALJ WOLFE: Yes, Mr. James.

19 MR. JAMES: I appreciate Ms. Mitchell's dilemma
20 and appreciate the fact that she's going to file something
21 that corrects the problem, but I just want to make sure
22 that you understand the basic issue or the basic concern
23 that we had. Obviously, this was filed late yesterday. I
24 went through it quickly last night.

25 The big concern I have is that in his surrebuttal

1 testimony filed on December 4, Mr. Parcell -- as you
2 recall, we discussed this during our prehearing
3 conference -- Mr. Parcell is testifying about the cost of
4 equity. Essentially, as I said, and I don't know whether
5 you've had a chance to read his testimony, but
6 essentially, as I said last Friday, he is essentially
7 talking about the DCF and CAPM models, and then there's a
8 section, as indicated at the end, that deals with the
9 current market volatility and whether -- how it should be
10 factored into the Commission's decision-making here today.

11 The concern I had last night when I read it, I
12 was trying to get ready for my cross-examination of
13 Mr. Fox today, and what was changed was the section that
14 deals with the way that the rate of inflation should be
15 determined and how the fair value rate of return should be
16 determined, and that was not in Mr. Parcell's testimony.

17 So again, I understand -- I'm not being critical
18 of Staff. It was a mistake. It's going to be fixed. My
19 concern today, of course, is I'm going to be
20 cross-examining Mr. Fox. And if Mr. Parcell is now going
21 even further and testifying on other issues, obviously
22 we're going to have another serious problem, but hopefully
23 that's not going to be the case.

24 ALJ WOLFE: Ms. Mitchell.

25 MS. MITCHELL: I did have some discussions with

1 Mr. James, and I said, you know, to the extent -- I know
2 that these issues are somewhat marginally intertwined with
3 the determination of fair value rate of return. And Staff
4 would give a little bit of latitude depending on how
5 Mr. James phrases his questions to Mr. Fox, and Staff may
6 have some objections, but, you know, I can't tell until I
7 get there. But I do understand the dilemma that he faces
8 and Staff would give a little bit of latitude, but it just
9 depends and there may have to be some objections made.

10 And then perhaps, you know, if there's some
11 issues that waft over into cost of capital, you know, if
12 need be to bring Mr. Fox back, that certainly is a
13 possibility.

14 ALJ WOLFE: Thank you.

15 Does RUCO have anything to add to this
16 discussion?

17 MS. WOOD: I do, Your Honor, and it's maybe my
18 confusion. I thought in the pretrial conference that we
19 discussed the fact that all cost of capital witnesses
20 would be on the same day, which I thought yesterday we
21 decided was the 8th and the 9th. I did not realize that
22 Mr. Fox would be testifying today, and maybe it's my
23 inexperience, but I perceived him as a cost of capital
24 witness.

25 ALJ WOLFE: Well, I was going to ask Mr. James

1 and you, too, if it would be helpful just to have Mr. Fox
2 testify on the 8th, if that would clear up any of the
3 issues possibly.

4 MR. JAMES: Well, Your Honor, I'm not sure it's
5 necessary. I had assumed that he would testify today
6 because he's -- what he's really testifying on is what has
7 been referred to as the fair value rate of return and how
8 you take the weighted cost of capital and adjust it.
9 Obviously, we're opposed to doing that. But there is
10 some -- as I had indicated in the prehearing conference,
11 there is some overlap between the two.

12 But as I also represented to Ms. Mitchell, I
13 frankly intend to use Mr. Chaves's testimony, but not on
14 cost of equity issues. I'm not going to get into the
15 issue of how the cost of equity should be estimated in
16 this case. What I'm interested in is how the inflation
17 rate should be estimated and how that should be used to
18 adjust the weighted cost of capital.

19 I don't view that as a cost of capital issue. I
20 view it -- or really when we talk about cost of capital,
21 what we're really talking about are the cost of equity
22 witnesses. You know, how do you estimate the current cost
23 of equity using the discounted cash flow model, the
24 capital asset pricing model, those sorts of issues.

25 There is some overlap, as Ms. Mitchell indicated,

1 but again, as I told her, I'm going to be asking questions
2 that, again, relate to those models, but my intent today
3 is not to cross-examine Mr. Fox and turn him into a cost
4 of capital witness. Rather, it's to show how Staff
5 computed the adjustment for inflation and how that should
6 be used to adjust the ultimate weighted cost of capital to
7 get to the fair value rate of return. It will be --
8 hopefully it will become a little clearer when the witness
9 is actually testifying.

10 ALJ WOLFE: I understand. But to Ms. Wood's
11 comment that she believes she is -- and I think this was
12 maybe part of her confusion at the prehearing conference,
13 that the rate of return and cost of capital, at least to
14 RUCO's mind, are very much intertwined and there is a
15 relationship here.

16 MR. JAMES: There is a relationship.

17 ALJ WOLFE: Due to the appeal and due to the
18 issues that were in the decision, the remand decision. So
19 I don't see why it wouldn't be helpful to have Mr. Fox and
20 Mr. Parcell testify in January instead of today so that it
21 would be all at the same time and they could be recalled,
22 is there? And I don't see why it would be a problem to
23 have those two issues bifurcated from the rest of the
24 issues in the case. If you have an argument against that,
25 then I'm certainly willing to hear it.

1 MR. JAMES: Well, you're suggesting, then, that
2 Mr. Fox would be postponed to January 8?

3 ALJ WOLFE: Yes.

4 MR. JAMES: If that's true, then Staff's final
5 witness today would also deal with that issue, too. So
6 we're going to end up with a hearing in January where
7 we're going to have a company witness, Mr. Bourassa, a
8 RUCO witness, Mr. Rigsby, and three and potentially four
9 Staff witnesses.

10 ALJ WOLFE: So the time is -- it's the timing
11 issue that you're concerned with?

12 MR. JAMES: Yes. I mean, we're pushing more and
13 more into the back end of the hearing. Again, I think we
14 can probably do that in two days. And frankly, I don't
15 have a lot of questions for Mr. Abinah, but I don't --
16 probably 20 minutes of cross, but his testimony -- again,
17 let me back up and explain, Your Honor, the difference
18 between Mr. Fox's testimony and Mr. Abinah's testimony.

19 Mr. Abinah's testimony says that -- suggests that
20 the Commission should consider what Staff refers to as,
21 quote, Method 1. Method 1 is essentially the method that
22 was adopted in Chaparral City's remand case. His
23 testimony, if you look at it, is very short. I don't have
24 a lot of questions for him. But it is Mr. Fox and I
25 understand the Staff's position still is that the

1 Commission should adopt -- should use Method 2.

2 So, you know, again, if we're going to consider
3 rate of return with cost of capital, all of those
4 witnesses' testimony are interrelated.

5 ALJ WOLFE: Yes.

6 MR. JAMES: Okay. All right. You understand
7 what I'm saying. All right.

8 ALJ WOLFE: Yes.

9 MR. JAMES: So today we would simply be finishing
10 Mr. Millsap and that would complete this phase of the
11 case.

12 ALJ WOLFE: Ms. Wood.

13 MS. WOOD: That was my feeling, Your Honor,
14 because the other witnesses are cost of capital witnesses.
15 And the one request that RUCO made --

16 ALJ WOLFE: They are rate of return witnesses. I
17 would disagree that they're --

18 MS. WOOD: Then that's my misunderstanding, Your
19 Honor. I guess it's my inexperience, but I thought we
20 were having the cost of capital day and all of those
21 witnesses that had something related to that, which I felt
22 was Mr. Fox on Method 1 and Method 2, Mr. Chaves,
23 Mr. Bourassa, and Mr. Rigsby. To the extent that
24 Mr. Abinah feels a need to elaborate on the policy
25 statements he made, he is as well.

1 ALJ WOLFE: So are you saying that you're not
2 prepared to cross Mr. Fox today?

3 MS. WOOD: That's true.

4 ALJ WOLFE: Okay.

5 MS. WOOD: And I apologize if I misunderstood.

6 ALJ WOLFE: Okay. Ms. Mitchell, do you have any
7 objection to having Mr. Fox and Mr. Abinah testify on
8 January 8th or 9th?

9 MS. MITCHELL: No, Your Honor. Staff has no
10 objection to that.

11 ALJ WOLFE: Okay. Is the company objecting?

12 MR. JAMES: Well, Your Honor, you know, again,
13 we've tried to work here with the Commission under these
14 circumstances. My concern again is we're delaying the
15 case.

16 ALJ WOLFE: I understand that. And if I had
17 known that RUCO was not prepared to cross-examine those
18 witnesses yesterday, I certainly would have informed them
19 that they would need to be prepared today, but I'm sort of
20 in a tough spot here.

21 MS. MITCHELL: Your Honor, may I interrupt?
22 Mr. Fox just informed me he won't be available on the 9th,
23 so he will need to go -- you know, he'll need to go on the
24 8th. And then, you know, I would also reserve the right
25 to perhaps -- you know, it depends on -- all of this

1 depends on what happens during Mr. Millsap's testimony,
2 because there may be some issues that Mr. Abinah may need
3 to address today. And, you know, I don't know whether you
4 would want me to put him on to address those issues or
5 hold those issues until he testifies in January. But I
6 would like to reserve the right, you know, to have him
7 address additional issues other than just fair value rate
8 of return issues should something arise during the
9 cross-examination of Mr. Millsap.

10 ALJ WOLFE: Okay. Why don't we go ahead and put
11 Mr. Abinah on today and then make him available also on
12 the 8th or the 9th for Ms. Wood's cross-examination.

13 I want to make sure that every party has a full
14 and fair opportunity to present their case.

15 MS. MITCHELL: No, I understand, and I didn't
16 know if -- well, this is just so confusing. Maybe it
17 would just be best to have Mr. Abinah and Mr. Fox testify
18 together. I mean, I'm hearing from RUCO that they feel
19 that those issues are intertwined, and certainly Staff
20 wants them to have an opportunity to prepare, you know,
21 and ask relevant questions to assist their case. And I
22 don't want to disadvantage anybody by being confusing. So
23 I'll let the other parties chime in and see what they
24 think.

25 MR. SHAPIRO: I guess I was going to jump in,

1 Judge Wolfe, and ask why Staff planned on calling
2 Mr. Abinah to follow Mr. Millsap on what sounded like
3 testimony that was outside the scope of what Mr. Abinah
4 testified to. If that was Ms. Mitchell's intent, then we
5 do have a concern with that. I wasn't clear.

6 ALJ WOLFE: Okay. She hasn't done it yet,
7 so we'll see what happens. We'll cross that bridge when
8 we come to it.

9 All right. So unless there's objection, we'll
10 have Gordon Fox, Elijah Abinah, and David Parcell
11 scheduled to testify on a date certain. Well, Mr. Fox
12 will testify a date certain of January 8th, and Mr. Abinah
13 and Mr. Parcell and Mr. Rigsby and Mr. Bourassa will
14 testify also on either the 8th or the 9th. We might have
15 to convene at 9:00 a.m. in order to make sure that we get
16 everybody in. I don't want it to go past the 9th. I
17 really don't have any intention of making it go any
18 further than that.

19 Ms. Wood.

20 MS. WOOD: I apologize, Your Honor, I have one
21 other procedural matter. I just need to lay a record and
22 I need to ask you to move to strike the testimony of
23 Mr. Millsap yesterday which was not within the scope of
24 his direct or surrebuttal testimony which related to
25 policy issues, which prior to yesterday at 10 minutes of

1 5:00 were not disclosed. That's in violation of the
2 court's procedural order which required any changes in
3 testimony to be disclosed five days ahead of time. It's
4 also violative of basic principles of due process which
5 require notice and a full and fair opportunity for
6 cross-examination.

7 Telling us 10 minutes before the close of the day
8 that his testimony had changed after we had closed our
9 case in chief is not notice and not a full and fair
10 opportunity for us to develop our case to address that
11 change, and a drastic change in his testimony. And we
12 feel that we need to at least lay the record for our
13 objection, and I will rest with that.

14 ALJ WOLFE: Does RUCO believe that if it's
15 allowed to recall its witness to respond that that would
16 heal the issue for you?

17 MS. WOOD: It might be one way to address the
18 issue. It doesn't address the pattern of behavior of
19 Ms. -- well, I won't -- Staff's filing late and changed
20 testimony to which the rest of us all have to adjust. I
21 understand that the court wants to take in everything they
22 have before it, and I don't have any opinion about that.
23 You have to do what you have to do.

24 But the undue surprise that we get to enjoy with
25 Mr. Parcell's changed testimony, which was not -- which

1 was announced in the notice of substitution, and with
2 Mr. Millsap's dramatic change in testimony with regard to
3 the proceeds, it's something that perhaps at some point
4 needs to be addressed, and I'm too new here to profess an
5 opinion as to how that should be addressed.

6 I was told yesterday when I asked about the
7 issue -- because I have represented state agencies for
8 over 15 years -- that this is the Commission and we can do
9 what we want.

10 Now, nobody in this room occupies one of the five
11 chairs to which the elected officials sit. I don't
12 disagree that the Commission has full opportunity to
13 address these cases in any way which they deem fit. But
14 the principles of due process, which is notice and full
15 and fair opportunity to cross-examine a witness, does not
16 disappear in this room.

17 In fact, this is a constitutionally created body,
18 and they understand the premise of constitutionality and
19 due process. In fact, one of the things that I enjoined
20 most when I first got here was Commissioner Mundell
21 emphasizing repeatedly the notion of openness and
22 transparency. And as he has pointed out, people may not
23 agree with the Commission in every instance, the decision
24 may make a company and ratepayers equally uncomfortable or
25 unhappy, or it may make them equally happy, but they will

1 appreciate the fact that this body deals with matters in a
2 way which is open and transparent.

3 And I don't know if you can address it in this
4 case, or we can come up with a method of proceeding from
5 here on after, but it's just unfair to the parties and --

6 ALJ WOLFE: Well, Ms. Wood, I am asking you now
7 what you believe is necessary in order to remedy the
8 issue.

9 MS. WOOD: I think the suggestion that you made,
10 Your Honor, might well be appropriate. I'm not sure I can
11 do it today, but I will do it before -- is there a process
12 by which RUCO can recall a witness?

13 ALJ WOLFE: Yes.

14 MS. WOOD: Okay. Because I have not appeared
15 before, I don't know what the process is. Is it at the
16 conclusion of all of the testimony or what is the process?

17 ALJ WOLFE: I'm asking you what would be the best
18 way for you to be able to present your case.

19 MS. WOOD: Okay.

20 ALJ WOLFE: And you haven't necessarily -- I
21 didn't ask you if you had rested your case yet, so there's
22 not an issue with that. I don't have a problem with you
23 recalling a witness, with filing additional responsive
24 testimony to address that issue if you want to do that. I
25 don't know. I don't know what it is that you want to

1 present. So it's up to you to tell me, and you don't have
2 to tell me right now. We can wait until after we take a
3 break and you have a chance to confer with your client.

4 MS. WOOD: Thank you very much. I appreciate
5 that.

6 ALJ WOLFE: Thank you.

7 MS. MITCHELL: Judge Wolfe, I need to address a
8 couple of issues. I think it was a misrepresentation that
9 the Commission can do whatever it wants. I think I
10 indicated to Ms. Wood yesterday that the Commission was
11 constitutionally created. That the rules of practice
12 before the Commission don't necessarily follow the rules
13 of evidence. That the role of Staff and the Commission is
14 to present what it feels is the best recommendation,
15 weighing the interests of the ratepayers and the interests
16 of the company.

17 You know, I would direct RUCO's attention to
18 A.R.S. 40-253, which talks about the conduct -- 243 that
19 talks about the conduct of hearings and investigations and
20 indicates that, you know, the Commission does issue its
21 own rules of practice and it's bound by those rules, and
22 that neither the Commission, nor a Commissioner, shall be
23 bound by technical rules of evidence, and no informality
24 in any proceeding or on any matter of taking testimony
25 before the Commission or Commissioners shall invalidate

1 any order, decision, rule or regulation made, approved or
2 confirmed by the Commission.

3 You know, Staff apologizes, but Staff has to do
4 what it is obligated to do, and that is to present facts
5 and testimony which it believes will give the Commission
6 an opportunity to make a fair and reasoned decision. And
7 if RUCO is suggesting something different, then I highly
8 take offense at that.

9 You know, Staff and RUCO have had a cordial
10 relationship, you know, and I hope that this is not
11 damaging it. But as I indicated to Ms. Wood, a lot of
12 times the positions do change. Mr. Shapiro even agreed
13 with me that during the course of a hearing testimony
14 changes and testimony of positions of parties change. I
15 indicated to Ms. Wood, you know, rejoinder testimony
16 sometimes is not addressed in writing. It's addressed on
17 the stand.

18 There was no indication -- there was no intention
19 of Staff to disadvantage anyone, to violate any rules of
20 due process. And any suggestion that that was Staff's
21 intent is highly offensive, I think, to the hard work that
22 everybody has done in this case.

23 You know, I joked with opposing counsel that I
24 think this case is born under a bad sign. Mr. James and I
25 share a love of blues and that's a blues song. But, you

1 know, to the extent that Staff has disadvantaged anyone,
2 has put anyone in a difficult position, I have to
3 apologize for that. But then I also have to say, as
4 representing my client, Staff has an obligation when it
5 has listened to testimony and it feels that there needs to
6 be a change of position, it needs to make that position.
7 I don't see anything wrong with that. That's what Staff
8 is supposed to do. It's supposed to ferret out
9 information that balances the needs of the company with
10 the needs of the ratepayers in order to give the
11 Commission a full and balanced record.

12 Was Staff supposed to not change its testimony
13 because RUCO didn't want it to? You know, Staff didn't
14 put on this case to be bound by any of the parties.
15 Staff, as the other parties, they put on their own case.

16 And so to the extent that anybody has been
17 disadvantaged, Staff apologizes, but I believe that there
18 are remedies to that. She has full cross-examination of
19 Mr. Millsap coming up. You have offered to let her recall
20 witnesses, which happens all of the time, at least in the
21 proceedings that I've been involved with. Staff doesn't
22 have a problem with that. And I just want to make that
23 record clear.

24 ALJ WOLFE: All right. Mr. Millsap, you're under
25 oath still, so I'll just remind you of that. And I'll let

1 the company cross-examine you first so that RUCO can have
2 the opportunity to hear your answers to the company's
3 questions.

4 MR. SHAPIRO: Thank you, Your Honor.

5

6 MARVIN E. MILLSAP (Continued),
7 called as a witness on behalf of ACC Staff, having been
8 first duly sworn by the Certified Reporter to speak the
9 truth and nothing but the truth, was examined and
10 testified as follows:

11

12

CROSS-EXAMINATION

13

14 Q. (BY MR. SHAPIRO) Good morning, Mr. Millsap.

15 A. Good morning, Mr. Shapiro.

16 Q. You've been waiting patiently.

17 Your rate base Adjustment No. 5 removed over
18 \$625,000 from rate base as part of a working capital
19 adjustment, correct?

20 A. That is correct.

21 Q. That included -- that \$625,000 included roughly
22 \$424,000 for the cost of debt, \$191,000 for prepayments,
23 and \$14,000 for supplies, correct?

24 A. Subject to check, that would be correct.

25 Q. And those were rough numbers. I didn't have the

1 exact.

2 Now, Mr. Bourassa testified that unamortized cost
3 of debt is not part of working capital. How do you
4 respond to that statement?

5 MR. VAN CLEVE: Your Honor, it might be helpful
6 if he can point out a page reference.

7 MR. SHAPIRO: I don't know if you've got it in
8 front of you. It's Mr. Bourassa's rebuttal, which is
9 Exhibit A-5, I believe. My trusty assistant will look
10 that up.

11 ALJ WOLFE: Let's go off the record so that the
12 court reporter can provide that exhibit.

13 (Brief pause in the proceedings.)

14 ALJ WOLFE: Back on the record. The witness has
15 been provided with a copy of Exhibit A-5.

16 Q. (BY MR. SHAPIRO) And just more specifically,
17 it's at line -- the Q and A that begins on Line 17,
18 Mr. Millsap.

19 ALJ WOLFE: On which page again?

20 MR. SHAPIRO: I'm sorry. Page 12. Line 17 is
21 where the Q and A begins.

22 THE WITNESS: Would you repeat the question
23 please?

24 Q. (BY MR. SHAPIRO) The question was: How do you
25 respond to Mr. Bourassa's position that the unamortized

1 debt costs that you removed as part of your working
2 capital adjustment are not part of working capital?

3 A. I would have to agree with that, and I
4 mischaracterized them as being part of working capital.

5 Q. So does that mean that the unamortized debt costs
6 should not be removed from rate base?

7 A. No, that is not correct. They should be because
8 they constitute a below-the-line expense. They're like
9 interest. They're amortized as interest over the life of
10 whatever the debt is.

11 And because they're a below-the-line expense,
12 that is part of the shareholders' costs, so it should not
13 be included in operating expenses, nor should it be
14 included in rate base.

15 Q. Okay. Let's take a step back. So you're
16 modifying your testimony at this point and saying that
17 these should not have been removed as part of your working
18 capital adjustment. That's step one, correct?

19 A. That would be correct.

20 Q. And you're saying that they should be removed
21 from rate base. And I'm sorry, I'm confused as to the
22 reason.

23 A. Well, as Mr. Bourassa says in his testimony,
24 they're amortized as interest expense; therefore, it's a
25 below-the-line expense and should be absorbed by the

1 shareholders and should not be part of rate base.

2 Q. So the cost of debt is not something -- well, let
3 me back up.

4 Staff encourages companies to have some debt in
5 their capital structure and to use debt to finance plant,
6 correct?

7 A. I believe that's correct, yes.

8 Q. And it does cost money to acquire debt, doesn't
9 it?

10 A. I don't believe that's the case in all
11 circumstances.

12 Q. Well, there are typically, you know, closing
13 costs, documentation fees, sometimes points paid, various
14 items that are charged by lenders associated with debt.
15 Isn't that a common practice?

16 A. That would be a common practice, yes.

17 Q. Okay. And if you have bonds, there is cost to
18 issue bonds, cost of underwriting, all of the people
19 involved in that effort, correct?

20 A. I would assume so, yes.

21 Q. And we have some bonds at issue in this case?

22 A. I'm not a cost of capital witness, so I really
23 don't know.

24 Q. So you don't know the source of the debt in the
25 company's capital structure in this case?

1 A. No, I'm not familiar with it.

2 Q. And if you remove the unamortized -- well, if the
3 debt is reasonable, reasonably and prudently obtained,
4 shouldn't there be some means by which the company
5 recovers the cost of obtaining that debt?

6 A. Would you repeat that question, please?

7 Q. If you have debt that is prudently obtained,
8 reasonably obtained to finance plant that's needed at a
9 reasonable rate, and that debt has a cost associated with
10 it, shouldn't the utility have an opportunity to recover
11 the cost of that debt as well as the interest or the
12 principal payments on that debt?

13 A. Yes, and that would be included as part of the
14 rate of return that's included in the revenue requirement.

15 Q. Well, if you were going to remove something from
16 rate base, why wouldn't you remove it to a different place
17 so the company doesn't lose the entire recovery, which is
18 what happens with your adjustment, correct?

19 A. Would you repeat the question, please?

20 Q. Yes. Let me simplify it. Why didn't you,
21 instead of disallowing the amount in its entirety, move it
22 to the place you believe it should have been recorded?

23 A. Because all I was concerned about was accurately
24 portraying rate base. I was not making adjustments for
25 financial reporting purposes, only for ratemaking

1 purposes.

2 Q. To your knowledge, did Mr. Chaves include it in
3 his analysis of the company's debt?

4 MR. VAN CLEVE: Objection, Your Honor. That goes
5 to, I think, a cost of capital issue.

6 ALJ WOLFE: I'll allow the question. He said to
7 your knowledge.

8 THE WITNESS: I honestly don't know whether he
9 did or not.

10 Q. (BY MR. SHAPIRO) Do you know whether interest
11 expense is part of the cost of capital?

12 MR. VAN CLEVE: Same objection, Your Honor.

13 MR. SHAPIRO: Well, I'm not --

14 ALJ WOLFE: Overruled.

15 MR. SHAPIRO: Thank you.

16 THE WITNESS: Whether interest expense is part of
17 cost of capital? No, I would say it's not.

18 Q. (BY MR. SHAPIRO) The amounts that you initially
19 removed, and that includes the debt cost and the other two
20 amounts, the materials and supplies, you said in your
21 testimony that you couldn't include those items in rate
22 base because the company did not prepare a lead/lag study.
23 That's at your direct testimony at Page 23.

24 Do you recall that?

25 A. Yes.

1 Q. What does the necessity of a lead/lag study have
2 to do with whether or not those items are included in rate
3 base?

4 A. That's Staff's position. It has been apparently
5 in cases for a long time. I don't know. This was the
6 first case that I have had to deal with this since I have
7 returned to the Commission.

8 Q. So do you know -- do you have any source to
9 support your testimony that that's Staff's position, or is
10 that just something that you were told?

11 A. That's Staff's position. That's my only answer
12 to that.

13 Q. There is a lead/lag study in this case, is there
14 not? RUCO prepared it and the company adopted it,
15 correct?

16 A. I believe that's correct, yes.

17 Q. So you could have gone back in your surrebuttal
18 case and made an adjustment to put these items back into
19 rate base on the basis that there is now a lead/lag study,
20 correct?

21 A. Since I did not perform the lead/lag study, I
22 could not use it for purposes of my testimony.

23 Q. So you're critical of the company for not
24 preparing a lead/lag study, which had they prepared you
25 wouldn't have needed to make the adjustment, but RUCO

1 prepared a lead/lag study and you can't use that because
2 you didn't prepare it. Is that your testimony?

3 A. Had the company prepared one and submitted it
4 with its application, I would have had an opportunity to
5 review it and then I could have commented on it.

6 Q. In your surrebuttal testimony you just ignored
7 this issue completely, correct? You didn't address
8 Mr. Bourassa's rebuttal testimony on your working capital
9 adjustment?

10 A. I wouldn't characterize it as having been
11 ignored, no.

12 Q. Well, did you address it in your surrebuttal
13 testimony?

14 A. No, I did not.

15 Q. You didn't even file schedules with your
16 surrebuttal testimony, did you?

17 A. They were not necessary.

18 Q. Is that because Staff's revenue requirement and
19 revenue increase recommendation has not changed since its
20 direct filing on October 3?

21 A. For the purposes of my surrebuttal testimony,
22 that's correct.

23 Q. So Staff's recommended requirement is the roughly
24 \$1.7 million that Ms. Mitchell referred to in her opening
25 statement, plus an adjustment based on your change of

1 position in the Fountain Hills Sanitary District
2 settlement proceeds?

3 A. Would you repeat the question, please?

4 Q. Yeah. Staff's current recommended revenue
5 increase is the roughly \$1.7 million increase that
6 Ms. Mitchell referenced to in her opening statement
7 yesterday, which will be adjusted now by Staff to account
8 for its change of position with respect to the treatment
9 of the Fountain Hills Sanitary District settlement
10 proceeds?

11 A. That's an awfully long question, but it sounds
12 like that would be correct.

13 MR. SHAPIRO: Could I have a minute? In light of
14 Mr. Millsap's change on the working capital, I need to
15 confer with Mr. Bourassa for a moment.

16 ALJ WOLFE: Okay.

17 (Brief pause in the proceedings.)

18 Q. (BY MR. SHAPIRO) The Commission uses a
19 historical test year, correct, Mr. Millsap?

20 A. That's correct.

21 Q. And as part of the historical test year approach,
22 adjustments are made based on known and measurable changes
23 in the test year, correct?

24 A. That's correct.

25 Q. And the goal of all of this is to set rates at a

1 level that allows for the recovery of the operating
2 expenses that will be incurred during the time the rates
3 will be in effect, correct?

4 A. That would be correct.

5 Q. And you would agree -- do you know Darron
6 Carlson?

7 A. Yes, I do.

8 Q. He's your supervisor, correct?

9 A. That's correct.

10 Q. You would agree with Mr. Carlson if he testified
11 before this Commission that averaging is not a known and
12 measurable change?

13 A. No, I guess I would not agree with that.

14 Q. Let me hand you what I have marked as Exhibit
15 A-12, which is an excerpt from proceedings before the
16 Commission in the matter of the application of Oak Creek
17 Water Company.

18 If I could direct your attention, Mr. Millsap, to
19 Line 7 of the second page.

20 The question is asked: "Well, is averaging a
21 known and measurable change?"

22 The answer: "No, it is not."

23 So you disagree with that?

24 A. To the extent that averaging is a form of
25 normalizing, I agree with his statement.

1 Q. And in this case you averaged chemical expense
2 and repairs and maintenance expense, correct?

3 A. Yes, I did.

4 Q. And you did that, according to your testimony, to
5 mitigate any extenuating circumstances that may have led
6 to the increase in the test year from the prior years?

7 A. Can you refer to my testimony?

8 Q. Yes. It would be your direct testimony at
9 Page 33 and 34. More specifically, it's at Lines 18, 19
10 on 33, and Lines 6 and 7 on 34.

11 A. Okay. Would you repeat the question, please?

12 Q. The question was whether your averaging
13 adjustment was done, according to your testimony, to
14 mitigate any extenuating circumstances that may have led
15 to increases in these expenses during the test year?

16 A. That is my testimony.

17 Q. And do you stand by your testimony?

18 A. Yes, I do.

19 Q. Okay.

20 A. Now, let me explain a little bit more about why I
21 did this. I discovered that there were two invoices for
22 deliveries of chemicals late in the year. The total of
23 those two invoices was almost \$17,000. These were
24 invoices for deliveries that were not made on a monthly
25 basis. They were made over longer time periods.

1 Consequently, my conclusion was that those
2 deliveries were for chemicals that were going to be used
3 in the following year, which led me to conclude that they
4 should not be included in expenses for the test year.
5 They should have been included as expenses for the
6 following year.

7 And since there was such a significant increase
8 from 2004 to 2006, and considering that I knew that the
9 treatment plant had come on line sometime during that time
10 period so the chemicals expenses would increase, I
11 normalized the chemicals expense using those three years
12 as a basis for it.

13 Q. So you did it because you found some invoices
14 that you concluded were anomalous in some fashion?

15 A. Correct.

16 Q. And you didn't believe that it was appropriate to
17 explain that background fact in your testimony anywhere?

18 A. I didn't address it in detail, no.

19 Q. And let me hand you what's been marked as
20 Exhibit A-13, which is a copy of data request 1.5 -- oh,
21 I'm sorry. Let me take that one back. I've got the wrong
22 one. It's 1.54.

23 When we asked you to identify extenuating
24 circumstances that Staff was aware of that led to the
25 increase in chemical expenses, you told us it was an

1 increase in chemical expenses resulting from increases in
2 freight costs and slight increases in unit prices. That
3 sounds somewhat or substantially different than what you
4 just explained here today, doesn't it?

5 A. My response was based on my analysis of chemical
6 expenses.

7 Q. Well, but when I asked you to identify the --
8 well, actually, you volunteered today that the extenuating
9 circumstances were invoices received late in the year that
10 you assumed were for chemicals next year. When we asked
11 you to explain the extenuating circumstances, you
12 indicated there were increased costs in the provision of
13 the chemical services.

14 So is it both? Is it neither? What is the
15 extenuating circumstance that justified averaging these
16 expenses based on the test year and the two prior years?

17 A. All of my analysis.

18 Q. You didn't find any extenuating circumstances at
19 all that led to an increase in repairs and maintenance
20 expense; isn't that correct?

21 A. No.

22 Q. No, that's not correct, or no, you didn't find
23 any? I want to make sure the record is clear.

24 A. I don't recall finding any.

25 Q. And Mr. Hanford testified that chemical expenses

1 have continued to increase since the test year, didn't he?

2 A. I believe that he testified to that, yes.

3 Q. Did you do anything to follow up and determine
4 whether the assumptions that you made regarding those
5 invoices may not have been correct and that maybe your
6 adjustment was inappropriate once Mr. Hanford supplied
7 that additional explanation in his testimony?

8 A. No.

9 Q. In fact, in your surrebuttal you just basically
10 asserted that normalizing or averaging is appropriate
11 ratemaking and left it at that, correct?

12 A. That would be correct, yes.

13 Q. So if I'm correct, then Staff removed \$48,000 of
14 operating expenses a year to mitigate against extenuating
15 circumstances that don't really exist, isn't that true, or
16 at least that we can't really put a finger on in this
17 case?

18 A. You want to repeat that question, please?

19 Q. Yeah. I'll withdraw the question.

20 Staff also averaged insurance expense, too,
21 didn't it?

22 A. That's correct.

23 Q. And the company, even though that increased the
24 company's expenses, the company opposes that adjustment as
25 well, correct?

1 A. I believe that's correct, yes.

2 Q. And in averaging the chemical expense and the
3 repairs and maintenance expense, you used '04, 05, and the
4 test year '06, correct?

5 A. That's correct.

6 Q. And you didn't look at 2007 to determine whether
7 your concern over increases from the years prior to the
8 test year, to the test year may not have been -- there may
9 not have been any need for concern because those costs
10 really were increasing?

11 A. Actually, for chemicals I did. And according to
12 the 2007 trial balance that was provided for me by the
13 company, chemical expenses were only about \$89,000, as
14 opposed to 127 for the test year.

15 Q. So you just didn't choose to provide that
16 information anywhere in your testimony?

17 A. I didn't, no. My testimony is what it is.

18 Q. Isn't the process of averaging to come up with an
19 expense level very subjective, Mr. Millsap? Doesn't the
20 analyst have to decide which expenses to average and which
21 years to use?

22 A. It would be subjective, yes.

23 Q. And, in fact, in your case you're using, as you
24 just said, 2004, 2005, and 2006 to average two expense
25 items, but you're using 2003, 2004, 2005, 2006, and 2007

1 to come up with an insurance expense level, correct?

2 A. That's correct. Because the test year, 2006, had
3 a negative expense, which is a little bit abnormal, and
4 2003 did not have any expense, which is also a little
5 abnormal. So if you're going to try to normalize, you
6 have to use some periods where there's actually some
7 expense there.

8 Q. But you would agree with me that these rates are
9 going in effect in 2009, correct?

10 A. It appears that that will be true, yes.

11 Q. So going back to 2004, 2005, that's a fairly long
12 ways removed from 2009 going forward, isn't it?

13 A. I suppose that would be correct, yes.

14 Q. And, of course, it's possible that in averaging
15 and making these subjective determinations, the analyst
16 can guess wrong, leaving the company significantly over-
17 or underrecovering, correct, for that particular expense
18 item?

19 A. No, I wouldn't characterize it that way.

20 Q. So Mr. Bourassa has testified in this case, both
21 in his prefiled testimony and when he took the stand
22 Monday, that in the last case the expenses that were
23 determined by averaging were substantially -- the expense
24 level authorized was substantially less than the amount
25 the company actually incurred for those expenses.

1 Did you do any analysis of whether or not we got
2 this right last time?

3 A. No.

4 Q. So as you sit here today, you don't really have
5 any evidence to submit to disagree with Mr. Bourassa's
6 testimony?

7 A. No. I don't have any basis to agree with it
8 either.

9 MR. SHAPIRO: Before I forget, Your Honor, let me
10 move those two exhibits that I have used so far, A-12 and
11 A-13.

12 ALJ WOLFE: Are there any objections to A-12 or
13 A-13?

14 MR. VAN CLEVE: No objections.

15 MS. WOOD: No, Your Honor.

16 ALJ WOLFE: A-12 and A-13 are admitted.

17 MR. SHAPIRO: Thank you.

18 (Exhibits A-12 and A-13 were admitted into
19 evidence.)

20 Q. (BY MR. SHAPIRO) Mr. Millsap, Chaparral City
21 Water Company is a Class A utility?

22 A. That's correct.

23 Q. And you would agree that rate cases for Class A
24 water companies are a fairly significant undertaking for
25 the parties involved?

1 A. I would assume that's true, yes.

2 Q. The utility incurs costs for copying, mailing,
3 publication. Those are all costs that you expect the
4 utility to incur in a rate case?

5 A. For customer notification? Is that what you're
6 referring to?

7 Q. Well, for all of the filings that have to be
8 made, all of the copying costs, costs of mailing out
9 notice, the cost of publishing notice, et cetera, yes.

10 A. I would agree.

11 Q. And they incur costs for consultants like
12 Mr. Bourassa?

13 A. Well, I don't know that all of them do.

14 Q. Okay. How about in this case?

15 A. In this case, apparently so.

16 Q. Okay. And often a Class A utility would incur
17 rate case expense for lawyers like me and the guy sitting
18 next to me?

19 A. In Chaparral's case, apparently, yes.

20 Q. I mean, Staff isn't suggesting that the utility
21 can't recover some amount of rate case expense for these
22 items that we just went through, correct?

23 A. Repeat the question, please.

24 Q. Staff is not suggesting that it's inappropriate
25 for this Class A utility to incur rate case expense for

1 things such as copying, mailing, publication, consultants,
2 and legal, is it?

3 A. No.

4 Q. And you have reviewed the company's backup
5 information regarding the rate case expenses incurred in
6 this case?

7 A. Yes.

8 Q. So you're aware that the company has spent on
9 just copying and mailing roughly \$11,000, subject to
10 check?

11 A. Subject to check.

12 Q. How much rate case expense should a Class A
13 utility incur for preparing direct testimony and an
14 application?

15 MR. VAN CLEVE: Your Honor, I object I guess as
16 to what -- I mean, he's asking what they should incur as
17 an expense? I don't know that Mr. Millsap would know what
18 a company should incur in expenses.

19 MR. SHAPIRO: Well, I'm sorry.

20 ALJ WOLFE: Is your objection that it calls for
21 speculation?

22 MR. VAN CLEVE: Yes, Your Honor.

23 MR. SHAPIRO: Well, if Mr. Millsap is not
24 qualified to state what a reasonable amount of rate case
25 expense is, then we would be happy to strike his

1 testimony. But he's testifying as to what he believes is
2 a reasonable amount of rate case expense, and I think the
3 questions regarding how he comes up with that are
4 certainly fair game.

5 MR. VAN CLEVE: I don't believe that was the
6 question before the witness, though.

7 ALJ WOLFE: Mr. Shapiro, it does -- I know you're
8 using the word incur instead of recover.

9 MR. SHAPIRO: I can change that. That's fine.
10 That's a fair change.

11 Q. (BY MR. SHAPIRO) Mr. Millsap, let me correct the
12 question and ask how much should a Class A utility in a
13 typical Commission rate case be allowed to recover in its
14 rate case expense for the time and expense of preparing
15 direct testimony and a rate application?

16 A. In my opinion, \$150,000.

17 Q. Just for the direct testimony and application?

18 A. No. That's for the entire rate case expense.

19 Q. Okay. Well, what portion of that would be fairly
20 attributable to that task?

21 A. That calls for speculation, and I can't answer
22 that question.

23 Q. What about with respect to a rebuttal filing?

24 A. Same answer.

25 Q. So you're objecting now to the questions that

1 we're asking you. The witness gets to pose objections? I
2 mean, if you don't know, please say you don't know, but
3 I'm not familiar with witnesses getting to decide whether
4 a question is objectionable or not. I apologize.

5 A. Okay.

6 Q. Are you unable to break this down into a
7 component-by-component basis? You just look at the top to
8 bottom at the 30,000-foot level? Is that what you're
9 saying?

10 A. Yes.

11 Q. And a reasonable amount of rate case expense,
12 then, of \$150,000 you believe is appropriate when \$11,000
13 is incurred just for mailing and copying alone?

14 A. That's my testimony, yes.

15 Q. And your testimony is, as you state it in your
16 direct testimony, the \$150,000 you recommend is based on
17 the rate case expense approved by the Commission in cases
18 of comparable-sized utilities; is that correct? And I
19 would be happy to refer you to your testimony, if you
20 would like.

21 A. Would you, please.

22 Q. Yes, sure. It's at your direct testimony at
23 Page 32.

24 A. Okay. That is my testimony.

25 Q. I'll just mark an exhibit.

1 Let me hand you Staff's response to data request
2 1.27, which has been marked as Exhibit A-14.

3 Mr. Millsap, it's correct that we asked you to
4 identify each and every comparable-sized utility that was
5 considered by Staff in reaching its recommendation for
6 rate case expense, correct?

7 A. That's correct.

8 Q. And you identified for us four utilities from the
9 state of Kansas, correct?

10 A. Yes.

11 Q. So these weren't approved -- these weren't
12 comparable-sized utilities in Commission rate cases,
13 correct, at least not the Arizona Commission?

14 A. They were, however, comparable-sized companies
15 based on my experience.

16 Q. But that wasn't my question. These were not
17 companies that had rate cases adjudicated by this
18 Commission, were they?

19 A. No.

20 Q. Can you tell me what rate case expense was
21 awarded to Empire District Electric Company?

22 A. No, I don't recall.

23 Q. Can you tell me what rate case expense was
24 awarded to People's Natural Gas?

25 A. No, I don't recall that either.

1 Q. How about Western Resources?

2 A. No.

3 Q. How about Oneok?

4 A. No.

5 Q. Can you tell me when rate case expense was
6 awarded to each of those companies?

7 A. 1993 through 1997.

8 Q. So you don't know the amount of these cases, the
9 amount of rate case expense that was awarded, and they
10 were awarded over 10 years ago, and you considered these
11 companies in reaching your conclusion in this case; is
12 that correct?

13 A. That's correct.

14 Q. How does the Kansas ratemaking process between
15 1993 and 1997 compare to the Arizona ratemaking process
16 today?

17 A. Very similar.

18 Q. Is there any difference in Kansas in how rate
19 case expense is accounted for and recovered by utilities?

20 A. Not that I recall.

21 Q. Did any of these entities use in-house staff
22 accountants or lawyers to handle these rate cases?

23 A. They all had a regulatory staff, yes.

24 Q. So that would have had an impact on the amount of
25 rate case expense that they incurred, correct?

1 A. Since they did it in-house, I don't have any way
2 to make that comparison.

3 Q. Well, if Chaparral City had in-house counsel that
4 did their rate cases or in-house accountants that were
5 qualified, they would reduce their rate case expense,
6 correct?

7 A. I assume that would be the case, but I really
8 don't have any way to answer the question.

9 Q. You also answered in the second paragraph,
10 Exhibit A-14, that Staff notes that rate case expense has
11 been awarded by the Commission in a number of dockets.

12 What does that mean, Staff notes?

13 A. It just means that rate case expense has been
14 awarded in these companies by these -- in those cases.

15 Q. Did you look specifically at any of these cases
16 that you mention here, Arizona-American, Arizona Water,
17 Pine Water?

18 A. No, I did not.

19 Q. Did you look at Decision 69164 for Black
20 Mountain, which was decided December 5, 2006, in which the
21 utility was awarded \$150,000, to compare to your
22 recommendation?

23 A. No, I didn't.

24 Q. How about Decision 69335, decided February 20,
25 2007, when Far West Sewer Company for its sewer division

1 received \$160,000 of rate case expense? Did you compare
2 that case?

3 A. No, I didn't.

4 Q. Let's try this one. Did you look at Decision
5 68176, the last rate case for this company, to see how
6 that compared in rate case expense to your recommendation
7 here?

8 A. Well, in my professional opinion, the rate case
9 expense should not exceed \$150,000.

10 Q. Okay. That's nice, but that wasn't my question.
11 My question was did you look at the last case?

12 A. And that's the answer that I'm going to give.

13 Q. So wouldn't Chaparral City be a very comparable-
14 sized utility to Chaparral City?

15 A. I don't think that's a question that makes any
16 sense exactly.

17 Q. Well, you said that you looked at comparable-
18 sized utilities, correct?

19 A. Yes.

20 Q. Well, what company is more comparable to
21 Chaparral City Water Company than Chaparral City Water
22 Company in its last rate case?

23 A. I still think that's a --

24 Q. Okay.

25 A. -- nonsense question.

1 Q. Staff recommends that rate case expense, whatever
2 amount that's awarded, be normalized, not amortized; is
3 that correct?

4 A. That's correct.

5 Q. And that means that the Commission would say that
6 this is a reasonable amount of rate case expense for the
7 company to incur in a given year?

8 A. Correct.

9 Q. But most of the rate case expense in a particular
10 rate case is incurred outside of a test year, correct?

11 A. That would be correct, yes.

12 Q. And so Staff's view would be, then, that if the
13 utility then comes back for another rate case, that a new
14 normalized amount should be included in its income
15 statement?

16 A. Repeat that question, please.

17 Q. So you're asking the Commission to normalize rate
18 case expense, put an amount in the income statement, and
19 then when a new rate case is filed, then you put a new
20 normalized amount in?

21 A. That's correct.

22 Q. So if Judge Wolfe were to award the company the
23 280,000 that is requested in this case and normalize it
24 over three years, it would be \$93,333 a year recovered
25 through rates, correct?

1 A. Subject to check, that sounds like it.

2 Q. I think Ms. Wood has a Hewlett-Packard if you
3 want to check it.

4 A. Actually, I have my own.

5 Q. If you could loan it to Ms. Wood tomorrow.

6 A. It's not a Hewlett-Packard.

7 Q. If the company were, then, to come back in for
8 rate relief based on a 2008 test year, Staff would
9 recommend a new normalized amount than the \$93,333?

10 A. That's correct.

11 Q. And what about the 150- to \$200,000 in that
12 hypothetical that the utility still hasn't recovered?
13 They just forfeit that?

14 A. I'm not sure I like the word forfeit, but --

15 Q. Well, how would they recover it?

16 A. They wouldn't.

17 Q. Is this intended to be some sort of a
18 disincentive for companies to seek rate relief too soon
19 after one rate case is decided?

20 A. I don't have any basis to answer that question.

21 Q. Doesn't Staff often suggest that if a utility is
22 not making its authorized return or recovering its
23 expenses it should come in again for a rate case?

24 A. I believe that's been done, yes.

25 Q. And don't numerous Commission decisions allow for

1 recovery of rate case expense amortized over a certain
2 number of years?

3 A. I couldn't tell you that. I don't know.
4 Oftentimes normalized and amortized are terms used
5 interchangeably, although they mean different things.

6 Q. Let me ask -- try this possibility. What if rate
7 case expense was recovered through a surcharge? And let's
8 just say for round numbers that \$200,000 was authorized to
9 be recovered over two years.

10 Wouldn't using a surcharge ensure that the
11 utility doesn't underrecover or overrecover rate case
12 expense, because as soon as it got to its recovery level
13 the surcharge could stop?

14 A. I would have to do a more detailed analysis then.

15 Q. Well, if we had -- let me simplify it further.
16 If we had \$120,000 of rate case awarded and it was to be
17 recovered by the utility over two years, couldn't the
18 utility recover \$5,000 a month for two years and recover
19 exactly the allowed rate case expense?

20 MR. VAN CLEVE: Objection, Your Honor. I'm not
21 sure this is relevant to what is before us.

22 MR. SHAPIRO: But if the issue is whether or not
23 a utility can -- how we treat recovery of rate case
24 expense, I'm not sure why this isn't relevant. I mean, if
25 he's not able to answer, he can certainly say so.

1 ALJ WOLFE: I'll allow the question because of
2 the issue of normalization versus amortization.

3 MR. SHAPIRO: Thank you.

4 THE WITNESS: I would agree with what you said.

5 Q. (BY MR. SHAPIRO) And shouldn't the goal of
6 authorizing a level of rate case expense and a mechanism
7 for recovering it be to ensure that the utility as close
8 as possible recovers no more or no less than it's
9 entitled to?

10 A. That is the intended purpose of the ratemaking
11 process.

12 Q. Thank you.

13 Now, Staff and the company agree that the
14 company's irrigation rate needs to be increased, correct?

15 A. Correct.

16 Q. The irrigation rate is currently lower than the
17 commodity rate for residential customers?

18 A. I believe that's the case.

19 Q. And the company proposes that the irrigation rate
20 be raised equal to the middle residential block and the
21 initial block for commercial and industrials, correct?

22 A. Could you repeat the question, please?

23 Q. Yeah, sorry. That was poorly worded.

24 ALJ WOLFE: Mr. Shapiro, you moved on to a
25 different issue.

1 MR. SHAPIRO: Yeah, although it's a very short
2 subject.

3 ALJ WOLFE: Go ahead.

4 Q. (BY MR. SHAPIRO) Thank you. The company
5 proposes that the irrigation rate be raised to a level
6 that equals the middle residential block and the initial
7 block for commercial and residential. I'm sorry. For
8 commercial and industrial.

9 A. I believe that's the case, yes.

10 Q. And the company's rationale was that would better
11 promote conservation?

12 A. I believe that's what they've testified to, yes.

13 Q. And Staff proposes less of an increase in the
14 irrigation rate, correct?

15 A. Correct.

16 Q. Why is it that Staff is proposing less of an
17 increase than the company?

18 A. Well, I think there's two reasons for that. One,
19 it's because Staff's recommended rates overall are lower,
20 and the second reason would be gradualism.

21 MR. SHAPIRO: Your Honor, I think this probably
22 would be a good time to take a break.

23 ALJ WOLFE: That sounds like a good idea. Let's
24 take a 20-minute break and come back at 11:05.

25 (A recess was taken from 10:45 a.m. to 11:06 a.m.)

1 ALJ WOLFE: Let's go back on the record.

2 Mr. Shapiro.

3 MR. SHAPIRO: Just a couple more questions.

4 Q. (BY MR. SHAPIRO) Mr. Millsap, in Mr. Bourassa's
5 rejoinder testimony, he testified that he prepared a
6 revenue proof of the rates proposed by Staff in its direct
7 filing, and that based on that he believes that Staff's
8 rates don't produce the revenue requirement that's set
9 forth in Staff's direct filing, and that he was working
10 with Staff to identify the reason.

11 Are you aware of that, and are you working with
12 Mr. Bourassa in an effort to address that?

13 A. Well, I was not aware that that was in his
14 testimony, but we were working trying to figure out what
15 was correct.

16 Q. So if there's some error that leads to the
17 problem of proof of revenue, Staff will endeavor to work
18 that out with the company?

19 A. That's correct. When I did the proposed rates
20 for -- or the proposed revenue that the company came up
21 with, I used the same bill count information that came
22 from Mr. Bourassa. Evidently he used something different,
23 so we don't know what exactly the difference is.

24 Q. But you're working on it?

25 A. We are working on it.

1 Q. Okay. And if there's some need to report back,
2 everybody will, correct?

3 A. Correct.

4 Q. Okay. Let me hand you what I have marked as
5 Exhibit A-15. This is Staff's response to data request
6 4.4. That is Staff's response to data request 4.4?

7 A. Yes. I'm sorry. I didn't know you had posed a
8 question.

9 Q. That's okay.
10 Why are the inflationary considerations for
11 operating expenses different than the inflationary
12 considerations for rate of return?

13 A. Because the rate of return only deals with one
14 component, whereas with operating expenses any inflation
15 or deflation could be dependent or would be dependent on
16 which expense is being considered.

17 Q. And what has Staff done to take into account the
18 effect of inflation on operating expenses since the end of
19 the test year, in this case 2006?

20 A. There's been no analysis like that.

21 Q. Would Staff agree to an adjustor based on the CPI
22 for the company's operating expenses to be included in
23 rate design?

24 A. That's not really in my field of expertise, but
25 I'm not sure that the CPI would be a good indicator to

1 use. I would have to do a lot more research on it before
2 I could really give you a good answer to the question.

3 Q. And will you do that research and analysis and
4 see if it would be appropriate to do that?

5 A. No. Nobody has asked me to so --

6 MR. SHAPIRO: Thank you, Mr. Millsap.

7 Oh, I'm sorry. I have some exhibits I better
8 move. A-14 and A-15, I believe, have not been moved yet,
9 so I'll move those.

10 ALJ WOLFE: Are there any objections?

11 MR. VAN CLEVE: No objections, Your Honor.

12 ALJ WOLFE: A-14 and A-15 are admitted.

13 (Exhibits A-14 and A-15 were admitted into
14 evidence.)

15 ALJ WOLFE: Mr. Millsap, I just have a couple of
16 questions I'm going to ask you before we move on to RUCO.

17

18 EXAMINATION

19

20 Q. (BY ALJ WOLFE) In Mr. Bourassa's rebuttal
21 testimony, Exhibit A-5, do you still have that up there?

22 A. Yes, I do.

23 Q. On Page 29, I have a question referring to
24 something that he said there. It's the question that
25 begins on Line 22 of Page 29 regarding what he believes

1 the treatment of unrecovered CAP allocation costs should
2 be.

3 A. Okay.

4 Q. Could you tell me how that differs from Staff's
5 recommendation?

6 A. I believe that Mr. Bourassa is implying that the
7 unrecovered M&I costs should be set up as a regulatory --
8 or a deferred regulatory asset. And although Staff never
9 has mentioned it anywhere, that would be Staff's position,
10 that it should be set up as a deferred regulatory asset.

11 Q. Okay.

12 A. It just inadvertently got missed.

13 Q. If that position is adopted by the Commission,
14 it's my understanding that that there needs to be some
15 accounting order language in the order; is that correct?

16 A. I believe that's the case, yes.

17 Q. Does Staff have any recommendation for language
18 like that or would Staff be willing to file that?

19 A. We could file that, yes.

20 Q. Okay.

21 A. I believe. I would have to check with my
22 attorneys, but I'm not sure why we would not be able to do
23 that.

24 ALJ WOLFE: Mr. Van Cleve.

25 MR. VAN CLEVE: Yes, I believe that's something

1 that Staff can do.

2 Q. (BY ALJ WOLFE) Could you make a note of that and
3 have that filed as a late-filed exhibit? I think the
4 company is planning to file something on December 23.
5 Would that be something that you would be able to do by
6 that date?

7 A. As far as I know, yes.

8 Q. Okay. And I had one more question for you.
9 Were you present in the hearing room yesterday
10 when Mr. Coley was testifying?

11 A. Yes, I was.

12 Q. And I asked him a question about -- it was an
13 accounting question regarding what happens to fully
14 depreciated plant that remains in service. Did you hear
15 his answer to that question?

16 A. Yes, I did.

17 Q. Do you have any reason to disagree with it, or
18 would you like to just give me your own answer? It's up
19 to you.

20 A. Well, if I could just give you my own answer.

21 Q. Okay.

22 A. If fully depreciated plant is separately
23 identifiable when it's fully depreciated, when it gets
24 considered for rate base then there's -- the accumulated
25 depreciation offsets what the cost would be. If group

1 asset accounting is used, as additions are made to the
2 plant account, depreciation is figured on the total
3 balance. So an asset that had a useful life that has
4 expired can conceivably under those circumstances not have
5 its full accumulated depreciation calculated because of
6 the way that type of asset accounting works.

7 Q. So if that were the case, then the company would
8 still be earning a return on that asset as well as of the
9 asset?

10 A. That's correct.

11 ALJ WOLFE: Thank you.

12 Ms. Wood.

13 MS. WOOD: Thank you, Your Honor.

14

15 CROSS-EXAMINATION

16

17 Q. (BY MS. WOOD) Good morning still yet,
18 Mr. Millsap.

19 A. Good morning.

20 Q. I just have a few questions for you. And by few
21 I don't mean -- I have a few more questions for you. I
22 don't mean to imply that I only have three or four, but I
23 have a few.

24 A. Few means different things to different people.

25 Q. Yes, it does, doesn't it?

1 You're a CPA?

2 A. That's correct.

3 Q. Okay. And you're licensed in the state of
4 Arizona?

5 A. Yes, I am.

6 Q. Okay. And how long have you been a CPA, whether
7 you were here licensed or licensed elsewhere? What is
8 your history?

9 A. I passed the CPA exam and became certified in
10 1973.

11 Q. Okay. And since that time you've been licensed
12 both here and in Kansas?

13 A. I've been licensed here since '73, yes. I was
14 licensed in Kansas during the time that I worked for the
15 Kansas Commission. And when I went to South Carolina,
16 even though I didn't work for the commission there, I also
17 got my license to practice public accounting in South
18 Carolina.

19 Q. Okay. And you also are a member of an
20 organization called the American Institute of CPAs?

21 A. That's correct.

22 Q. Okay. And they have a code of conduct, correct?

23 A. That's correct.

24 Q. And within that code of conduct, is it
25 appropriate for a member to subordinate their opinion to

1 another, or would you agree that's not appropriate?

2 MR. VAN CLEVE: Objection. Your Honor, I don't
3 see the relevance of this. I don't see the relevance of
4 this question.

5 ALJ WOLFE: Ms. Wood.

6 MS. WOOD: It's entirely relevant, Your Honor.
7 If he has a code of conduct in which he operates, I want
8 to examine the extent that the conduct -- the code of
9 conduct applies to him and how he feels it applies to this
10 case and whether or not he's met it.

11 ALJ WOLFE: To which point?

12 MS. WOOD: To the point of his change in position
13 on his testimony on the settlement proceeds.

14 MR. VAN CLEVE: I continue to object. I don't
15 see the relevance to this in this proceeding. Staff's
16 entitled to change its position as testimony evolves in a
17 case, and that's what happened here. And I don't see -- I
18 mean, it doesn't involve ethics at all.

19 MS. WOOD: I have to simply disagree.

20 ALJ WOLFE: I'm confused as well. I don't
21 understand. Could you point to exactly which accounting
22 issue it is that you're referring to?

23 MS. WOOD: I'm laying foundation, Your Honor, and
24 I ask just a little bit of latitude. I'm exploring under
25 what standards he believes he operates, and I think I'm

1 entitled to examine that as a foundation for any opinion
2 that he gave today, any opinion. And I just think it's
3 totally relevant, and any argument to the contrary borders
4 on frivolous.

5 ALJ WOLFE: I would like to know to which
6 accounting point you're aiming your questioning --

7 MS. WOOD: And let me just --

8 ALJ WOLFE: -- in order to establish whether or
9 not it's relevant or not in this case.

10 MS. WOOD: What I'm trying to explore, Your
11 Honor, is whether or not his change in position on the
12 issue of the settlement proceeds is merely reflecting and
13 conveying the opinion of a party who is not here, or
14 whether he personally has changed his opinion. And if he
15 personally has changed his opinion, whether or not he
16 believes that rises to a level of subordinating his
17 opinions to another, and I think that's entirely relevant.

18 ALJ WOLFE: I'll allow you to ask him whether
19 he's personally changed his opinion.

20 MS. WOOD: Thank you.

21 Q. (BY MS. WOOD) Have you changed your opinion on
22 the analysis of settlement proceeds?

23 A. My personal opinion?

24 Q. Yes.

25 A. No.

1 Q. Thank you.

2 I would like to talk to you a little bit about
3 the issue of working capital. Okay.

4 A. Okay.

5 Q. Did you review RUCO's lead/lag study?

6 A. Not in any detail, no.

7 Q. Why not?

8 A. I don't recall actually why. I read the
9 testimony and kind of glanced at it, but I didn't study it
10 in detail. I didn't feel like it was necessary, I guess.

11 Q. And why wouldn't it be necessary to review that?
12 It was adopted by the company, correct?

13 A. I believe that would be the case, but I didn't
14 find out about that until -- I don't recall. I'm sorry.

15 Q. That's all right.

16 Can you tell me what Staff's position is on the
17 analysis of -- I guess this is cash working capital. You
18 use a -- I think it's called a zero amount; is that
19 correct?

20 MR. VAN CLEVE: Could you point to a specific
21 reference in his testimony?

22 Q. (BY MS. WOOD) Are you confused about my
23 question, Mr. Millsap?

24 A. Yes, I am.

25 Q. Are you recommending a zero amount for working

1 capital?

2 A. That's correct.

3 Q. Okay. Why?

4 A. Because the company didn't submit a lead/lag
5 study.

6 Q. Do you believe that your zero amount for working
7 capital is more accurate than the fully developed lead/lag
8 study performed by RUCO?

9 A. I would say no.

10 Q. Thank you.

11 I want to draw your attention to your direct
12 testimony, Page 11. Does the change in Staff's position
13 on the issue of settlement proceeds change the fact that
14 Wells 8 and 9 were put in service in 1971 and 1972,
15 respectively?

16 MR. SHAPIRO: Sorry, Ms. Wood. What page?

17 THE WITNESS: No, it wouldn't change that.

18 MR. SHAPIRO: What page are you on?

19 MS. WOOD: I was on Page 11, Mr. Shapiro. I'm
20 now on Page 12.

21 MR. SHAPIRO: Thank you very much.

22 Q. (BY MS. WOOD) I'm going to start at the top of
23 Page 12 of direct testimony, Mr. Millsap.

24 Does the change in position by Staff negate the
25 fact that these wells became fully depreciated in 2001 and

1 2002 according to the company's response to data request
2 MEM7.3?

3 A. No, it didn't change.

4 Q. Does the fact that the Staff has changed position
5 on this matter change the fact that the ratepayers through
6 depreciation expense and return on rate base included in
7 the water service rates have paid the company for the
8 original cost of the wells and have continued to pay
9 because Chaparral uses a group depreciation method?

10 A. No, that didn't change.

11 Q. Thank you.

12 Now I'm on Page 13 of your direct testimony.

13 Does the fact that Staff changed its position on the
14 allocation of settlement proceeds change the testimony of
15 Mr. Hanford, the manager of Chaparral?

16 MR. VAN CLEVE: Objection, Your Honor. I don't
17 know how his testimony would have any effect on
18 Mr. Hanford's testimony.

19 MS. WOOD: I'm simply trying to explore which, if
20 any, portions of these facts have changed, Your Honor,
21 which are the foundation or were the foundation of the
22 prior decision. I'm just trying to explore to the extent,
23 if any, some of them have changed now.

24 MR. VAN CLEVE: I think Mr. Hanford's testimony
25 speaks for itself on that matter.

1 ALJ WOLFE: I would agree with that, Ms. Wood.
2 Sustained.

3 Q. (BY MS. WOOD) Does the change in position by
4 Staff reflect a change in the analysis that the equivalent
5 cost of the water to replace the amounts in the wells, the
6 \$1.52 million, was to -- was the equivalent cost to
7 replace the water -- the cost of the water to replace the
8 amount the wells would have produced for the remainder of
9 their useful life?

10 A. That is what Mr. Hanford testified to, and I
11 don't know of any reason why it would have changed.

12 Q. Thank you.

13 Would the Staff's change in position have
14 modified the fact that the customers have fully paid for
15 the well and approximately 1.52 million in water contained
16 in it?

17 ALJ WOLFE: In water -- what was the last word
18 you said?

19 MS. WOOD: Contained in it. Sorry, Your Honor.

20 ALJ WOLFE: Thank you.

21 THE WITNESS: Could you repeat the question,
22 please?

23 Q. (BY MS. WOOD) I'm looking at your testimony on
24 Page 13, Lines 11 and 12. And what I'm trying to examine
25 is whether or not the change in position now means that

1 the customers have not fully paid for the well and
2 approximately 1.52 million in water contained in it. Is
3 that changed?

4 A. No.

5 Q. Does Staff's change in position mean that the
6 \$1.52 million would effectively lower the cost of more
7 expensive CAP water to that of less expensive water that
8 could have been pumped from Well 9, therefore making the
9 customers whole?

10 A. No.

11 Q. Does the Staff's change in position alter the
12 notion that CAP water is more expensive than pumping
13 groundwater?

14 MR. SHAPIRO: Objection. Assumes facts not in
15 evidence.

16 MS. WOOD: Let me ask the question, then, as
17 foundation.

18 Q. (BY MS. WOOD) Mr. Millsap, is CAP water more
19 expensive than groundwater?

20 A. This is Staff's position, yes.

21 Q. Thank you. So does the fact that Staff has
22 changed position on the allocation of the proceeds change
23 that fact?

24 MR. VAN CLEVE: Your Honor, I'm going to object
25 to this line of questioning. I mean, I don't think

1 Mr. Millsap has indicated his testimony has changed. I
2 think he said yesterday that a policy decision was made by
3 the Directors's office to change the recommendation. I
4 don't think there's been any testimony by Mr. Millsap that
5 the accounting has changed in his testimony that's been
6 filed in this matter.

7 ALJ WOLFE: And Staff is willing to stipulate to
8 that?

9 MR. VAN CLEVE: Yeah.

10 ALJ WOLFE: Thank you.

11 Ms. Wood, does that end your line of questioning?

12 MS. WOOD: I just have one global question, then.

13 And actually, apparently I have a few more
14 questions now. I have just been handed a few.

15 Q. (BY MS. WOOD) When you testified yesterday,
16 then, you were simply conveying a Staff policy change.
17 You were not providing expert testimony on the cost or
18 benefits of that change. You're not adding the weight of
19 your CPA status or anything to the weight of that
20 decision. You were just conveying a decision made by
21 Staff's policymakers?

22 A. That's correct, yes.

23 Q. Thank you.

24 And when that change was made, did anybody try to
25 determine what the impact on the ratepayer would be?

1 MR. VAN CLEVE: Objection, vague. Anyone?

2 Q. (BY MS. WOOD) Well, did you, Mr. Millsap?

3 A. I did not, no.

4 Q. Okay. Has anyone in Staff provided you with
5 information about that type of analysis before you
6 appeared and reflected that change?

7 A. No.

8 Q. Okay. So it's fair to say you have no idea what
9 the impact on the ratepayer is?

10 MR. VAN CLEVE: Objection, Your Honor.

11 ALJ WOLFE: Why don't you ask him if he has any
12 idea first.

13 Q. (BY MS. WOOD) Do you have any idea what the
14 impact is on ratepayers?

15 A. I'm going to assume that it will increase rates,
16 but to what extent I have no idea.

17 Q. Thank you, Mr. Millsap.

18 When did you discover this change in position?

19 A. Yesterday afternoon.

20 Q. Yesterday afternoon or yesterday morning?

21 ALJ WOLFE: Asked and answered. He said
22 yesterday afternoon. You don't have to answer again.

23 THE WITNESS: Okay. Thank you.

24 Q. (BY MS. WOOD) Is that why the position was not
25 reflected in your direct, surrebuttal, or summary that

1 were provided to RUCO?

2 A. That would be correct.

3 MS. WOOD: I have no further questions, Your
4 Honor.

5 ALJ WOLFE: Thank you.

6 MR. SHAPIRO: Judge Wolfe, before Staff does its
7 redirect, may we ask a couple of follow-up questions?

8 ALJ WOLFE: Yes.

9 MR. SHAPIRO: Thank you.

10

11 FURTHER CROSS-EXAMINATION

12

13 Q. (BY MR. SHAPIRO) Not to belabor the point, but I
14 do want to ask a similar question that Ms. Wood asked.

15 Does the change in position change the fact that
16 Wells 8 or 9 were not serving customers at the time that
17 they were impacted by the Fountain Hills Sanitary
18 District?

19 MS. WOOD: I think that's objection. Those facts
20 are not in evidence.

21 MR. SHAPIRO: Sure, they are. They were
22 testified to yesterday and they are in the record.
23 They're in a data request response that we put in the
24 record, and they're in the testimony of Mr. Hanford. So
25 they are in evidence.

1 ALJ WOLFE: Overruled.

2 THE WITNESS: I was under the impression that
3 Well 9 was in use at the time.

4 Q. (BY MR. SHAPIRO) Do you have --

5 A. Because I have nothing --

6 Q. You don't know either way? You're not familiar
7 with the fact that those wells were both capped pursuant
8 to the settlement agreement?

9 A. They were -- yeah, they -- well, they've been
10 taken out of service pursuant to the agreement.

11 Q. Right. So you're not sure whether they were
12 serving customers or not before the impact?

13 A. That's correct.

14 Q. Okay.

15 A. I do not know that for sure.

16 Q. And you testified that Staff changed its position
17 for policy reasons, correct?

18 A. That's correct.

19 Q. Would you agree with me that the Commission's
20 decision in the Arizona Water Company case that the Judge
21 has taken judicial notice of was a policy decision; the
22 Commission wanted to incent utilities to pursue the rights
23 of the ratepayers and shareholders when people impair
24 their assets?

25 MR. VAN CLEVE: Objection, Your Honor. I think

1 the decision speaks for itself as to what it accomplished.

2 ALJ WOLFE: Sustained.

3 MR. SHAPIRO: My question was -- I'm sorry.

4 ALJ WOLFE: I sustained the objection because it
5 calls for a legal conclusion, I believe.

6 Q. (BY MR. SHAPIRO) Okay. Is groundwater less
7 expensive than CAP water if the groundwater has to be
8 treated for something like arsenic?

9 A. I have not done an analysis of that, so I can't
10 answer that question.

11 Q. But certainly you would agree with me that
12 treating groundwater for arsenic, if required, would make
13 that groundwater more expensive?

14 A. It would make it more expensive, yes.

15 Q. And Ms. Wood asked you if Staff had done an
16 analysis of the impact of what is now adopting the
17 company's position on the ratepayers.

18 My question is did Staff determine the impact of
19 its prior position on the company?

20 A. No.

21 MR. SHAPIRO: Thank you. Thank you, Judge.

22 ALJ WOLFE: Ms. Wood, do you have follow-up to
23 that? Normally the company would have gone -- anyway, you
24 can follow up on that.

25 MS. WOOD: Nothing at this point, Your Honor.

1 Thank you.

2 ALJ WOLFE: Thank you.

3 Is there redirect?

4 MR. VAN CLEVE: Just one question.

5

6

REDIRECT EXAMINATION

7

8 Q. (BY MR. VAN CLEVE) Mr. Millsap, earlier the
9 attorneys for the company asked you a question regarding
10 the \$1.7 million increase in revenue. Do you remember
11 that question?

12 A. Yes, I do.

13 Q. Is there also another method that Staff is
14 putting before the Commission that has a revenue -- an
15 increase in revenue of 1.4 million?

16 A. I believe that Mr. Abinah addresses that.

17 Q. But you are aware that there is another method
18 that Staff is putting forward for the Commission's
19 consideration?

20 A. Yes.

21 MR. VAN CLEVE: No further questions.

22 ALJ WOLFE: Thank you.

23 Is there recross on that issue?

24 MR. SHAPIRO: No.

25 ALJ WOLFE: Okay. Thank you for your testimony,

1 Mr. Millsap. You are excused as a witness.

2 Okay. We have some procedural issues that we
3 need to talk about this morning.

4 Ms. Wood, have you had an opportunity to confer
5 with your client regarding what would be necessary in
6 order to remedy what you believe is the procedural
7 disadvantage that RUCO has been exposed to?

8 MS. WOOD: Thank you, Your Honor. Do you mind if
9 I just consult based on the testimony we just received?
10 It would just take me a minute.

11 ALJ WOLFE: Okay. If you would rather take a
12 break and do it, we can do that, because we also have to
13 talk about the briefing schedule. So we can go on and
14 talk about the briefing schedule, and then we can take a
15 break and you can come back and let us know what it is
16 that RUCO would like to do. I don't want to rush that at
17 all.

18 MS. WOOD: Okay. Thank you so much.

19 ALJ WOLFE: Have the parties had a chance to
20 confer regarding briefing?

21 MR. SHAPIRO: Yes. The parties have agreed that
22 the Phase I briefing, which would deal with everything, I
23 guess, that will be covered through today, we would file
24 closing briefs on January 23 and reply briefs on
25 February 9.

1 ALJ WOLFE: Okay. And just to make it clear on
2 the record, the posthearing briefs for the Phase I issues
3 would include all of the issues with the exception of cost
4 of capital and rate of return.

5 MR. SHAPIRO: Is that correct, Mr. James?

6 MR. JAMES: Yes.

7 MR. SHAPIRO: Yes.

8 ALJ WOLFE: Because if you're going to cover
9 other issues besides cost of capital or rate of return in
10 January, I would like to know today. I just want that to
11 be clear on the record.

12 MR. SHAPIRO: You mean in the hearings in
13 January?

14 ALJ WOLFE: In the hearings in January, yes.

15 MR. SHAPIRO: Because we will cover them in the
16 briefs.

17 ALJ WOLFE: Right.

18 Okay. Those dates sound acceptable to me. Final
19 schedules need to be filed before that that tell the
20 parties what the parties' positions are. We've been doing
21 that, and is there any reason not to do that in this case?

22 MS. MITCHELL: No.

23 ALJ WOLFE: So have the parties talked about --

24 MR. SHAPIRO: We didn't, but do we want to do
25 that by the next hearing date? Would that be appropriate?

1 ALJ WOLFE: That would be fine. To have final
2 schedules filed by the next hearing date, is that what
3 you're talking about, or tell me what date?

4 MR. SHAPIRO: I guess that's what I was
5 suggesting.

6 Okay. Mr. James was suggesting that maybe just
7 in case something changes at that next hearing, that maybe
8 we do it in between the close of the hearing on the 9th
9 and the closing brief on the 23rd.

10 ALJ WOLFE: That seems like it would make sense
11 to me because of the possible impact of rate of return and
12 cost of capital.

13 MR. SHAPIRO: I'm pulling up my calendar.

14 MS. WOOD: Do you want to do the following
15 Friday, a week from the 9th?

16 MR. SHAPIRO: That will work for the company.

17 MS. MITCHELL: That's fine.

18 ALJ WOLFE: Okay. So simultaneous filing of
19 final schedules on January 16, and closing briefs on the
20 Phase I issues January 23, reply briefs on the Phase I
21 issues February 9.

22 Okay. And we'll take a short break so that RUCO
23 can confer.

24 MS. WOOD: Thank you, Your Honor.

25 ALJ WOLFE: Just let me know whenever you're

1 ready to come back.

2 (A recess was taken from 11:43 a.m. to 11:55 a.m.)

3 ALJ WOLFE: Let's go back on the record.

4 Ms. Wood.

5 MS. WOOD: Yes, Your Honor. I have talked to
6 both counsel, and what I have come up with is the
7 following. There are no witnesses who have provided
8 testimony on this shift in policy. It's just a simple
9 withdrawing objection to the company's position. So as
10 long as there are no policy witnesses coming forward, then
11 we don't feel the need to provide a rebuttal witness at
12 this juncture. However, in the event that any testimony
13 comes forward on this issue in terms of policy
14 perspective, we would reserve the right to ask or have a
15 rebuttal witness.

16 ALJ WOLFE: I don't have a problem with that.
17 Are you withdrawing your motion to strike at this time
18 then?

19 MS. WOOD: With much reluctance, yes.

20 ALJ WOLFE: Thank you. I appreciate not having
21 to rule on it.

22 Is there anything further procedurally that we
23 need to -- the order of witnesses, perhaps, on the 8th.
24 But Mr. James, you had something else?

25 MR. SHAPIRO: I think we have another witness

1 today, a rebuttal witness.

2 ALJ WOLFE: Oh, I apologize.

3 MR. SHAPIRO: That's okay. It will be short and
4 sweet, we hope, but we would like to call Mr. Bourassa.

5 ALJ WOLFE: Thank you. I knew there was a
6 possibility, but I wasn't sure whether you were calling a
7 rebuttal witness or not.

8 Mr. Bourassa you are still sworn in.

9 THE WITNESS: Yes.

10 ALJ WOLFE: Mr. James.

11

12

THOMAS J. BOURASSA,

13 called as a rebuttal witness on behalf of the Applicant,
14 having been first duly sworn by the Certified Reporter to
15 speak the truth and nothing but the truth, was examined
16 and testified as follows:

17

18

DIRECT EXAMINATION

19

20 Q. (BY MR. JAMES) Mr. Bourassa, are you situated?

21 A. Yes. Thank you, Mr. James. Thank you for
22 considering my comfort.

23 Q. Let's start with something that was mentioned, I
24 believe, in connection with Mr. Shapiro's cross-
25 examination of Mr. Millsap.

1 There appears to be a discrepancy between Staff's
2 revenue requirement and the revenues that are actually
3 produced by Staff's rate; is that correct?

4 A. Yes. According to my analysis, Staff's rates in
5 its direct filing do not produce the Staff's revenue
6 requirement in their direct filing. And I used the same
7 model I used in the company's initial application, the
8 same bill counts, and so I'm using the same data that I
9 used in the company's filing. And I did a revenue proof
10 on RUCO's rates and charges and was able to proof out
11 their revenues to their revenue requirement.

12 So having said that, I believe that there is a
13 problem in Staff's rates, and I believe it may be related
14 to the annualization for the golf courses. That may be
15 one of the problems, and I have not been able to go
16 further and identify anything else that might be a
17 problem.

18 Q. And I understand that there have been some
19 discussions to try to work out this issue?

20 A. Yes. I have been working with Staff and they're
21 cooperating. And with the hearings, we just haven't had
22 time to narrow down what exactly the issue is. So we are
23 working on it, and hopefully within the next week or so
24 we'll have a resolution of that and we'll be able to
25 comment on it at the next hearing, or sooner than that

1 maybe in our --

2 Q. Submitted in the schedules that have to be --
3 final schedules that have to be filed?

4 A. Yes, yes.

5 Q. Let's move on to depreciation, which seems to
6 have gotten extremely confusing for everybody.

7 And this again goes back to, I guess, the status
8 of Wells 8 and 9 that were constructed in the early 1970s,
9 appear to have been fully depreciated at some point in the
10 recent future, but there seems to be a lot of uncertainty
11 over the effect of including those wells in the company's
12 rate base in the last case.

13 Can you try to clarify for us, Mr. Bourassa, what
14 was the impact of those wells from a depreciation
15 standpoint?

16 A. Well, as I stated in my testimony on Monday, and
17 I believe in either my rebuttal or rejoinder testimony,
18 the company utilizes a group method or account-based
19 method of recording depreciation.

20 Q. Let me interrupt. Is that normally how it's
21 done? Is that typical?

22 A. Yeah, it's an acceptable regulatory accounting
23 practice.

24 Q. And there isn't any issue with respect to using
25 group accounting as opposed to looking at each individual

1 asset?

2 A. Correct.

3 Q. I'm sorry. Go ahead.

4 A. So when you're depreciating assets as a group,
5 remember that the depreciation rates we use are an
6 estimate of useful life. That is, on average we expect
7 assets to last approximately equal to the period of time
8 we're depreciating them over. Some will last less than
9 the estimated use of life; some will last more.

10 So to that extent, you know, we're looking for a
11 level of precision here that just isn't there. Unless a
12 depreciation study is to know exactly historically what's
13 happened with respect to useful lives of assets, we are
14 using typical and customary rates to record depreciation.

15 Q. So again, just so it's clear for the record, we
16 have an asset that typically has a useful life of, say,
17 20 years, and that means, then, you would use 20 years for
18 the purpose of determining the depreciation rate; is that
19 correct?

20 A. Correct. And we extend that to the group of
21 assets on the books. And we might have, for example, a
22 million dollars in wells and springs, and we would
23 depreciate that asset class or that group account on the
24 basis of \$1 million of investment.

25 Q. But to go back to your point, though, if a

1 particular well -- to use that example -- what is the
2 typical useful life of a well assumed to be?

3 A. It's assumed to be 30 years.

4 Q. So a well may last 25 years, it may last 40
5 years, but for depreciation purposes the group -- the rate
6 for that group is based on a 30-year useful life?

7 A. Correct. And so for ratemaking -- and this is
8 shown in my depreciation schedules calculation on the
9 C-2 -- it's basically done by asset group. And as long as
10 there is a depreciable balance, there will be depreciation
11 for that asset group.

12 And when we start to talk about specific assets
13 within that group and saying, well, one is fully
14 depreciated or I've overrecovered depreciation on a
15 specific asset within that group, we start to get into an
16 area of making a lot of assumptions. Okay.

17 I agree with Mr. Millsap in saying that if the
18 group is not fully depreciated, that is we still have a
19 depreciable balance, and you were to allocate that
20 accumulated depreciation at some point in time among the
21 assets within that group, that the wells -- in doing so
22 you would come up that the wells at this point in time are
23 not fully depreciated.

24 On the other hand, if you want to take another
25 view and say, well, I want to recalculate what the

1 accumulated depreciation would have been on a specific
2 asset, you could go back and do an individual calculation,
3 but that's not -- and then say, well, the assets would
4 have been depreciated by 2001 or 1979 or 1978. You could
5 do that.

6 But when we depreciate on an asset group, the
7 rate -- ultimately, the ratepayers are not harmed by that
8 methodology. Why is that? Because there is still a
9 depreciable balance, and the company is including in its
10 cost of service depreciation on that depreciable balance.

11 Okay. So if one wants to take the individual
12 asset view and say that the wells -- the company has
13 overrecovered depreciation on the wells, that is, let's
14 assume the wells cost \$100,000, and let's assume that in
15 1999 that the wells were fully depreciated, if you were,
16 again, looking on a specific asset view. Then, from 1999,
17 if the company continued to depreciate those wells, then
18 conceivably accumulated depreciation would exceed the
19 \$100,000 that was in that account and they would continue
20 to depreciate forward.

21 Q. So at that point -- just again to make sure I'm
22 following you -- at that point you would have a situation
23 where in the plant in service account you would have
24 100,000. And I think \$100,000 is roughly the amount --
25 the cost of constructing those two wells. So you would

1 have \$100,000 in a plant in service account -- in this
2 case wells and springs of \$100,000 -- but you would then
3 have, say, \$125,000 of corresponding depreciation, so you
4 would have, in effect, a negative \$125,000.

5 A. Well, you would have -- if I took that asset and
6 said, well, how would that asset appear in rate base, I
7 would essentially have a negative rate base portion for
8 that asset, you see? So then I would be getting a
9 negative return if we applied the return to that
10 particular asset in rate base. And so again, the
11 ratepayer isn't necessarily harmed by that.

12 Q. Well, let's go back --

13 A. Even though we might have included depreciation
14 in operating expenses.

15 Q. Well, let's go back to what has apparently caused
16 the confusion. In this particular case, there was an
17 adjustment made in this rate case. There was an
18 adjustment made to remove the two wells and, I think, a
19 related piece of equipment from rate base.

20 Now, how did you make that adjustment?

21 A. Well, as I explained the other day, I removed the
22 cost of the wells, the original cost of the wells, and I
23 made a similar adjustment to accumulated depreciation for
24 that same amount. That is, assuming my wells cost
25 \$100,000, I removed \$100,000 from plant in service, and I

1 removed \$100,000 from accumulated depreciation.

2 Q. So the net effect -- sorry to interrupt -- the
3 net effect on rate base is zero then?

4 A. Correct.

5 Q. Okay.

6 A. However, if we're now going to take the view that
7 the company overrecovered -- again, I don't agree with
8 this view -- on a specific asset, then we would need to go
9 back and make some assumptions as to when this plant was
10 fully depreciated, calculate how much excess accumulated
11 depreciation I recorded, and I would make -- I would
12 remove the \$100,000 of cost from plant in service and
13 maybe 125- or \$150,000 from accumulated depreciation. The
14 net effect of that would be to increase rate base; not to
15 have a zero impact on rate base, but to increase rate
16 base.

17 Q. Because the deduction to accumulated
18 depreciation, at that point you're reducing accumulated
19 depreciation more than you're reducing the plant in
20 service account?

21 A. Correct.

22 Q. So the overall effect is a higher rate base?

23 A. Correct.

24 ALJ WOLFE: So what you did, Mr. Bourassa, that's
25 in conformance with NARUC accounting standards?

1 THE WITNESS: Exactly. And that would be
2 consistent with the group asset approach.

3 Q. (BY MR. JAMES) And again, that goes back to what
4 you said initially, Mr. Bourassa, that some assets last
5 longer than others. And I assume if you have an asset
6 that is retired before its useful life, it's expected
7 useful life, you make the same adjustment, right?

8 A. Yes. And I may have underdepreciated it.
9 Looking at it on an asset specific view, I may have
10 underdepreciated that asset, in which case I'm -- while
11 making an equivalent adjustment to accumulated
12 depreciation as I do to plant in service, what I may be
13 doing is essentially lowering the accumulated depreciation
14 because I haven't fully -- I haven't fully depreciated
15 that asset.

16 So it all comes out in the wash by the
17 methodology we employ. And the ratepayer is not harmed by
18 this methodology, because either the rate base is going to
19 be less or it's going to be more, but the ratepayer is not
20 harmed and the company will not overrecover its investment
21 in that asset group.

22 Q. Let me ask you a few questions that relate to
23 Mr. Scott's testimony yesterday about the RCN study and
24 the RCND rate base just so it's clear on the record.

25 What is the purpose of an RCN study Mr. Bourassa?

1 A. The purpose of the RCN study is to help us
2 ascertain or derive a fair value of the company's utility
3 property. Traditionally, this Commission has required
4 that when a true fair value rate base is filed, that a
5 reconstruction cost new less depreciation rate base also
6 be filed, and then they -- that gives us the current value
7 of that property, plant and equipment. Then it's averaged
8 with original cost so it is a lower value than the current
9 value as produced by an RCN.

10 So the fair value rate base ends up being a very,
11 very, very conservative measure of value, and it's -- had
12 we done an appraisal or had I done an income-based
13 approach to valuing the company's property, I may have
14 come up with the same or more value than the RCND.

15 Q. Okay. And RCN, we're referring to the
16 reproduction or reconstruction cost study?

17 A. Right, using the Handy-Whitman indexes.

18 Q. And the purpose of that, if I understood what you
19 said, the purpose is to value the company's assets; is
20 that right?

21 A. Yes. And as I stated, ultimately what we end up
22 with is a very conservative measure of value. For
23 example, just on the RCN alone, we do not trend land,
24 water rights, intangibles things like that. They're not
25 trended. They're in at original cost. Had we appraised

1 the land, we might have had a higher value for the land
2 portion in the RCND study. Also, the plant that was added
3 during the test year is in its original cost. There is no
4 trending upward to increase that value.

5 Q. Now, one of the topics we discussed yesterday
6 with Mr. Scott was whether the RCN value includes
7 inflation. And in response to a follow-up question I
8 asked, I think you heard Mr. Scott say that by inflation
9 he meant that the cost of labor and materials have
10 increased.

11 Is it the purpose of the RCN study or the
12 Handy-Whitman indices to keep track of the impact of
13 inflation?

14 A. No. It's purpose is to drive a value. Had I,
15 again, used a market-based approach, comparative sales or
16 an income approach, you know, what these assets can
17 produce in terms of income, there would be no issue
18 with -- I mean, nobody would be able to point to,
19 quote-unquote, inflation.

20 In my mind it's a red herring. We're trying to
21 determine value, and one of the valid methods of
22 determining value is an asset-based approach like an RCND
23 study.

24 MR. JAMES: That's all I have, Your Honor.

25 ALJ WOLFE: Thank you.

1 Ms. Wood, does RUCO have any cross-examination
2 for this witness?

3 MS. WOOD: Yes, we do, Your Honor. Thank you.

4

5

CROSS-EXAMINATION

6

7 Q. (BY MS. WOOD) Just two questions. Mr. Bourassa,
8 just so that we're clear, is it fair to say that if we do
9 the adjustments that you suggested using the \$100,00
10 example of removing from plant in service and then also
11 from accumulated depreciation --

12 A. Correct.

13 Q. -- that there would be no depreciation expense on
14 a going-forward basis for the retired wells?

15 A. The depreciation expense for that asset group
16 would be lower.

17 Q. And there would be no depreciation expense for
18 the wells going forward. I'm sorry. For the retired
19 wells.

20 A. Well, my best answer, again, I don't -- again,
21 we're using the asset-based or the group-based accounting
22 methodology. So my answer is that for the asset group,
23 the depreciation expense would be lower now that we've
24 removed the cost of the wells from plant in service.

25 Q. Okay. Is it true that the RCND restates the

1 plant's assets in current dollars?

2 A. It restates the plant in service in dollars of
3 what it would cost to construct that same plant today.

4 MS. WOOD: Thank you.

5 ALJ WOLFE: Does Staff have cross-examination for
6 this witness?

7 MS. MITCHELL: No, Your Honor.

8 ALJ WOLFE: Any redirect, Mr. James?

9 MR. JAMES: No, Your Honor.

10 ALJ WOLFE: Thank you for your testimony,
11 Mr. Bourassa. You're excused.

12 THE WITNESS: Thank you.

13 ALJ WOLFE: Okay. Just to make sure that my
14 notes are correct, we have for January 8, Gordon Fox will
15 be testifying, and Mr. Parcell as well on the 8th.

16 MS. MITCHELL: Yes, that's correct.

17 ALJ WOLFE: Would that be your order: Fox,
18 Parcell, Abinah?

19 MS. MITCHELL: Yes.

20 ALJ WOLFE: And then -- well, Mr. James, do you
21 want your cost of capital witness to go first on the 8th?
22 Is there any --

23 MR. JAMES: No. I mean, that's fine. We're
24 happy to have Mr. Bourassa testify last.

25 MS. MITCHELL: I just need a date certain for

1 Mr. Fox. He won't be available on the 9th, so he will
2 have to go sometime on the 8th.

3 ALJ WOLFE: Will Mr. Parcell be here both days?

4 MS. MITCHELL: We can make him available for both
5 days, yes.

6 ALJ WOLFE: Okay. We'll have Mr. Fox with a date
7 certain of the 8th, and here is the order: Fox, Abinah,
8 Bourassa, Rigsby, and Parcell, unless there's any
9 objection.

10 Ms. Wood?

11 MS. WOOD: I just wanted to follow up on an issue
12 raised by Mr. Shapiro with regard to Mr. Chaves. Is that
13 issue yet resolved?

14 MR. JAMES: No. My understanding -- well, it's
15 resolved in the sense that I think Staff is going to file
16 a revised, redacted -- or redacted isn't the right word,
17 but revised version of Mr. Chaves's testimony indicating
18 what specifically is being adopted and what isn't being
19 adopted.

20 ALJ WOLFE: Okay.

21 MR. JAMES: The version -- as I tried to explain
22 this morning, Your Honor, as I said, the version that we
23 received was not -- unfortunately, was not the same
24 version as Mr. Chaves's testimony filed in the docket, and
25 that was a mistake and that's being corrected. So I

1 assume we'll probably see that in a couple of days.

2 ALJ WOLFE: And Mr. James, the company is
3 planning to file its rejoinder testimony to Mr. Parcell's
4 testimony based on that filing that we're expecting in a
5 couple of days on -- is it still December 23?

6 MR. JAMES: Yes, Your Honor. I would call it
7 supplemental rejoinder, but we're simply going to address
8 Mr. Parcell's testimony. Hopefully we'll keep it
9 relatively short.

10 ALJ WOLFE: At the time that you file your
11 supplemental rejoinder, will you please file something
12 regarding whether you intend to call Mr. Chaves?

13 MR. JAMES: Yes, I will. That will be perfect,
14 Your Honor, because by then we'll have a much better feel
15 for where we are. Thank you.

16 ALJ WOLFE: Does that answer your question?

17 MS. WOOD: Yes. Thank you, Your Honor.

18 ALJ WOLFE: Okay. Does RUCO intend to file any
19 further testimony in response to what Staff is planning to
20 file?

21 MS. WOOD: At this time, Your Honor, we don't
22 anticipate it. Okay. We'll take our opportunity to
23 address it through testimony. Thank you.

24 ALJ WOLFE: Through testimony on the stand. I
25 would ask that if RUCO does wish to file some sort of

1 prefilled testimony that they file it by December 23, at
2 the same time that the company files its testimony.

3 MS. WOOD: Thank you, Your Honor.

4 ALJ WOLFE: All right. Is there anything
5 further?

6 MS. MITCHELL: Nothing from Staff.

7 ALJ WOLFE: Okay. I'll wait to see what is
8 filed, and if there are no motions, then we'll reconvene
9 on January the 8th at 9:00 a.m. in order to make sure we
10 get all the witness in.

11 Thank you and enjoy your holidays.

12 (The Hearing recessed at 12:20 p.m.)

13

14

15

16

17

18

19

20

21

22

23

24

25

1 STATE OF ARIZONA)
) ss.
 2 COUNTY OF MARICOPA)

3

4 I, MICHELE E. BALMER, Certified Reporter
 5 No. 50489 for the State of Arizona, do hereby certify that
 6 the foregoing printed pages constitute a full, true and
 7 accurate transcript of the proceedings had in the
 8 foregoing matter, all done to the best of my skill and
 9 ability.

10

11 WITNESS my hand this 28th day of December, 2008.

12

13

14

Michele E. Balmer
 MICHELE E. BALMER
 Certified Reporter
 Certificate No. 50489

15

16

17

18

19

20

21

22

23

24

25