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ORIGINAL

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
SANDRA D. KENNEDY  
PAUL NEWMAN  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT.

DOCKET NO. W-01303A-08-0227

Arizona Corporation Commission

DOCKETED

MAR 17 2009

DOCKETED BY 

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT.

DOCKET NO. SW- 01303A-08-0227

NOTICE OF FILING  
TESTIMONY SUMMARIES

1 Arizona-American Water Company hereby files testimony summaries for the following

2 12 witnesses:

- 3 1. Thomas M. Broderick
- 4 2. Christopher C. Buls
- 5 3. Bradley J. Cole
- 6 4. Ian C. Crooks
- 7 5. G. Troy Day

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6 Hon. Bob Stump, Commissioner  
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11 Giancarlo Estrada, Aide to Chairman Mayes  
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36 Teena Wolfe, Administrative Law Judge  
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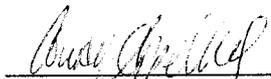
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By:

  
\_\_\_\_\_  
Courtney Appelhans

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
THOMAS M. BRODERICK  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

DIRECT TESTIMONY

1 Thomas M. Broderick testifies as follows:

2 This new rate case filing complies with deadlines for filing new rate cases established by the  
3 Commission in Decisions 68825, 69173, 69181, and 69396.

4 The total requested revenue increase is \$19,961,632 and the test year is 2007. Test year adjusted  
5 revenues and expenses include annualized actual ACRM revenues and expenses.

6 This case includes all Arizona districts, except the districts of Anthem Water, Anthem/Agua Fria  
7 Wastewater, Sun City Water, Sun City Wastewater, and Sun City West Wastewater which had  
8 rate cases recently.

9 Arizona-American's cost of capital is not less than 8.40%. The average cost of long-term debt is  
10 5.463% and the cost of equity is 11.75%. The forecasted equity ratio is 46.75% and the debt ratio  
11 is 53.25%. Short-term debt has again been excluded from the calculation of the capital structure.

12 Arizona-American's proposed rate case expense is \$612,000.

13 Amortizations of imputed regulatory AIAC should extend through July 14, 2008, rather than  
14 cease at December 31, 2007, because the full six and one-half year amortization period will  
15 expire July 14, 2008 and new rates in this case will not be established until late 2009 - long after  
16 the end of the amortization period.

17 White Tanks Plant CWIP should be included in rate base in the amount of \$25 million because  
18 the real estate slowdown has caused actual hook-up fees to be far below the forecast and it is fair  
19 for existing Agua Fria customers to pay for a portion of the White Tanks Plant in order to stay  
20 the course on funding the balance of the Plant via hook-up fees.

21 Arizona-American proposes a White Tanks Plant O&M deferral mechanism equivalent to an  
22 ACRM step increase which authorizes a deferral of twelve months of O&M expenses and  
23 recovery in the subsequent twelve months. Such a mechanism also provides the Commission an  
24 additional opportunity to include White Tanks Plant in service in rate base in the event that  
25 actual hook-up fees further disappoint.

26 Arizona-American proposes to amortize incremental White Tanks Plant hook-up fees in an  
27 accelerated amount, but not to exceed the total post in-service AFUDC accrued in that month to  
28 keep the deferred accumulated balance of post-in-service AFUDC at zero. Second, each month  
29 Arizona-American will also amortize any remaining available incremental WHU-I fees in an  
30 amount not to exceed the monthly depreciation expense for the White Tanks Plant. Third, each  
31 month any remaining incremental WHU-I funds will be applied as a contribution to the White  
32 Tanks Plant. All such contributions shall reduce the White Tanks Plant in the next month for  
33 purposes of calculating post-in-service AFUDC, depreciation expense, and the White Tanks  
34 plant balance.

35 Arizona-American requests an ACRM for Tubac district as a result of the US EPA's denial of a  
36 3-year extension in the arsenic compliance deadline and because Arizona-American plans to  
37 construct a facility in Tubac to be in-service in 2010. The estimated Step 1 increase is a \$25.98  
38 per month increase in the basic service charge and a \$3.14 per 1000 gallons increase for a 5/8  
39 inch meter residential customer.  
40

1 The existing ACRM surcharges for Agua Fria, Havasu, Paradise Valley and Sun City West  
2 should cease upon implementation of permanent rates at the conclusion of this case as the  
3 revenues and expenses would thereafter be in permanent rates.

4 Other Arizona-American's witnesses present important requests in this case.

#### 5 REBUTTAL TESTIMONY

##### 6 REBUTTAL REVENUE REQUIREMENT

7 Arizona-American's revised rebuttal requirement is shown on Schedule A-1 Rebuttal. Arizona-  
8 American has reduced its requested revenue requirement increase to \$16.2 million (40.2%  
9 increase) from its original request of \$20.0 million (50.2% increase).

##### 10 VOLUNTARY COMMUNITY OUTREACH

11 Arizona-American completed at least one voluntary community presentation in each of the  
12 districts included in this rate case in addition to voluntary written communication. Each  
13 community presentation consisted of a formal presentation, followed by a question-and-answer  
14 session. We also responded to approximately 500 customer e-mails received at  
15 "azrates@amwater.com" requesting that the proposed rate increase be calculated for an  
16 individual account.

##### 17 PARADISE VALLEY FIRE FLOW UPDATE

18 Arizona-American withdraws its request to re-establish the Public Safety surcharge in the  
19 Paradise Valley Water District to further fund its discretionary fire-flow projects.

20 High Block surcharge proceeds will be adequate to recover the costs of the initial study  
21 conducted several years ago and to recover the costs of the suspended Phase 3b before the High  
22 Block surcharge is eliminated upon conclusion of this case. The Public Safety surcharge can  
23 remain at zero.

##### 24 WHITE TANKS PROJECT

25 The existing WHU-1 hook-up fee tariff is a single fee by meter size that combines the original  
26 hook-up fee (\$1,150 for a 5/8 inch meter) and the incremental hook-up fee (\$2,130 for a 5/8 inch  
27 meter) approved in late 2007 to help pay for the White Tanks Water Treatment Plant. Arizona-  
28 American proposes to separate the single fee hook-up fee into two components with the second  
29 component (the White Tanks portion) ineligible for offset credits. The original hook-up fee  
30 (\$1,150, Component A) will continue to be used to pay for Arizona-American's existing  
31 investment in common facilities and will be eligible for offset against developer built common  
32 facilities. The White Tanks portion of the hook-up fee (Component B) will not be eligible for  
33 offset against developer built common facilities and will always be applied towards White Tanks  
34 plant.

##### 35 RATE CONSOLIDATION

36 Arizona-American has developed a flexible analysis tool to evaluate rate consolidation in this  
37 case. This will be made available to any party.

38 Based on several assumptions, rate consolidation today would result in the following rate  
39 changes by district:

40 Anthem (\$4.6) million or (47.74%) rate decrease

1 Tubac (\$0.3) million or (47.13%) rate decrease  
2 Havasu (\$0.6) million or (42.90%) rate decrease  
3 Agua Fria (\$3.5) million or (17.75%) rate decrease  
4 Sun City West (\$1.3) million or (15.69%) rate decrease  
5 Paradise Valley \$0.3 million or 2.95% rate increase  
6 Mohave \$1.7 million or 37.22% rate increase  
7 Sun City \$8.4 million or 136.00% rate increase

8 MOHAVE WASTEWATER FUTURE RATE ADJUSTMENT

9 If the Commission includes all of Mohave Wastewater's Wishing Well Plant in rates, Arizona-  
10 American is willing to accept a deadline to file the next Mohave Wastewater rate case, which  
11 may result in a rate decrease in the future for that district due to reflecting such mitigating factors  
12 as accumulated depreciation, increases in test year treatment volumes and accumulated hook-up  
13 fees. Additionally, in the interim until the next rate case, Arizona-American is willing to accept  
14 an annual requirement of a surcredit filing.

15 REBUTTAL OF STAFF

16 Imputed Regulatory Assets

17 Arizona-American shareholders have been shouldering these expenses in the interim following  
18 American Water's acquisition of the affected districts from Citizens in 2002. The mismatch is in  
19 the direction opposite than Staff testifies. Due to a number of factors, especially the three-year  
20 rate moratorium imposed as a condition of RWE's acquisition of Arizona-American's parent  
21 company, actual amortizations due to the passage of time have fallen far short of what Arizona-  
22 American bargained for.

23 The following table compares the actual cumulative increase to rate base versus what was  
24 contemplated in 2001:

25 **Increases to Rate Base Resulting From Amortizing**  
26 **Imputed Regulatory Advances for Arizona American Water**

|         | Commission Approved   | Test Year Amounts Actually |
|---------|-----------------------|----------------------------|
|         | Amortization Schedule | Reflected in Rate Base     |
| 29 2002 | \$16,769,441          | \$0                        |
| 30 2003 | \$32,209,659          | \$0                        |
| 31 2004 | \$51,649,878          | \$1,209,090                |
| 32 2005 | \$69,090,096          | \$42,182,344               |
| 33 2006 | \$86,350,315          | 43,961,770                 |
| 34 2007 | \$103,970,533         | TBD in this case           |

35 RUCO supports Arizona-American's request concerning imputed regulatory advances.

36 Cost of Capital

37 Short-term debt should not be included in Arizona-American's capital structure. Arizona-  
38 American's short-term debt has increased due to the on-going construction of the White Tanks

1 project. This large project is in CWIP and is being financed in the interim by short-term debt. It  
2 is inappropriate to include this short term debt in our permanent capital structure, when it is  
3 financing CWIP. RUCO was earlier persuaded by Arizona-American's rationale on this point  
4 and continues to remain in agreement in this case.

5 Long-term interest rates have been dramatically increasing. Arizona-American's affiliate  
6 American Water Capital Corporation ("AWCC") issues long-term debt for Arizona-American  
7 and other regulated affiliates. Just in recent months, AWCC's debt cost has risen by  
8 approximately 350 basis points. The interest rate is 10.0%, compared to just 6.5% not long ago.

9 Water Use Data

10 It would be unwise for the Commission to order Staff to automatically declare insufficiency and  
11 suspend the time clock if Arizona-American submits inaccurate water use data in the next rate  
12 case. This would be an overly harsh penalty on Arizona-American. These water-use errors had  
13 no impact on the original cost-of-service study or the original rate design. Staff already has  
14 adequate authority in the sufficiency process and does not need an automatic requirement which  
15 may not be appropriate, given the facts in the next rate case.

16 Rate Design

17 Paradise Valley's residential rate design should be expanded from three to five rate blocks. If  
18 the price of a new fourth rate block is higher, it provides an incentive for those customers with  
19 one-acre lots to conserve to levels below 65,000 gallons per month. Paradise Valley residential  
20 customers consuming more than 80,000 gallons per month will receive a substantial rate  
21 reduction upon conclusion of this case.

22 Water Loss

23 Arizona-American should not be required to reduce its water loss percentage to below 10 percent  
24 in several districts as proposed by Staff. Rather, it would make much more sense to require  
25 Arizona-American and Staff to work cooperatively together to derive a plan to further reduce  
26 water loss, with the cost of the plan made transparent to all. If the consequence of somewhat  
27 higher water losses for a district would be no rate relief, Arizona-American could be forced to  
28 cancel or defer other worthwhile capital projects in favor of addressing water losses.

29 Mohave Hook-Up Fee Compliance

30 Arizona-American is in compliance concerning the Mohave wastewater hook-up fee. However,  
31 Arizona-American does not oppose the new future compliance recommended by Ms. Hains.

32 REBUTTAL OF RUCO

33 Rate Case Expense

34 Arizona-American's revised request for rate case expenses totals \$456,275 which is down from  
35 \$612,000 requested in the original application. This is very close to RUCO's recommended  
36 level.

37 White Tanks Hook-Up Fee Extension

38 RUCO simultaneously recommends denial of the requested hook-up fee extension, while  
39 recommending that Arizona-American stay the course and rely only on hook-up fees and never  
40 put the costs for the initial phase of White Tanks in rate base. In light of the real estate  
41 depression which has dramatically eroded hook-up fee proceeds, the consequence of these

1 combined RUCO recommendations, if adopted, would be to permanently deny Arizona-  
2 American cost recovery of White Tanks. Arizona-American's requested extension to 2020 is  
3 reasonable and probably will need to be extended further.

4 REBUTTAL OF MAGRUDER

5 Rate Case Expense

6 Arizona-American accepts Mr. Magruder's recommendation to eliminate any expense for  
7 witness training.

8 Arsenic Cost Recovery Mechanism ("ACRM")

9 The Commission should reject Mr. Magruder's proposal to not allow an ACRM for the Tubac  
10 Water District. The ACRM concept was created precisely because arsenic facility costs occur  
11 after the test year end in a rate case and yet the costs – when incurred – are very significant and  
12 due to a federal mandate. The Commission has previously approved ACRMs for four other  
13 Arizona-American water districts. In each case, once the ACRMs were approved, construction  
14 commenced. By design, this occurred after the test year. Then, after the treatment facility  
15 entered service, Arizona-American made an ACRM Step I filing, including all the required  
16 schedules, exhibits and project invoices. The procedure Arizona-America is following for Tubac  
17 Water is completely consistent with this past practice and that of other water utilities, such as  
18 Arizona Water.

19 Third Pricing Block for Tubac

20 The Commission should reject Mr. Magruder's proposal to set a very expensive third pricing  
21 block for Tubac Water. Higher use water consumers in Tubac are price sensitive and drill  
22 private wells to fully or partially bypass our system. Since most of our costs are fixed costs, such  
23 dramatic conservation only serves to raise rates later for the remaining customers.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
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IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

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DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
CHRISTOPHER C. BULS  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

1 **REBUTTAL TESTIMONY**

2 Christopher C. Buls testifies as follows:

3 **To Reduce Future Rate Impacts, Arizona-American Proposed Using Hook-Up Fees to**  
4 **Finance the Plant**

5 Arizona-American carefully considered a number of factors in making this decision. First,  
6 Company leadership realized that this plant needed to be built sooner rather than later, as it  
7 improves the overall groundwater situation and provides a benefit to our existing customers. A  
8 second consideration was the high cost of constructing a "Greenfield" facility such as the White  
9 Tanks Plant. \$60 Million while the second increment of 6.5 MGD is expected to cost less than  
10 \$5 Million. Another consideration was an attempt by Arizona-American to minimize the rate  
11 impact of this project on our current customers. Finally, because of the dire financial condition  
12 of Arizona-American, Arizona-American needed to minimize the negative financial impacts  
13 associated with a project of this size.

14 The use of hookup fees would potentially reduce the financial impacts to current customer  
15 without further exacerbating the already difficult financial situation Arizona-American was in.

16 **Hook-Up Fee Receipts Have Declined Precipitously**

17 Our projection of these fees has dropped precipitously. In Case W-01303A-05-0718, which was  
18 filed roughly two years ago, Arizona-American projected that the entire \$60 million plant could  
19 be paid for by hook-up fees by the end of 2013. Current projections now show that we will only  
20 collect about \$8 million over that same time frame.

21 The decline in cash flow from the hook-up fees will impact our ability to rely on hook-up fees in  
22 numerous ways. To deal with this state of events, Arizona-American proposed including \$25  
23 million of CWIP in rate base.

24 **The Decline in Hook-Up Fees Will Seriously Hurt Arizona-American**

25 Without some mitigation, the impact of this decline will have serious consequences for Arizona-  
26 American. An immediate impact is that Arizona-American is experiencing a sharp increase in  
27 short-term debt levels. Another impact is that the cost of the plant which includes AFUDC, is  
28 growing at a faster pace than the original projections. Additionally, shortly after the plant goes  
29 in service in late 2009, Arizona-American will immediately begin to suffer severe, negative  
30 impacts on net income.

31 The driver of the growth in total costs lies in the calculation of the AFUDC. AFUDC for this  
32 project is calculated on a "net" basis meaning the base for the calculation is the construction  
33 costs to date less the applicable hook-up fees. Because the hook-up fees have been and will be  
34 much lower than originally estimated, the "net" amount is greater, and consequently the AFUDC  
35 is higher. This creates a situation where the amounts available to pay down the plant are lower,  
36 while the amount to pay down is growing.

37 Authorizing \$25 million of CWIP in rate base will mitigate the problem, but will not provide a  
38 full solution. It will however allow for some additional time and, most importantly, slow down  
39 the growth of the balance related to the plant. Without placing CWIP into rate base Arizona-  
40 American will be forced to try to carry a large asset with no cost recovery. From a GAAP

1 perspective, even with the existing authorization, Arizona-American will still suffer from  
2 diminished earnings in the near term as hook-up fees are inadequate.

3 Excluding all O&M, depreciation and other associated expenses the required return on the \$60  
4 million plant would be approximately \$8.3 million annually. This compares to expected hook-up  
5 fees of roughly \$1 million per year for the first two years of operation. This difference, less  
6 taxes, represents the lost net income or financial harm to Arizona-American.

7 Based on the current assumptions it is doubtful this project will ever get paid off. By 2029 the  
8 net unfunded balance is \$58 million, roughly equal to the total of the original 2009 construction  
9 cost. Over that time-period, Arizona-American would have recovered a total of \$68 million in  
10 post in-service AFUDC, with out paying down a single dollar of the White Tanks Plant.

#### 11 **Other Options Could Mitigate the Financial Harm**

12 Putting \$25 million of CWIP into rate base is an important first step. The revenue requirement  
13 effect of including \$25 million of White Tanks construction costs in rate base assuming Arizona-  
14 American's requested rate of return of 8.4% is approximately \$3.476 million per year. If this  
15 were recovered via a customer charge to the Agua Fria district customers, the resulting charge  
16 would be \$9.09 per month based on the average test year customer count of 31,882.

17 As an alternative, it would be acceptable to the Company to set the revenue requirement equal to  
18 that of putting CWIP in rate base using the White Tanks Plant Surcharge Mechanism that Mr.  
19 Broderick proposed in his Direct Testimony. This would be a temporary surcharge that would be  
20 in place only until completion of the next rate case.

21 Arizona-American would consider a variety of helpful options in addition to or alternatively to  
22 avoid further financial harm to Arizona-American. Creating some form of renewable-water-  
23 supply surcharge that would be added to customer bills is one such option. If the surcharge was  
24 expanded to cover all of our Valley water districts still on groundwater, that would lessen the  
25 amount of the surcharge.

#### 26 **Arizona-American Could Be Forced to Mothball or Sell the White Tanks Plant**

27 The White Tanks Plant is very large relative to Arizona-American's total investment. Arizona-  
28 American cannot carry the cost of this project on hook-up fees alone. If the results of this rate  
29 case are disappointing, Arizona-American must consider mothballing or selling the facility.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
BRADLEY J. COLE  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

1 DIRECT TESTIMONY

2 WATER DISTRICT DESCRIPTIONS

3 Mr. Cole first describes the service areas and facilities for each of Arizona-American's six water  
4 districts that are included in this case: Agua Fria Water; Havasu Water; Mohave Water; Paradise  
5 Valley Water; Sun City West Water and Tubac Water.

6 WHITE TANKS DEFERRED O&M RECOVERY

7 Mr. Cole supports Mr. Broderick's request for a mechanism to recover deferred first-year O&M  
8 costs for the White Tanks Regional Treatment Facility. Exhibit BJC-1 estimates these costs.

9 TUBAC ARSENIC-TREATMENT FACILITY

10 Mr. Cole discusses the need for an arsenic-treatment facility for the Tubac Water District.  
11 Exhibit BJC-2 is a copy of a January 18, 2008 letter from the U.S. Environmental Protection  
12 Agency, which denied Arizona-American's request for an exemption from the new federal  
13 Arsenic standard.

14 STORAGE-TANK MAINTENANCE PRO PRAM

15 Mr. Cole discusses Arizona-American's new storage-tank maintenance program and supports  
16 Ms. Hubbard's request to fund this program. Exhibit BJC-3 provides the cost and schedule of all  
17 tanks scheduled for maintenance in the districts.

18 CHEMICALS

19 Mr. Cole explains why chemical expenses have increased in recent years. The first reason is that  
20 chemical costs have risen from year-to-year, typically tracking the Consumer Price Index.  
21 Second, we are now operating arsenic-treatment facilities located in the Agua Fria, Havasu, Sun  
22 City West and Paradise Valley water districts. New chemicals used in these facilities include  
23 Ferric Chloride, Polymer, Sodium Chloride, Sodium Hydroxide, Sodium Hypochlorite, and  
24 Sulfuric Acid. The third and final reason is growth, particularly in the Agua Fria and Mohave  
25 Water Districts.

26 SERVICE CHARGES

27 Mr. Cole explains why Arizona-American proposes to increase various service charges:

- 28 1. For the Agua Fria, Havasu, Mohave, Paradise Valley, Sun City West water districts,  
29 Arizona-American proposes to increase the service and meter-installation fees for meters  
30 1 1/2-inch or smaller from \$660 to the amounts consistent with Staffs recommendations;
- 31 2. Revise its service and meter-installation fees for meter size 2-inch or larger from \$660 to  
32 the actual cost of installing the service line and meters (Exhibit BJC-4 details the cost  
33 estimates for installing service lines and meter);
- 34 3. Increase its meter-test charge to \$81 per meter; and
- 35 4. Standardize its after-hours reconnect charge in each district at \$90.00.

36 MOHAVE WASTEWATER

37 Mr. Cole describes the service areas and facilities for Arizona-American's Mohave Wastewater

1 District

2 SUN CITY WATER - FIRE HYDRANT INSPECTION

3 Mr. Cole supports Arizona-American's request to terminate the annual fire-hydrant inspection  
4 compliance report requirement for the Sun City Water District.

5 REBUTTAL TESTIMONY

6 Arizona-American will be hiring a Production Supervisor and four Plant Operators over the next  
7 six months to Staff the White Tanks Water Treatment Plant ("White Tanks Plant")

8 Once the White Tanks Plant enters service, Arizona-American's power savings for groundwater  
9 production are estimated at \$791,765. Estimated chemical-treatment savings are \$30,138.

10 Arizona-American accepts Staff's Recommendations for the Service Line and Meter Installation  
11 fees.

12

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
IAN C. CROOKS  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

REJOINDER TESTIMONY

Mr. Crooks testifies as follows:

Mr. Crooks answers the eleven questions posed by Mr. Olea in his rebuttal testimony concerning Arizona-American's proposal to amend its Water Facilities Hook-Up Fee WHU-1, for its Agua Fria Water District. The responses to questions 5, 9 and 10 discuss the core issues. Generally, most of the other changes in Arizona-American's proposed tariff were to conform the existing tariff to the Off-Site Water Hook-up Fee tariff ("ACC HUF Template"), dated January 8, 2009, as posted on the Commission's website.

Arizona-American believes the term "Common Facilities" is more descriptive and less subject to confusion or misinterpretation than is "Off-Site Facilities." The physical location of Water Facilities constructed and/or funded by the HUF does not necessarily determine whether the Facilities are for the exclusive benefit of a particular development or are for the benefit of multiple developments.

Arizona-American is proposing to split within a single tariff the current unified hook-up fee into two components, the original 2004 HUF amount as "Component A" and the incremental increase in the current 2007 HUF as "Component B". Component A will continue to be used to pay for Arizona-American's existing and future investment in Common Facilities and will be eligible for offset against Applicant built Common Facilities. Component B will be solely used to pay for Arizona-American's White Tanks Surface Water Treatment Facility ("WTSWTF") investment and will not be eligible for offset against Applicant built Common Facilities. If this change is lot made, the cash receipts to Arizona-American needed to pay for the WTSWTF will be delayed out many years.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
JOSEPH E. GROSS  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

DIRECT TESTIMONY

Joseph E. Gross testifies as follows:

Arizona-American has three major capital projects under way for which it seeks to recover associated post-test-year investment:

1. White Tanks Regional Water Treatment Plant. The White Tanks Regional Water Treatment Plant ("White Tanks Plant"), currently under construction, is a 13.5 MGD surface water treatment facility to treat CAP water for distribution to customers in the Agua Fria Water District. Construction of the White Tanks Plant began in November 2007. As of March 31, 2008, total White Tanks Plant investment, including preconstruction costs, was \$13 million. By September 30, 2008, the total investment should total \$31 million. The overall project budget is estimated at \$61.5 million.
2. Mohave Wastewater Treatment Plant Expansion. In September 2007, Arizona-American began expanding the capacity of the Wishing Well Wastewater Treatment Plant ("Mohave Treatment Plant") that treats wastewater for Mohave Wastewater District customers. Based on growth projections, demands will approach the 250,000 gpd design capacity of the Mohave Treatment Plant in 2008. The expansion of the Mohave Treatment Plant will add 250,000-gallons-per-day in new treatment capacity, allowing service for up to 1,500 additional service connections. Arizona-American expects to place the Mohave Treatment Plant Expansion in service in July 2008. As of the end of the test year, Arizona-American had invested \$1.5 million in the Mohave Treatment Plant Expansion. The total investment is expected to be \$4.0 million.
3. Paradise Valley Fire Flow Project, Phase 3. In its Paradise Valley Water District, Arizona-American is in the midst of a multi-year, phased, program to upgrade main capacity, add fire hydrants, increase water storage and pumping capacity. Arizona-American expects to complete Phase 3 of its fire-flow projects by September 30, 2008, at a cost of \$3.6 million. In 2007, we began constructing one-half mile of 24" water main in McDonald Drive. Phase 3 construction will continue in 2008, with one-half mile of 16" water main in Lincoln Drive, and one-third mile of 8" water main in Tatum Boulevard.

Arizona-American also has four smaller projects underway, which should be completed in time for the Commission Staffs engineering report.

1. Well 12 Replacement (Paradise Valley Water). The existing Well 12 is being replaced due to a failure in its casing, which restricted its production to approximately 50% of the original 2200 gallons per minute. The replacement well will allow the facility to regain its original production capacity, and should be completed by December 2008, at a cost of \$1.93 million.
2. Big Bend Acres Tank (Mohave Water). This storage tank is being built to replace an old existing tank which has experienced severe structural problems and has inadequate capacity. The new 250,000 gallon tank should be completed by August 31, 2008, at a cost of \$611,000.

1 3. Sierra Montana Tank (Aqua Fria Water). This 2.2 million gallon storage tank is being  
2 built to increase storage capacity at Arizona-American's Water Plant 8. The tank should  
3 be completed in August 2008, at a cost of \$2.05 million.

4 4. Distribution System Improvements, Phase 2 (Aqua Fria Water). This consists of essential  
5 projects needed for groundwater distribution and storage improvements before the 2010  
6 completion of the White Tanks Plant. The components of this project involve connecting  
7 an MWD well to the reservoir at Water Plant 8, adding a water line to serve the Cool  
8 Well subdivision, and eliminating a pipeline bottleneck at Bell and Reems Roads. The  
9 three components of this project should be completed in October 2008, at a total cost of  
10 \$1.19 million.

11 Tubac Arsenic Treatment Facility.

12 Arizona-American is also planning to build an arsenic-treatment facility for its Tubac Water  
13 District to comply with the new arsenic mcl. The EPA denied our request for a three-year  
14 exemption. The current plan is to partner with the developer of Tubac Marketplace, a  
15 commercial project in the downtown area. The partnership reduces the expected cost of the  
16 facilities by approximately \$1 million. The developer will provide the required site, storage, and  
17 pumping capacity; and Arizona-American will provide the water supply and arsenic-treatment  
18 facilities. The present cost estimate is \$2.3 million. Design will begin this summer (2008), with  
19 construction to begin in spring 2009 and be completed approximately one year later.

20 Mohave County Comprehensive Planning Study. This study lays out a five-year plan for  
21 prioritized improvements required to provide adequate water supply, storage, and pumping  
22 capacity within the Bullhead City and Havasu service areas. In Bullhead City, site procurement  
23 is underway this year for one well, which should be operational in 2009. Also, the Big Bend  
24 Acres 250,000-gallon storage tank will be completed in August 2008. Future projects include  
25 additional wells, storage, and an interconnection with Bermuda Water. In the Havasu Water  
26 District, an interconnection with the City of Lake Havasu will be completed this year. Future  
27 projects include upgrades to Well No. 9, additional storage facilities, and SCADA  
28 improvements.

29 Aqua Fria Water Supplies. Because of the construction of the White Tanks Plant, developers are  
30 now only being required to supply water to satisfy average-day demand for the development,  
31 rather than maximum-day demand. New groundwater supplies will still be required to meet  
32 customer demands during the annual scheduled outage of the Beardsley Canal, scheduled  
33 outages of the White Tanks Plant, and any unscheduled outages of the Canal, Plant, or associated  
34 facilities. There is no longer any need for the 3.5-mile contingency pipeline.

35 Aqua Fria District Projected Growth. Arizona-American previously forecasted 4200 new hook-  
36 ups in 2008. Because of the recent real-estate slowdown, the Company now expects many fewer  
37 Hook-ups in 2008, with the downward trend expected to continue. Further, many existing  
38 projects are grandfathered, so these customers will not be responsible for the increased hook-up  
39 fee. A forecast of new customers that will actually be subject to the increased hook-up fees  
40 follows:

| Year      | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 |
|-----------|------|------|------|------|------|------|
| Customers | 134  | 615  | 764  | 1030 | 1031 | 2180 |

1 Therefore the proceeds generated by hook-up fees to fund the White Tanks Plant will also be  
2 much less.

3 **REBUTTAL TESTIMONY**

4 Arizona-American's White Tanks Water Treatment has been under construction for over one  
5 year and is on schedule to be in service by December 2009, at a total project cost of  
6 approximately \$62 million. Because of the current economy, customer growth has continued to  
7 slow. Arizona-American now projects the following number of additional customers will be  
8 subject to the Agua Fria Water District Hook-Up fee:  
9

| 10 | Year      | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 |
|----|-----------|------|------|------|------|------|------|
| 11 | Customers | 48   | 98   | 154  | 293  | 545  | 645  |

12  
13 Staff witness Dorothy Hains proposes disallowance of one adsorber vessel at each of three of  
14 Arizona-American's arsenic-treatment plants, Agua Fria Water Plant No. 5, Havasu Water Plant  
15 No. 4, and Sun City West Water Plant No. 2. This would be improper. Without these adsorber  
16 vessels, the plants could not treat the full output of the associated wells, which would jeopardize  
17 the water supplies in these districts.

18  
19 The 2.2 million gallon Sierra Montana Reservoir was placed in service as post-test-year plant on  
20 December 8, 2008, at a cost of \$1,794,728.

21  
22 The Agua Fria Phase 2 distribution system improvements project was placed into service as post-  
23 test-year plant on October 6, 2008 at a cost of \$1,389,895.

24  
25 The .25 million gallon Big Bend Acres Reservoir was placed into service on November 26, 2008,  
26 at a cost of \$643,127.

27  
28 Arizona-American is currently designing an arsenic treatment facility at Water Plant No. 5,  
29 which should be in service by summer 2010. This facility is required to comply with the EPA  
30 revised arsenic standards of 10 parts per billion, issued in January 2001. Mr. Magruder's  
31 interpretation of the EPA standards is incorrect. Arizona-American is no longer planning on  
32 receiving developer funds toward the project. The arsenic facility project has been reduced in  
33 scope and designed to fit within the existing walls of Tubac Water Plant #5.

34  
35 At the Mohave Wastewater Wishing Well Treatment Plant, new plant construction entered  
36 service in summer 2008 at a cost of \$4,276,039. A portion of the new construction was to  
37 replace or upgrade existing plant components, with a portion designed to increase plant capacity.  
38 The decision to increase the plant capacity was based on daily flows exceeding existing capacity  
39 and significant requests for capacity assurance letters. These additional requests far exceeded  
40 existing capacity. The decision was also consistent with ADEQ and Commission standards. The  
41 decision to upgrade and expand the Wishing Well Plant was prudent.

42  
43 Phase 3a of the Paradise Valley Fire Flow project was placed in service on August 14, 2008 at a  
44 cost of \$1,502,882. This project installed a 24" waterline in McDonald Drive from Miller Road  
45 to Scottsdale Road. Charges for planning and design remain for the suspended Phase 3b of that  
46 project in the amount of \$514,223.23. Phase 3b was to construct a 16" waterline in Lincoln  
47 Drive and an 8" waterline in Tatum Boulevard, but was cancelled just prior to construction.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
LINDA J. GUTOWSKI  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
DATED MARCH 17, 2009**

DIRECT TESTIMONY

RATE BASE

Ms. Gutowski sponsors rate base Exhibits B-1 through B-5. Rate base for each district follows:

**Table 1 - Summary of Rate Base**

| District                   | OCRB                 |
|----------------------------|----------------------|
| Agua Fria Water            | \$96,976,395         |
| Havasu Water               | \$4,221,474          |
| Mohave Water               | \$12,041,310         |
| Paradise Valley            | \$40,864,986         |
| Sun City West Water        | \$37,901,085         |
| Tubac Water                | \$1,527,454          |
| Mohave Wastewater          | \$4,740,149          |
| <b>Total All Districts</b> | <b>\$198,272,853</b> |

Common Rate-Base Adjustments

Adjustment LJG-3 reallocates the UPIS balance from the Corporate District into the proper District, based on plant coding:

Adjustment LJG-4 allocates the Common, or Corporate, Plant and Accumulated Depreciation to each of the districts:

Adjustment LJG-5 is the opposite side of Adjustment LJG-3. It reverses the December 2007 Journal Entry and removes \$753,965 from the Corporate Plant accounts.

Adjustment LJG-6 decreases Advances and/or Contributions in Aid of Construction for dollars associated with projects that are still in Construction Work in Progress ("CWIP").

Mr. Broderick has three adjustments on Schedule B-2. Adjustment TMB-7 is reserved for the Imputed Regulatory Advances in Aid of Construction. Adjustment TMB-8 is reserved for the Imputed Regulatory Contributions in Aid of Construction. Adjustment TMB-9 is reserved to remove the Acquisition Adjustment from the Citizens Utilities purchase.

Agua Fria Water Rate-Base Adjustments

Adjustment LJG-1 removes \$76,503 from UPIS and \$1 9,453 from Accumulated Depreciation.

Adjustment LJG-2 removes Excess Hook-Up Fee Contribution for the White Tanks Project.

Adjustment LJG-10 adds \$25,000,000 of White Tanks Project Costs to Rate Base.

Adjustment LJG-11 adds Post-Test-Year Additions of \$3,214,033.

Havasu Water Rate-Base Adjustments

Adjustment LJG-1, corrects Accumulated Depreciation for Havasu Water District by decreasing it \$20,809.

Adjustment LJG-2 removes \$77,319 of Plant and reduces Accumulated Depreciation by \$29,047 for the Plant that the Commission found to be not useful in Decision 67093.

Adjustment LJG-10 adds \$94,996 to rate base for deferred ACRM O&M costs.

1           Mohave Water Rate-Base Adjustments

2 Adjustment LJG-1, adjusts the under-collection in the Accumulated Depreciation for rate-  
3 making purposes. Adjustment LJG-2 removes (\$4,915) from plant as a proposed retirement to go  
4 along with a Post-Test-Year addition recommended by Staff in the last rate case.

5 Adjustment LJG-10 includes estimated project costs of \$610,732 for the Mohave Water District's  
6 Big Bend Acres 0.25MG Reservoir.

7           Paradise Valley Water Rate-Base Adjustments

8 Adjustments LJG-1 and LJG-2 correct accumulated depreciation balances from the last rate case  
9 and the calculation going forward.

10 Adjustment LJG-10 corrects an error in plant-account assignment.

11 Adjustment LJG-11 adds \$1,899,267 to UPIS associated with well replacements and  
12 rehabilitations.

13 Adjustment LJG-12 corrects a refund of High Block Surcharge monies.

14           Sun City West Water Rate-Base Adjustments

15 Adjustment LJG-1 reduces Accumulated Depreciation for over-expensing.

16           Tubac Water Rate-Base Adjustments

17 Adjustment LJG-1 increases Accumulated Depreciation for an under-collection that has been  
18 building up since the last rate case, Decision No. 67093.

19 Adjustment LJG-2 decreases UPIS by \$1,624 for Plant Not Used.

20           Mohave Wastewater Rate-Base Adjustments

21 Adjustment LJG-1 reduced accumulated depreciation by \$225,743.

22 Adjustment LJG-10 adds \$3,932,080 to UPIS for the Wishing-Well Wastewater Treatment Plant  
23 project.

24           Schedule B-5

25 Ms. Gutowski sponsors the Materials & Supplies and Prepayment portions of the working capital  
26 calculation.

27 INCOME STATEMENT ADJUSTMENTS

28 Ms Gutowski sponsors the following income-statement adjustments:

29 Adjustment LJG-1 removes unbilled revenues for each district.

30 Adjustment LJG-2 Blank

31 Adjustment LJG-3 provides various types of individual adjustments for the districts.

32 Adjustment WG-4 (Agua Fria Water, Havasu Water, Paradise Valley, and Sun City West Water)  
33 moves the ACRM revenue collected during the test year from Other Revenue to Water Revenue.

34 Other adjustments were made for Paradise Valley Water and Mohave Wastewater.

35 Adjustment LJG-5 annualizes customer revenues for each district.

36 E SCHEDULES

1 Ms. Gutowski prepared Schedule E-1, the Comparative Balance Sheet schedule for each district,  
2 and Schedule E-5, the Detail of Plant in Service schedule for each district.

3 H SCHEDULES

4 Ms. Gutowski sponsors the Present Rate portion of the H Schedules.

5 REBUTTAL TESTIMONY

6 RATE BASE – UTILITY PLANT IN SERVICE

7 Agua Fria Water District

8 In Rebuttal Adjustment LJG-1R, Arizona-American is reducing the cost of the Sierra Montana  
9 2.2 MG Reservoir from an estimated amount to the actual cost. This adjustment reduces Plant in  
10 Service by \$252,470.

11 Staff Rate-Base Adjustment No.1 would inappropriately disallow any recognition of the Rancho  
12 Cabrillo Subdivision On-Site Costs. These costs are currently estimated at \$1,189,832. The  
13 project is in service, and Ms. Hains did not make any determination that the project is not used  
14 and useful. Therefore, the costs should be included in rate base.

15 Arizona-American accepts Staff Rate-Base Adjustment No.5 to include \$1,167,268 in post-test-  
16 year additions for distribution system improvements.

17 Staff Rate-Base Adjustment No.5 would inappropriately exclude \$2,046,765 in post-test-year  
18 additions for the Sierra Montana 2.2 Mg Reservoir. The project was placed in Utility Plant in  
19 Service in December 2008 at a cost of \$1,794,295. .

20 Staff Rate-Base Adjustment No.6 would inappropriately exclude \$25,000,000 in White Tanks  
21 Project CWIP. RUCO Rate-Base Adjustment No.7 is the same as Staff Rate Base Adjustment  
22 No. 6 and should also be rejected.

23 Arizona-American accepts RUCO Rate-Base Adjustment No.4 to increase rate base by \$18,581  
24 for two projects that are actually in the Agua Fria water district, but were mistakenly included in  
25 the Sun City West Water District.

26 Havasu Water District

27 Adjustment, LJG-2R is to move the Gateway water and wastewater plant from the Havasu Water  
28 District and put it properly into the Mohave Water District and into the Mohave Wastewater  
29 District. Gateway is geographically located half way between our Havasu District and our  
30 Mohave District, but is in our Mohave Water And Wastewater CC&N areas. The decrease to  
31 plant in service in Havasu is \$814,761 and there is a companion decrease to accumulated  
32 depreciation discussed below.

33 Mohave Water District

34 There are two rate base adjustments for the Mohave Water District. Rebuttal Adjustment LJG-  
35 1R updates the estimated cost for the 0.25 mg Big Bend Acres Reservoir to actual costs of  
36 \$643,127. This increases plant by \$32,395. Rebuttal Adjustment LJG-2R adds the Gateway  
37 Water Plant to the Mohave Water District in the amount of \$721,333.

38 Staff Rate-Base Adjustment No.1 would inappropriately disallow \$1,539,768 for three projects  
39 lacking supporting invoices. All three projects are in service and the plants are used and useful.

1 All of the projects were built in accordance with other commission-approved line extension  
2 agreements. It would be punitive not to include a million-dollar project in rate base, just because  
3 we are having difficulty getting final paperwork.

4 Staff Rate Base Adjustment No. 5 would inappropriately disallow all of the estimated costs for  
5 the Big Bend Acres Reservoir in the amount of \$610,732. The project was completed, and used  
6 and useful as of November 26, 2008.

7 Paradise Valley Water District

8 Arizona-American accepts Staff Rate-Base Adjustment No.1 to decrease plant in service by  
9 \$180,916 to account for plant retirements. Arizona-American retired tanks and pumps as a result  
10 of building the arsenic treatment plant in the Paradise Valley Water District. However, these  
11 retirements were incorrectly booked in 2007 to our sun city and Sun City West Water Districts

12 RUCO Rate-Base Adjustment No.5 would inappropriately decrease plant in service to account  
13 for plant retirements. The adjustment is for the same retirement-errors that Staff identified, but is  
14 not for the full amount.

15 Arizona-American accepts RUCO Rate-Base Adjustment No.3 to remove \$2,109,032 of post test  
16 year plant, the estimated cost of the rehabilitation of Well No. 12. However, the correct amount  
17 is \$1,775,026.

18 Sun City West Water District

19 Arizona-American accepts RUCO Rate-Base Adjustment No.3 to increase plant in service by  
20 \$76,672, to adjust for plant retirements that should have been made in the Paradise Valley Water  
21 District.

22 Arizona-American rejects Staff Rate-Base Adjustment No.1. This is a similar adjustment to  
23 RUCO RB-3. RUCO's adjustment is for the correct amount, as Staff did not retire \$6,672 and  
24 made no adjustment to accumulated depreciation.

25 Arizona-American accepts RUCO Rate-Base Adjustment No.4 to decrease plant in service by  
26 \$18,581 to adjust for two projects that belong in Agua Fria Water District instead of the Sun City  
27 West Water District.

28 Tubac Water District

29 There are no rate base adjustments for the Tubac Water District.

30 Mohave Wastewater District

31 Arizona-American makes three rebuttal adjustments for the Mohave Wastewater District. LJG-  
32 1R lowers accumulated depreciation for a change in depreciation rates approved in the previous  
33 rate case. LJG-2R for \$94,978 adjusts for the Gateway Wastewater Plant being moved from the  
34 Havasu Water District and being placed in the Mohave Wastewater District. LJG-3R adds  
35 \$343,959 to plant in service for the difference between the actual cost of the Wishing Well  
36 Wastewater Treatment Plant expansion and the estimated cost used in my direct testimony.

37 Staff Rate-Base Adjustment No.1 would inappropriately decrease plant in service by \$306,362  
38 by disallowing two projects that do not have invoices. It would be punitive to disallow including  
39 plant in rate base that is in service, just because all the final invoices have not been collected.

1 Staff Rate-Base Adjustment No.5 would inappropriately decrease plant in service by \$3,932,808  
2 by disallowing all costs associated with the upgrade and expansion of the Wishing Well  
3 Treatment Plant. Mr. Gross discusses why this would be inappropriate.

4 RUCO Rate-Base Adjustment No.4 would inappropriately decrease plant in service by  
5 \$1,966,040 by deferring its estimate (50%) of the costs of the Wishing Well Treatment Plant.  
6 Mr. Gross discusses why this would be inappropriate.

7 RATE BASE – ACCUMULATED DEPRECIATION

8 All Districts

9 RUCO Rate Base Adjustment No. 1, RUCO inappropriately recomputed depreciation expense  
10 for all districts claiming that the only acceptable methods of depreciation are mid-year or mid-  
11 month. RUCO is incorrect. Arizona-American changed from the mid-year method to the end of  
12 month method as of January 2003. The Company's depreciation methodology is accepted by our  
13 outside auditors and complies with all Sarbanes-Oxley requirements. All three methods give the  
14 same results over the life of the asset. Arizona-American's case is based on the actual  
15 depreciation expenses booked and approved by the auditors. RUCO would improperly substitute  
16 a fictional depreciation expense.

17 Agua Fria Water District

18 Staff Rate Base Adjustment No. 1 would inappropriately decrease accumulated depreciation in  
19 the amount of \$7,532. This appears to be the result of an arithmetical error.

20 Havasu Water District

21 Arizona-American made two adjustments. Adjustment LJG-1R decreases accumulated  
22 depreciation by \$6,540 to reflect the depreciation rates that were effective on June 30, 2004 in  
23 Decision no. 67093. Adjustment, LJG-2R, decreases accumulated depreciation by \$14,000 with  
24 the removal of the Gateway Plant discussed above.

25 RUCO's Rate-Base Adjustment No.1 is not entirely accurate. It is appropriate to adjust  
26 depreciation rates since June 30, 2004, but RUCO inappropriately uses its half-month  
27 convention.

28 Mohave Water District

29 Rate Base Adjustment LJG-1R and LJG-2r increases accumulated depreciation to adjust for the  
30 Gateway Water Facilities in the amount of \$45,790.

31 Staff Rate Base Adjustment No. 1 would inappropriately remove \$26,559 from accumulated  
32 depreciation. This adjustment corresponds to the improper rate-base reduction for three projects,  
33 which discussed above.

34 RUCO's Rate-Base Adjustment No.1 would inappropriately adjust accumulated depreciation.  
35 The adjustment relies on RUCO's mid-month convention, which is improper. Second, RUCO  
36 improperly used several Havasu Water District depreciation rates instead of the currently  
37 approved rates for Mohave Water District.

38 Paradise Valley Water District

1 Arizona-American accepts Staff Rate Base Adjustment No. 1 to reduce accumulated  
2 depreciation. This adjustment corresponds to the rate-base adjustment for plant retirements,  
3 previously discussed.

4 Arizona-American accepts RUCO's Rate-Base Adjustment No.1 to adjust accumulated  
5 depreciation. The Company made a math error in decreasing Paradise Valley's accumulated  
6 depreciation instead of increasing it. The appropriate correction is \$100,554.

7 RUCO's Rate-Base Adjustment No.5 would inappropriately adjust accumulated depreciation for  
8 Paradise Valley wells. RUCO should have included well #17 for \$288,080 and not included well  
9 #12 for \$1,935,000 since the company withdrew the project before computing accumulated  
10 depreciation. RUCO also should not have reduced accumulated depreciation in the post test year  
11 exhibit by a retirement for Well #12 that will not happen until the well project is undertaken  
12 sometime this year.

13 Sun City West Water District

14 RUCO's Rate-Base Adjustment No.1 inappropriately adjusts accumulated depreciation by use of  
15 its half-month convention.

16 Arizona-American accepts RUCO's Rate-Base Adjustment No.3 to adjust accumulated  
17 depreciation to account for two retirements that were booked in Sun City West, but should have  
18 been attributed to Paradise Valley. One minor adjustment is needed to adjust for RUCO's  
19 improper mid-month convention.

20 Arizona-American accepts RUCO's Rate-Base Adjustment No.4 to adjust accumulated  
21 depreciation to account for plant booked to Sun City West, that should have been attributed to  
22 Agua Fria Water. However, RUCO took out accumulated depreciation of \$860 in Sun City West  
23 and added accumulated depreciation to Agua Fria in the amount of \$2,375. These amounts  
24 should both be \$2,446, as the depreciation rates for these items were the same in the two  
25 districts.

26 Tubac Water District

27 RUCO's Rate-Base Adjustment No.1 inappropriately adjusts accumulated depreciation by use of  
28 its half-month convention.

29 Mohave Wastewater District

30 Rate Base Adjustment LJG-1R, calculates accumulate depreciation using correct rates and  
31 provides a decrease of \$17,306.

32 Rate Base Adjustment LJG-2R increases accumulated depreciation by \$7,621 to reflect the  
33 additional depreciation that should have been calculated in Mohave Wastewater to account for  
34 the transfer of the Gateway Wastewater Facilities.

35 RUCO's Rate-Base Adjustment No.1 inappropriately adjusts accumulated depreciation by use of  
36 its half-month convention.

37 RATE BASE – ADVANCES IN AID OF CONSTRUCTION

38 Agua Fria Water District

39 Staff Adjustment No. 1 improperly reduced advances for the Rancho Cabrillo project because it  
40 removed the associated plant from utility plant in service.

1           Mohave Water District

2 RUCO's Rate Base Adjustment No. 2 would inappropriately add back \$291,910 to advances for  
3 plant items that are still in CWIP, rather than in utility plant in service. If plant is not in rate base  
4 to begin with, it is inappropriate to reduce rate base for the amount of advances directly  
5 associated with that plant.

6           Tubac Water District

7 RUCO's Rate Base Adjustment No. 2 would inappropriately add back \$20,266 to advances for  
8 plant items that are still in CWIP, rather than in utility plant in service. If plant is not in rate base  
9 to begin with, it is inappropriate to reduce rate base for the amount of advances directly  
10 associated with that plant.

11           Mohave Wastewater District

12 Staff inappropriately deducted the advances associated with used and useful plant that they  
13 disallowed for having no invoices in the amount of \$306,362.

14 RATE BASE – CONTRIBUTIONS IN AID OF CONSTRUCTION

15           Agua Fria Water District

16 RUCO's Rate Base Adjustment No. 2 would inappropriately add back \$28,019 to contributions  
17 for plant items that are still in CWIP, rather than in utility plant in service. If plant is not in rate  
18 base to begin with, it is inappropriate to reduce rate base for the amount of contributions directly  
19 associated with that plant.

20 Arizona-American accepts RUCO Rate Base Adjustment No. 3 to move amortization of  
21 contributions from Mohave Water to Agua Fria Water.

22           Havasu Water District

23 RUCO's Rate Base Adjustment No. 2 would inappropriately add back \$10,645 to contributions  
24 for plant items that are still in CWIP, rather than in utility plant in service. If plant is not in rate  
25 base to begin with, it is inappropriate to reduce rate base for the amount of contributions directly  
26 associated with that plant.

27           Mohave Water District

28 RUCO's Rate Base Adjustment No. 2 would inappropriately add back \$94,453 to contributions  
29 for plant items that are still in CWIP, rather than in utility plant in service. If plant is not in rate  
30 base to begin with, it is inappropriate to reduce rate base for the amount of contributions directly  
31 associated with that plant.

32 Arizona-American accepts RUCO Rate Base Adjustment No. 3 to move amortization of  
33 contributions from Mohave Water to Agua Fria Water. When the contribution balances were  
34 moved from Mohave Water, the associated amortization of these contributions did not get  
35 moved.

36           Paradise Valley Water District

37 RUCO's Rate Base Adjustment No. 2 would inappropriately add back \$322,588 to contributions  
38 for plant items that are still in CWIP, rather than in utility plant in service. If plant is not in rate  
39 base to begin with, it is inappropriate to reduce rate base for the amount of contributions directly  
40 associated with that plant.

1           Sun City West Water District

2 RUCO's Rate Base Adjustment No. 2 would inappropriately add back \$17,318 to contributions  
3 for plant items that are still in CWIP, rather than in utility plant in service. If plant is not in rate  
4 base to begin with, it is inappropriate to reduce rate base for the amount of contributions directly  
5 associated with that plant.

6           Mohave Wastewater District

7 RUCO's Rate Base Adjustment No. 2 would inappropriately add back \$65,395 to contributions  
8 for plant items that are still in CWIP, rather than in utility plant in service. If plant is not in rate  
9 base to begin with, it is inappropriate to reduce rate base for the amount of contributions directly  
10 associated with that plant.

11 RATE BASE – IMPUTED REGULATORY ADVANCES

12           Agua Fria Water District

13 Staff Rate Base Adjustment No. 3 would inappropriately add back \$2,268,167 to imputed  
14 regulatory advances for the period January 1, 2008 through July 15, 2008. Mr. Broderick  
15 discusses this issue in his rebuttal testimony.

16           Havasu Water District

17 Staff Rate Base Adjustment No. 3 would inappropriately add back \$34,679 to imputed regulatory  
18 advances for the period January 1, 2008 through July 15, 2008. Mr. Broderick discusses this  
19 issue in his rebuttal testimony.

20           Mohave Water District

21 Staff Rate Base Adjustment No. 3 would inappropriately add back \$348,557 to imputed  
22 regulatory advances for the period January 1, 2008 through July 15, 2008. Mr. Broderick  
23 discusses this issue in his rebuttal testimony.

24           Paradise Valley Water District

25 Staff Rate Base Adjustment No. 3 would inappropriately add back \$233,188 to imputed  
26 regulatory advances for the period January 1, 2008 through July 15, 2008. Mr. Broderick  
27 discusses this issue in his rebuttal testimony.

28           Sun City West Water District

29 Staff Rate Base Adjustment No. 3 would inappropriately add back \$1,006,408 to imputed  
30 regulatory advances for the period January 1, 2008 through July 15, 2008. Mr. Broderick  
31 discusses this issue in his rebuttal testimony.

32           Tubac Water District

33 Staff Rate Base Adjustment No. 3 would inappropriately add back \$233,188 to imputed  
34 regulatory advances for the period January 1, 2008 through July 15, 2008. Mr. Broderick  
35 discusses this issue in his rebuttal testimony.

36           Mohave Wastewater District

37 Staff Rate Base Adjustment No. 3 would inappropriately add back \$61,769 to imputed regulatory  
38 advances for the period January 1, 2008 through July 15, 2008. Mr. Broderick discusses this  
39 issue in his rebuttal testimony. Further, this amount should be only \$14,090. Staff appears to  
40 have used the imputed ciac amount from sun city west water.

1 RATE BASE – DEFERRED DEBITS

2 Agua Fria Water District

3 Arizona-American accepts Staff Rate Base Adjustment No. 4 and RUCO Rate Base Adjustment  
4 No. 5 to reduce deferred debits by \$3,321,116 to correct an error in the original filing.

5 Havasu Water District

6 Arizona-American accepts Staff Rate Base Adjustment No. 4 and RUCO Rate Base Adjustment  
7 No. 5 to reduce deferred debits by \$145,701 to correct an error in the original filing.

8 Mohave Water District

9 Arizona-American accepts Staff Rate Base Adjustment No. 4 and RUCO Rate Base Adjustment  
10 No. 5 to reduce deferred debits by \$1,649,972 to correct an error in the original filing.

11 Paradise Valley Water District

12 Arizona-American accepts Staff Rate Base Adjustment No. 4 and RUCO Rate Base Adjustment  
13 No. 5 to reduce deferred debits by \$1,083,637 to correct an error in the original filing.

14 Sun City West Water District

15 Arizona-American accepts Staff Rate Base Adjustment No. 4 and RUCO Rate Base Adjustment  
16 No. 5 to reduce deferred debits by \$892,284 to correct an error in the original filing.

17 Tubac Water District

18 Arizona-American accepts Staff Rate Base Adjustment No. 4 and RUCO Rate Base Adjustment  
19 No. 5 to reduce deferred debits by \$51,122 to correct an error in the original filing.

20 Mohave Wastewater District

21 Arizona-American accepts Staff Rate Base Adjustment No. 4 and RUCO Rate Base Adjustment  
22 No. 5 to reduce deferred debits by \$7,071 to correct an error in the original filing.

23 RATE BASE – CASH WORKING CAPITAL

24 Arizona-American rejects the adjustments proposed by Staff and RUCO for each district. Ms.  
25 Hubbard has revised her lead-lag study. Based on this study, Arizona-American makes the  
26 following adjustments.

27 Agua Fria Water District

28 The correct amount of cash working capital for the Agua Fria Water District is \$ 60,105, a  
29 decrease to the original filing of \$1,349,754.

30 Havasu Water District

31 The correct amount of cash working capital for the Havasu Water District is \$46,992, a decrease  
32 to the original filing of \$55,427.

33 Mohave Water District

34 The correct amount of cash working capital for the Mohave Water District is \$185,707, a  
35 decrease to the original filing of \$181,855.

36 Paradise Valley Water District

37 The correct amount of cash working capital for the Paradise Valley Water District is \$79,326, a  
38 decrease to the original filing of \$469,708.

39 Sun City West Water District

1 The correct amount of cash working capital for the Sun City West Water District is \$77,120, a  
2 decrease to the original filing of \$403,020.

3 Tubac Water District

4 The correct amount of cash working capital for the tubac water district is \$21,683, a decrease to  
5 the original filing of \$18,982.

6 Mohave Wastewater District

7 The correct amount of cash working capital for the Mohave Wastewater District is \$425, a  
8 decrease to the original filing of \$57,933.

9 REVENUE

10 Havasu Water District

11 Arizona-American is adjusting present rate revenue for the annualization of the ACRM Phase 2  
12 increase. This increases present rate revenue by \$150,935.

13 Paradise Valley Water District

14 Arizona-American is adjusting present rate revenue for the annualization of the ACRM Phase 2  
15 increase. This increases present rate revenue by \$371,853

16 Sun City West Water District

17 Arizona-American is adjusting present rate revenue for the annualization of the ACRM Phase 2  
18 increase. This increases present rate revenue by \$155,835.

19 DEPRECIATION EXPENSE

20 Agua Fria Water District

21 Arizona-American reduced the plant accounts for the actual costs of the Sierra Montana 2.2 mg  
22 reservoir. This also would reduce annualized depreciation expense by \$5,316.

23 Havasu Water District

24 In Decision No. 67093, the depreciation rates for the Havasu Water District changed. The new  
25 rates would increase annual depreciation expense by \$9,761. Arizona-American also removed  
26 the Gateway Water and Wastewater Plant from Havasu District and added it to Mohave Water  
27 and Mohave Wastewater, respectively. This reduced annual depreciation expense by \$22,440.  
28 the two changes result in a net decrease to depreciation expense of \$12,679. .

29 Mohave Water District

30 Due to moving the Gateway Water Plant from the Havasu Water District to the Mohave Water  
31 District. plant increased by \$721,333 and depreciation expense increases \$16,386 for these  
32 facilities. The second change decreases depreciation expense for post test year plant.

33 Paradise Valley Water District

34 The post test year amount for depreciation expense is reduced by \$51,921 to \$9,403 due to the  
35 delay in the well no. 12 rehabilitation project.

36 Sun City West Water District

37 There were two rate base adjustments to utility plant in service that effect the annual depreciation  
38 expense in Sun City West Water District. The first was to add back \$76,672 in retirements from  
39 November and December 2007 that belonged in Paradise Valley. The second was to remove  
40 additions that occurred in January and February 2005 in Sun City West Water that actually

1 belonged in Agua Fria Water. The net result of the additions to plant is \$2,606 in additional  
2 depreciation expense..

3 Mohave Wastewater District

4 Arizona-American has three rebuttal adjustments to annual depreciation expense for the Mohave  
5 Wastewater District.

6 a. Decision No. 69440 changed the approved depreciation rates for Mohave Wastewater  
7 District. This change in depreciation rates results in a decrease in annual depreciation expense of  
8 \$23,880. The second adjustment is needed to account for moving the Gateway Wastewater  
9 Treatment Plant from the Havasu Water District to the Mohave Wastewater District. The  
10 additional plant results in additional depreciation expense of \$2,406. The third adjustment to  
11 annual depreciation expense flows from including the actual costs of the wishing well treatment  
12 plant in plant. The actual costs were higher than the estimate by \$343,959 and the resulting  
13 increase in annual depreciation expense is \$10,627.

14 All Districts

15 Arizona-American recommends the following common changes to depreciation rates that would  
16 apply to all districts.

17 Account 304510. Currently, staff is recommending a depreciation rate of 1.67%, or 60 years, for  
18 professional services, permits, fees, and other costs association with evaluating, developing, and  
19 setting up our corporate offices on 7th street. the life of the lease is seven years, so i recommend  
20 a rate of 14.28% to reflect depreciating the set up over the life of the lease.

21 Account 334100, meters. Arizona-American is on a program to change meters every 15 years.  
22 We recommend a rate of 6.7% for all districts. We currently have rates ranging from 2.51% (40  
23 years) to Mohave's recently approved 6.53%.

24 Account 339600. Arizona-American uses this account for comprehensive planning studies,  
25 which are done every five years. Currently, we have 0% depreciation expense. Our internal  
26 audit department is questioning why the rate is not 20%. We recommend a 20% rate to reflect  
27 the five-year applicable period of these studies.

28 Account 340200, computer & peripheral equipment. Staff is recommending a 10% rate for Agua  
29 Fria, Paradise Valley, Sun City West, and Corporate, but is recommending rates of 4.47% for  
30 Havasu, 15.59% for Mohave Water, and 10.83% for Tubac. Arizona-American recommends  
31 using one rate of 10% for every district.

32 Account 341100, transportation equipment light trucks. This account is used for smaller pick-up  
33 trucks. Staff's recommended depreciation rate for our districts varies from 20% to 25%. We  
34 recommend that we use either rate consistently for all districts.

35 Account 341400, transportation equipment – other. This account reflects depreciation being  
36 taken on golf carts purchased for meter readers. The only approved rate is 0.93% in paradise  
37 Valley. In April of 2008, we purchased golf carts in Agua Fria and Mohave Water. Golf carts  
38 last four to six years, so we recommend a consolidated rate of 20% for every district.

1 REJOINDER TESTIMONY

2 Linda J. Gutowski responds to Staff and RUCO surrebuttal testimony concerning rate-base  
3 issues and depreciation expense.

4 RATE BASE – UTILITY PLANT IN SERVICE

5 Agua Fria Water District

6 In Rebuttal Adjustment LJG-1R, Arizona-American is reducing the cost of the Sierra Montana  
7 2.2 MG Reservoir from an estimated amount to the actual cost. This adjustment reduces Plant in  
8 Service by \$252,470.

9 Staff has failed to include an upward adjustment of \$18,581 for Agua Fria projects that were  
10 originally added to Sun City West Water district in error.

11 Havasu Water District

12 Arizona-American moves the Step 2 ACRM Deferral allowed in Decision No. 70626 from  
13 Utility Plant in Service to Deferred Debits. This does two things – puts the deferral where it is  
14 booked, and reduces depreciation expense for Arizona-American by removing it from Plant.

15 Staff removed the Gateway Water Plant from Havasu, but erroneously left the Gateway Sewer  
16 Plant in Havasu.

17 Mohave Water District

18 Staff still left the Mira Monte project plant out of plant in service, despite being provided the  
19 invoices.

20 Paradise Valley Water District

21 Both Staff and RUCO once again have incorrectly included the deferred Well No. 12 project in  
22 rate base.

23 Sun City West Water District

24 Staff failed to remove \$18,581 in Agua Fria project costs that were erroneously recorded in Sun  
25 City West Water District's rate base

26 Mohave Wastewater District

27 Staff and RUCO still fail to properly include all of the Wishing Well Plant in rate base, even  
28 though most of the construction costs were to upgrade the existing capacity.

29 RATE BASE – ACCUMULATED DEPRECIATION

30 All Districts

31 RUCO still claims without support that Arizona-American cannot change its accounting  
32 methodology.

33 RATE BASE – ADVANCES IN AID OF CONSTRUCTION

34 Havasu Water District

35 The advances associated with the Gateway Water Plant need to be removed from Havasu  
36 Water's rate base and included in Mohave Water's rate base.

37 RATE BASE – CONTRIBUTIONS IN AID OF CONSTRUCTION

38 Agua Fria Water District

1 Staff failed to accept an adjustment of \$28,019 of Accumulated Amortization of Contributions in  
2 Aid of Construction ("CIAC") that should be moved from Mohave Water to Agua Fria Water.  
3 The CIAC was moved, but the associated reduction for accumulated amortization was not.

4 Staff and RUCO continue to include the advances and contributions related to plant that is in  
5 CWIP. Arizona-American does not receive cash from developers, it receives plant. There is  
6 nothing to offset existing plant in rate base, until the new plant leaves CWIP to rate base.

7 RATE BASE – DEFERRED DEBITS

8 Havasu Water District

9 Arizona-American moved the Step 2 ACRM deferral out of Utility Plant in Service and into a  
10 Regulatory Asset.

11 SUMMARY OF ARIZONA-AMERICAN'S REJOINDER RATE BASE POSITIONS

|                     | <u>Rate Base</u> |
|---------------------|------------------|
| Agua Fria           | \$92,097,209     |
| Havasu              | \$3,887,188      |
| Mohave Water        | \$10,233,637     |
| Paradise Valley     | \$37,436,060     |
| Sun City West Water | \$38,374,522     |
| Tubac Water         | \$1,457,349      |
| Mohave Wastewater   | \$5,138,539      |

12  
13 DEPRECIATION EXPENSE

14 For corporate plant, Staff uses different depreciation rates for allocations of the same plant to  
15 different districts.

16  
17 Staff failed to include the following amounts in the following districts for the amortization of  
18 regulatory expenses which were approved in Decision 67093:

|                   | Amortization<br>Exp |
|-------------------|---------------------|
| Agua Fria Water   | \$2,918             |
| Havasu Water      | \$ 834              |
| Mohave Water      | \$9,384             |
| Paradise Valley   | \$ 72               |
| Sun City West     | \$5,841             |
| Tubac             | \$ 0                |
| Mohave Wastewater | \$ 0                |

19  
20 Arizona-American has supported its 15-year program of meter change-outs, so an average  
21 vintage life of 6.6% is appropriate.  
22

- 1 Arizona-American inadvertently included the Depreciation Expense of the Citizens' Acquisition
- 2 Adjustment in Agua Fria Water for \$230,973 and in Havasu Water for \$13,852.
- 3
- 4 Staff should have amortized Havasu Water District ACRM O&M over 12 years for an annual
- 5 amortization expense of \$7,916.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
PAUL R. HERBERT  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

DIRECT TESTIMONY

1  
2 Mr. Herbert explains the cost-of-service and rate-design studies prepared for each of the  
3 operating districts submitted in this case. The purpose of the cost-allocation studies is to  
4 determine and allocate the total district cost of service to the several service classifications  
5 served by the Agua Fria, Havasu, Mohave, Paradise Valley, Sun City West and Tubac Water  
6 Districts and by the Mohave Wastewater District. The studies provide a basis for determining .he  
7 extent to which the revenues to be derived from each classification are commensurate with the  
8 cost of serving that classification, within each district.

9 Mr. Herbert sponsors Schedules G-1 through G-9, and the proposed-rates portion of the H  
10 schedules.

REBUTTAL TESTIMONY

11  
12 In his rebuttal testimony, Mr. Herbert responds to the testimony of Staff Witness Mr. Steve Olea  
13 concerning the cost-of-service allocation studies submitted in this proceeding. Mr. Olea contends  
14 that the cost-of-service studies submitted in this case should be given little weight because  
15 certain data related to system delivery volumes were corrected. This is incorrect. Any corrections  
16 are trivial and do not affect the results of my cost-of-service study.

17 The cost-of-service studies prepared and submitted in this case properly reflect the allocation of  
18 costs to the various classes of users and can be used as a guide to design the appropriate rates in  
19 this case

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
SHERYL L. HUBBARD  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

**DIRECT TESTIMONY**

**SPONSORED SCHEDULES**

Ms. Hubbard sponsors the following schedules for each district in the case:

- Schedule A-2 - Arizona-American Summary of Operations
- Schedule A-4 - Arizona-American Construction Expenditures and Gross Utility Plant in Service
- Schedule A-5 - Arizona-American Summary of Cash Flows
- Schedule B-6 - Arizona-American Computation of Cash Working Capital
- Schedule C-1 - Arizona-American Adjusted Test Year Income Statement
- Schedule C-2 - Arizona-American Income Statement Pro Forma Adjustments
- Schedule C-3 - Arizona-American Computation of Gross Revenue Conversion Factor
- Schedule E-2 - Comparative Income Statements
- Schedule E-3 - Comparative Statement of Changes in Financial Position
- Schedule E-6 - Comparative Operating Income Statements
- Schedule E-7 - Operating Statistics
- Schedule E-8 - Taxes Charged to Operations
- Schedule F-1 - Projected Income Statements
- Schedule F-2 - Statement of Cash Flows-Present and Proposed Rates
- Schedule F-3 - Projected Construction Requirements
- Schedule F-4 - Assumptions Used in Developing Projections

**REVENUE REQUIREMENT**

Ms. Hubbard supports the revenue-requirement calculation for each district. Mr. Broderick shows these amounts in his testimony.

**CASH WORKING CAPITAL**

Ms. Hubbard sponsors the lead-lag study that supports Arizona-American's request for cash working capital.

**OPERATING INCOME ADJUSTMENTS**

Ms. Hubbard sponsors the following adjustments to operating income:

- Adjustment SLH-1 - Annualize Payroll Expense
- Adjustment SLH-2 - Annualize Power Expense
- Adjustment SLH-3 - Normalize Purchased Water
- Adjustment SLH-4 - Annualize Chemicals Expense
- Adjustment SLH-6 - Annualize Management Fees

- 1 • Adjustment SLH-7 - Annualize Pensions Expense
- 2 • Adjustment SLH-8 - Amortize Rate Case Expense
- 3 • Adjustment SLH-9 - Annualize Insurance Expense
- 4 • Adjustment SLH-10 - Tank Maintenance Accrual
- 5 • Adjustment SLH-11 - Annualize Depreciation/CIAC
- 6 • Adjustment SLH-12 - Annualize Property Taxes
- 7 • Adjustment SLH-15 - Annualize 40 1 K Expense
- 8 • Adjustment SLH-16 - Line 2 1 Clean-up
- 9 • Adjustment SLH-17 - Remove CAP Revenue and Expense
- 10 • Adjustment SLH-18 - Interest Synchronization
- 11 • Adjustment SLH-19 - Federal and State Income Taxes
- 12 • Adjustment SLH-20 - Annualize Postage Increase
- 13 • Adjustment SLH-21 - One-Time Service Company Charges
- 14 • Adjustment SLH-22 - Adjust Conservation Expenses
- 15 • Adjustment SLH-23 - Blank

16 ADDITIONAL REQUESTS

17 Ms. Hubbard also supports the following requests by Arizona-American:

18 For a power supply adjustment mechanism that will enable Arizona-American to adjust its rates  
19 in the future for changes in rates paid for electric and gas costs;

20 For a tank maintenance reserve to fund tank maintenance expenditures; and

21 For formal adoption by the Commission of the terms and conditions of service on file at the  
22 Commission.

23 REBUTTAL TESTIMONY

24 WORKING CAPITAL

25 The following tables summarize Arizona-American's revised request for the cash-working-  
26 capital component of working capital for each water and wastewater district:

**Table 1 –Cash Working Capital Component of Working Capital**

| District                    | Agua Fria Water | Havasu Water | Mohave Water | Paradise Valley Water | Sun City West Water | Tubac Water | Mohave Wastewater |
|-----------------------------|-----------------|--------------|--------------|-----------------------|---------------------|-------------|-------------------|
| <b>Cash Working Capital</b> | \$ 60,105       | \$47,000     | \$ 185,717   | \$ 79,326             | \$ 77,120           | \$ 21,683   | \$ 425            |

In computing the cash working capital, Staff has made several errors, both formulaic and theoretical. The schedule on which Staff calculates its recommended cash working capital contains mathematical errors and the resulting adjustments are not consistently reflected in each district's Rate Base calculations. Instead of subtracting the expense lag from the revenue lag, the formula subtracts the revenue lag from the expense lag, thus making Staff's Net Lag calculations incorrect. Another error is the use of the Mohave Water District's expense lags for Fuel & Power and Chemicals for the Mohave Wastewater District.

One theoretical error noted while reviewing Staff's recommended cash working capital was the use of an inappropriate level of income tax expense. Staff's cash working capital calculation reflects income tax expense based on adjusted test year revenue instead of the proposed revenues.

RUCO's working-capital calculation also contains many errors. Income tax expense as opposed to the calculations made by Staff discussed above. There were enough errors in a majority of the districts to render RUCO's recommended cash working capital calculations unreliable as filed.

Arizona-American accepts Staff's recommendation to use the expense lags from a recent rate proceeding, the Mohave Water and Mohave Wastewater docket (WS-01303A-06-0014).

**ADJUSTED OPERATING INCOME**

The following tables summarize Arizona-American's rebuttal position for Adjusted Operating Income for each water and wastewater district seeking rate increases in this proceeding:

**Table 2 – Adjusted Operating Income**

| District                  | Agua Fria Water | Havasu Water | Mohave Water | Paradise Valley Water | Sun City West Water | Tubac Water | Mohave Wastewater |
|---------------------------|-----------------|--------------|--------------|-----------------------|---------------------|-------------|-------------------|
| Adjusted Operating Income | \$ 2,878,406    | \$ 47,158    | \$ 305,753   | \$ 2,042,832          | \$ 736,193          | (\$ 40,106) | \$116,454         |

**OPERATING REVENUES**

No party objected to removal of Central Arizona Project ("CAP") surcharge revenues. Ms. Gutowski is sponsoring Arizona-American's adjustment to include Arsenic Cost Recovery Mechanism ("ACRM") surcharge revenues recently approved by the Commission in Arizona-American's Step 2 filings for Havasu Water, Paradise Valley Water, and Sun City West Water districts.

**OPERATING EXPENSES**

The following tables summarize adjusted test year operating expenses for each district:

**Table 3 – Operating Expenses**

| <b>District</b>           | Agua Fria<br>Water | Havasu<br>Water | Mohave<br>Water | Paradise<br>Valley<br>Water | Sun City<br>West Water | Tubac<br>Water | Mohave<br>Wastewater |
|---------------------------|--------------------|-----------------|-----------------|-----------------------------|------------------------|----------------|----------------------|
| <b>Operating Expenses</b> | \$15,940,207       | \$1,130,363     | \$ 4,807,878    | \$ 6,177,754                | \$ 5,121,073           | \$ 467,006     | \$ 679,707           |

Labor Expense

Arizona-American accepts RUCO's adjustment to labor expenses in Agua Fria Water, Mohave Water and Sun City West Water districts.. However, RUCO did not properly apply a 4-factor allocator. The effect of that labor adjustment is summarized in the table below:

**Table 4 – Labor Expense Adjustment**

| District              | Adjustment  |
|-----------------------|-------------|
| Agua Fria Water       | (\$ 37,665) |
| Havasu Water          | ( 2,259)    |
| Mohave Water          | ( 12,768)   |
| Paradise Valley Water | ( 12,536)   |
| Sun City West Water   | ( 13,568)   |
| Tubac Water           | ( 1,183)    |
| Mohave Wastewater     | ( 1,678)    |

Waste Disposal Expense

Arizona-American accepts RUCO's adjustment to adjust waste-disposal expenses in Agua Fria Water, Havasu Water, Mohave Water, Paradise Valley Water, Sun City West Water, Tubac Water and Mohave Wastewater districts. The adjustment is summarized in the table below.

**Table 5 – Waste Disposal Expense Adjustment**

| District                     | Adjustment    |
|------------------------------|---------------|
| <b>Agua Fria Water</b>       | <b>\$ 870</b> |
| <b>Havasu Water</b>          | <b>52</b>     |
| <b>Mohave Water</b>          | <b>295</b>    |
| <b>Paradise Valley Water</b> | <b>290</b>    |
| <b>Sun City West Water</b>   | <b>313</b>    |
| <b>Tubac Water</b>           | <b>27</b>     |
| <b>Mohave Wastewater</b>     | <b>39</b>     |

Chemicals Expense

1 Arizona-American accepts the adjustment proposed by both Staff and RUCO to the chemical  
2 expenses for the Paradise Valley Water District. The proposed adjustment reduces Arizona-  
3 American's original request for chemicals expense in the Paradise Valley district by \$51,945  
4 from a total of \$236,982 to \$185,037. Chemical costs for ferric chloride in the amount of  
5 \$49,530 and polymer in the amount of \$2,415 had been inadvertently double counted. In the  
6 Agua Fria Water District, chemical expenses were also double counted. The amount of this error  
7 is \$139,625.

8 In the Havasu Water District, Arizona-American requested, through Mr. Broderick's testimony,  
9 approval for an amortization period of twelve years for the deferred arsenic O&M costs that were  
10 the subject of Decision No. 69162 (issued December 5, 2006). The effect of this amortization  
11 was inadvertently omitted from the calculation of the chemicals expense for that district.  
12 Arizona-American has included an amount of \$7,916 per year in its chemical expense for  
13 Havasu Water. Ms. Gutowski calculates the deferred balance that Arizona-American is seeking  
14 to amortize.

15 Management Fees

16 Arizona-American reluctantly accepts RUCO's disallowance of the AIP awards as the result of  
17 Arizona-American meeting its financial targets. RUCO's adjustment affects each district  
18 through an allocation process that uses a 4-factor allocation methodology. The adjustment is  
19 summarized in the table below:

20 **Table 6 – Management Fees Adjustment**

| District              | Adjustment  |
|-----------------------|-------------|
| Agua Fria Water       | (\$ 33,408) |
| Havasu Water          | ( 2,004)    |
| Mohave Water          | ( 11,325)   |
| Paradise Valley Water | ( 11,119)   |
| Sun City West Water   | ( 12,035)   |
| Tubac Water           | ( 1,049)    |
| Mohave Wastewater     | ( 1,489)    |

21 Rate Case Expense

22 Arizona-American does not agree with RUCO's recommended three-year amortization period.  
23 Mr. Broderick testifies concerning Arizona-American's revised rate case expense of \$456,000,  
24 which is very close to RUCO's recommended level

25 At the time that Arizona-American revised its filing to eliminate Anthem Water, Anthem  
26 Wastewater and Agua Fria Wastewater districts, it did not revise the 4-factor allocation factors  
27 used to allocate the rate case expenses among the remaining districts. The revised rate case  
28 expense proposed by Arizona-American in this rebuttal filing has been computed using revised  
29 allocators based on the seven remaining districts.

1 Arizona-American agrees with RUCO's finding that an incorrect 4-factor allocator was used in  
2 calculating Tubac Water District's portion of the total rate case expenses. This issue is now  
3 moot because Arizona-American has recomputed the 4-factor for allocating rate case expenses to  
4 reflect the reduction to seven districts in the revised application versus the 10 districts included  
5 in Arizona-American's original application.

6 Regarding RUCO's assertion that Arizona-American included rate case expenses from previous  
7 rate cases, Arizona-American agrees that the rate case expenses for the Sun City West Water  
8 District should be removed but disagrees in the case of the Mohave Water and Mohave  
9 Wastewater districts. The amortization of rate case expense from Decision 69440 began in May  
10 of 2007 and the expenses will not be fully recovered until April of 2010.

11 Water Testing Expense

12 Arizona-American accepts the level of water testing expense contained in Staff witness Dorothy  
13 Hains' testimony. However, it does not appear that Staff included any water-testing expenses in  
14 its proposed Miscellaneous Expenses or any other expense.

15 Line 21 Clean-Up

16 Arizona-American accepts RUCO'S proposed adjustments to miscellaneous expense to disallow  
17 certain line 21 expenses.

18 Tank Maintenance Expense (Maintenance Expense)

19 Arizona-American has reviewed its original request and is proposing some modifications. The  
20 basis of the cost estimates has been revised and is discussed in greater detail in Mr. Day's  
21 testimony. These revised cost estimates have been incorporated into the original calculations and  
22 a revised request has been proposed.

23 Property Taxes

24 The proposed adjustments to property taxes recommended by Staff and RUCO are merely  
25 conforming adjustments to reflect each party's changes to the revenue requirement. Arizona-  
26 American has revised this expense in its rebuttal filing to conform with its revised revenue  
27 increase proposal as well.

28 Income Taxes

29 The proposed adjustments to income taxes recommended by Staff and RUCO are merely  
30 conforming adjustments to reflect each party's changes to the revenue requirement. Arizona-  
31 American has revised this expense in its rebuttal filing to conform with its revised revenue  
32 increase proposal as well.

33 FUEL AND POWER SUPPLY ADJUSTMENT MECHANISM

34 In response to RUCO, Arizona-American stands by its recommended Fuel and Power Supply  
35 Adjustment Mechanism. Power costs are a large component of Arizona-American's operating  
36 expenses. For the seven districts in this proceeding, fuel and power costs represent  
37 approximately 12% of the total operating expenses. Most businesses are able to adjust their  
38 prices to accommodate large increases in these expenses which may be uncontrollable depending  
39 on their operations. A utility cannot make these adjustments without a fuel and power supply  
40 adjustment mechanism.

1 The majority of the power costs that Arizona-American incurs are in relation to the delivery of  
2 water to its customers. Increases are typically the result of changes in rates and tariffs of its  
3 power suppliers, which are regulated by the Corporation Commission, so Arizona-American has  
4 no control over their price increases. That is why this cost is the perfect expense for an adjustor  
5 mechanism.

6 WHITE TANKS SURFACE WATER TREATMENT PLANT

7 In order to maintain a healthy, viable utility, actual recovery of the invested capital and  
8 associated operating costs must occur in a timely fashion. Deferrals of the depreciation expense  
9 and return on the investment cannot sustain Arizona-American's financial condition.

10 Arizona-American requested hook-up fee financing of the White Tanks Plant under the  
11 assumption that there would be sufficient contributions in aid of construction ("CIAC") from  
12 hook-up fees to enable it to offset the deferred return and deferred depreciation on its investment  
13 in the White Tanks Plant to avoid the write offs that will be required if accumulated hook up fees  
14 are inadequate to offset the equity portion of the deferred return and depreciation expense when  
15 the plant goes into service.

16 Currently, a hook-up fee has been approved by the Commission to finance the construction of the  
17 White Tanks Plant. The hook-up fees are recorded as contributions in aid of construction  
18 ("CIAC") which reduces rate base and the associated revenue requirement of the investment.  
19 Since the plant was projected to be in service prior to collection of all of the hook-up fees  
20 necessary to finance the plant, Arizona-American sought, and the Commission approved, the  
21 accounting treatment proposed, which addressed the timing of the completion of construction  
22 and recovery of the plant costs in excess of the CIAC collected at that time.

23 The Financial Accounting Standards Board ("FASB") issued Statement of Financial Standards  
24 No. 92 ("SFAS 92") to amend its original FASB Statement No. 71 which provided accounting  
25 guidance to regulated enterprises when the regulator issues decisions that depart from  
26 conventional rate-making methods regarding the recovery of allowable costs of the plant. A  
27 departure from conventional rate-making occurs when alternatives to the recovery scenario are  
28 adopted by the regulator such as deferral of depreciation expense, deferral of O&M expenses,  
29 and deferral of the return on the investment which results from providing the accumulation of  
30 post in-service allowance for funds used during construction ("AFUDC"). These statements  
31 provide guidance as to when a regulated entity might be required to write off an asset.

32 Mr. Broderick stated that a write off of the plant was possible after August 2011. Now it appears  
33 that the write-off could come even earlier. Mr. Broderick's projections were based on estimated  
34 hook-up fees that have been adjusted downward based upon the housing market in Arizona and  
35 more current economic indicators. Based upon the amount of hook-up fees collected to date and  
36 the projections of future hook-up fees to be collected, it appears that the potential write off will  
37 occur well before that date.

38 Arizona-American is hopeful that the parties first, and then the Commission will be persuaded  
39 that inclusion of \$25 million of the White Tanks Plant's construction work in progress ("CWIP")  
40 in rate base is a reasonable solution to avert a potential financial disaster. Without the necessary  
41 rate relief in this proceeding, Arizona-American will face certain financial hardship shortly after

1 the completion of construction of the White Tanks Plant. A regional surface water treatment  
2 plant will be beneficial to Arizona-American's customers in Maricopa County as well as the  
3 State of Arizona. Inclusion of White Tanks Plant's CWIP in rate base in this case, and/or  
4 Commission assurance of future recovery by approving a mechanism such as was approved for  
5 arsenic treatment plant cost recovery is imperative to Arizona-American's financial health.

6 **REJOINDER TESTIMONY**

7 **WORKING CAPITAL:**

8 Arizona-American has incorporated revised service and billing lags in the calculation of  
9 the revenue lag filed in conjunction with this rejoinder testimony.

10 Average daily revenues and average accounts receivable balance should both be  
11 computed on a comparable basis or 365 daily balances. Based on these computations,  
12 Arizona-American has recalculated revenue lags and cash-working capital for each  
13 district.

14 **MISCELLANEOUS EXPENSE**

15 Staff failed to include Ms. Hains' water-testing expenses in its proposed Miscellaneous  
16 Expenses or any other expense in its direct case or surrebuttal case presentations.

17 **PROPERTY TAXES AND INCOME TAXES**

18 Based on the cash-working capital adjustment and the inclusion of water-testing expense,  
19 Arizona-American recalculates property tax and income tax expense.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
JOHN C. (JAKE) LENDERKING  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

1 DIRECT TESTIMONY

2 Mr. Lenderking testifies as follows:

3 WATER CONSERVATION

4 Arizona-American presently spends approximately \$40,000 annually in its Sun City Water, Sun  
5 City West Water and Agua Fria Water Districts on water conservation. This amount was  
6 authorized by Commission Decision No. 60172, issued on May 7, 1997. This level of funding  
7 has been used in part to assist Arizona American to meet ADWR conservation regulations.

8 Arizona-American's conservation program is called Save H2O. The Save H2O program  
9 encourages and promotes water conservation in many ways, including:

- 10 • Participation in community events;
- 11 • Home Water Audits;
- 12 • Internet communication;
- 13 • Rinsesmart Program;
- 14 • Water conservation messages in customer bills;
- 15 • Providing water conservation kits (upon request);
- 16 • Financial assistance and staff participation in the Regional "Water Use it Wisely"  
17 Campaign; and
- 18 • As a compliance requirement, a report to the Commission is provided each year that  
19 provides greater detail.

20 Arizona-American is considered by ADWR to be a "municipal water provider," which makes it  
21 generally subject to ADWR regulation. The new ADWR water conservation program is known  
22 as the Modified Non-Per Capita Conservation Program ("MNPCCP"). Because Arizona-  
23 American already implements conservation measures, the effects of the MNPCCP on the  
24 Arizona-American districts will be minimal.

25 CAP SURCHARGE MODIFICATION

26 Because of a failure at the Miller Road Treatment Facility, untreated water from the PCX-1 well  
27 owned by the Salt River Project ("SRP"), a well contaminated with trichloroethylene was  
28 introduced into the district's water supply. There were no health effects, but the incident  
29 highlighted the risk of using the PCX-1 well as part of the district's water supply. Among other  
30 things, Arizona-American has determined that it will no longer use the PCX-1 well as part of the  
31 water supply for its Paradise Valley Water District.

32 Arizona-American has secured an allotment of CAP water for the benefit of its Paradise Valley  
33 Water District customers. However, it has no economical way to physically deliver and treat the  
34 CAP water for delivery to customers. Arizona-American was able to make use of its CAP  
35 allocation through an exchange with SRP where it exchanged its CAP allocation with SRP in  
36 return for rights to water pumped from the PCX-1 well. The exchange allowed Arizona  
37 American to take water from the PCX-1 well, treat it at the Miller Road Treatment Facility to

1 remove TCE, and then blend it with other water sources for delivery to Paradise Valley Water  
2 District customers.

3 The current SRP water delivery charges and the SRP administrative charges total \$22.62 per  
4 acre-foot. The current CAP annual Municipal and Industrial water service charges are \$91 per  
5 acre-foot and the Municipal and Industrial capital charges are \$21 per acre-foot. The seventh  
6 revised CAP Surcharge, authorized by Commission Decision No. 61831, recovers both the SRP  
7 and CAP costs.

8 Arizona-American has added storage for the Paradise Valley Water District and presently has  
9 enough capacity to run the system without the PCX-1 well. Further, as discussed by Mr. Gross  
10 in his testimony, Arizona-American is, among other things, replacing Well 12 with a new well,  
11 which will return its production to its original level of 2200 gallons per minute.

12 Arizona-American will store and recover the district's 3,231 acre-feet allocation of CAP water at  
13 the Tonopah Desert Recharge Project, owned by the Central Arizona Water Conservation  
14 District ("CAWCD"). The stored CAP water will then be "recovered" from wells in the Paradise  
15 Valley Water District. The cost to store water is much lower than the cost to exchange water with  
16 SRP. The current price to store water at a CAWCD facility in the Phoenix AMA is \$8 per acre  
17 foot while the cost to exchange water with SRP is \$22.62 per acre foot.

18 REJOINDER TESTIMONY

19 Marshall Magruder cites a statutory provision that allows some water providers to prevent  
20 exempt wells from being drilled within their service area. However, this provision does not  
21 apply to Arizona-American's Tubac Water District. This statute clearly disallows exempt wells  
22 within the lands served by a municipal provider with an assured water supply designation.  
23 However, Arizona-American's Tubac Water District, which is considered to be a municipal  
24 provider, has not received an assured water supply designation. Therefore, Arizona-American  
25 cannot prevent exempt wells in its service area.

26  
27 Using certificates of assured water supply placed the burden and costs of proving 100 years of  
28 water on the developer, but gaining an assured water supply designation places the burden and  
29 costs on the water provider.

30  
31 Although many certificates of assured water supply have been obtained in the Tubac Water  
32 District, Arizona-American has been exploring the possibility of obtaining an assured water  
33 supply designation. A big issue which will impede Arizona-American's progress is the  
34 development of new assured water supply rules by the Arizona Department of Water Resources.  
35 This may substantially delay, or prevent Arizona-American from obtaining an assured water  
36 supply designation.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
JEFFREY W. STUCK  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

1 **REBUTTAL TESTIMONY**

2 Jeffrey W. Stuck testifies as follows:

3 **Tubac Water District**

4 Arizona-American is planning to construct a central plant to treat the district's water supply,  
5 which presently exceeds the federal arsenic standard of 10 parts per billion. The Central Plant  
6 treatment option is less expensive, more thorough, easier to manage, and consistent with  
7 recommendations provided by the Arizona Department of Environmental Quality ("ADEQ").

8 In the Tubac Water District, the initial cost for the Central Plant treatment option will be  
9 approximately \$2.3 million versus only about \$544,000 for the Point-Of-Use option. However,  
10 the annual O&M costs for the Central Plant option are only about \$173,000 compared to  
11 \$349,000 for the Point-Of-Use option. Consequently, the he cross-over point in our Tubac  
12 Water District would occur in approximately the tenth year.

13 The Central Plant option treats all water delivered to the customer. This means that the water  
14 from every tap will meet the federal arsenic standard, including water used for showering and  
15 tooth brushing. The Point-Of-Use option would only treat water at one location, the kitchen tap.

16 For the Point-Of-Use Option, Arizona-American would have to regularly enter every customer  
17 residence or business to test the systems and to replace filters. This would not only be a burden  
18 on Arizona-American, but also on our customers.

19 Our Tubac Water District had an average of 535 customers during the test year. In its Arsenic  
20 Master Plan, a compliance guidance document for the arsenic regulation, ADEQ does not  
21 recommend use of Point-Of-Use devices in public water systems that serve more than 300  
22 connections due to the breakpoint cost for O&M. This is consistent with our projections.

23 **Mohave Water District**

24 Arizona-American is currently negotiating an agreement with the Laughlin Ranch Developer  
25 which currently owns the LR1 well. We hope to finalize the agreement very quickly and to have  
26 the well in service by August 31, 2009, as recommended by Staff.

27 **Mohave Wastewater**

28 In 2007, the actual waste disposal expense associated with hauling away liquid sludge from the  
29 Wishing Well Plant was \$186,330. As part of the upgrade, Arizona-American installed a screw  
30 press to dewater the sludge. I estimate that the annual cost of disposing of solid waste from the  
31 Wishing Well plant will drop to just \$45,000. Therefore, I conservatively estimate plant  
32 operating-expense savings of approximately \$140,000 per year.

33 Flows have continued to increase at the Wishing Well Treatment Plant. December 2008 saw the  
34 greatest monthly flows in the plant's history. Peak flows have also continued to increase. Our  
35 peak day was November 26, 2008, where flows reached 284,000 gallons. This was 84,000  
36 gallons more than the Plant's former effective capacity of 200,000 gallons per day, or 42% above  
37 daily capacity.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
PAUL G. TOWNSLEY  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

DIRECT TESTIMONY

Mr. Townsley testifies as follows:

Arizona-American's current financial condition is poor; timely and adequate rate relief from the Commission is critically important.

Arizona-American has reached agreement with the Maricopa County Municipal Water Conservation District Number One ("MWD") which provides MWD an option to participate in the White Tanks Plan

Arizona-American's requests to extend the expiration date of the Agua Fria Hook-up Fees and to include construction work in progress in rate base are appropriate.

Arizona-American's Achievement Incentive Pay benefits our customers.

American Water is now a publicly-traded company.

REBUTTAL TESTIMONY

Arizona-American's current financial condition continues to be poor - timely and adequate rate relief from the Commission is necessary. In addition, management at Arizona-American is undertaking a number of actions to improve Arizona-American's financial performance by reducing costs, staffing, and capital expenditures.

Arizona-American's request to establish a deferral account for O&M costs for the White Tanks Plant is reasonable. In addition, Arizona-American's request to extend the expiration date of the Agua Fria hook-up fees and to include construction work in progress in rate base is appropriate.

Staff and RUCO recommendations regarding the White Tanks Water Treatment Plant and the Wishing Well Wastewater Treatment Plant will cause harm to Arizona-American and should be rejected.

There are long-term benefits to customers of consolidation for ratemaking purposes between Arizona-American districts. Arizona-American supports consolidation of its districts but needs to ensure that the consolidation process does not cause further financial harm to Arizona-American through delays in this case.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman  
GARY PIERCE  
PAUL NEWMAN  
SANDRA D. KENNEDY  
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**TESTIMONY SUMMARY  
FOR  
BENTE VILLADSEN  
ON BEHALF OF  
ARIZONA-AMERICAN WATER COMPANY  
MARCH 17, 2009**

1 DIRECT TESTIMONY

2 Dr. Bente Villadsen, a Principal at The Brattle Group, files testimony on the cost of capital for  
3 Arizona-American districts (collectively, "Arizona-American").

4 Dr. Villadsen selects two benchmark samples, water utilities and gas local distribution  
5 companies ("LDC"). She estimates the sample companies' cost of equity, associated after-tax  
6 weighted-average cost of capital, and the corresponding cost of equity at 46.9 and 41.6 percent  
7 equity. She also reviews recent Arizona water and wastewater decisions. In undertaking her  
8 analysis, Dr. Villadsen notes that the overall cost of capital is constant within a broad middle  
9 range of capital structures although the distribution of costs and risks among debt and equity  
10 holders is not. Because Arizona-American's requested target of 46.9 percent equity is lower than  
11 the percentage equity among many utilities, its financial risk is higher and the return required by  
12 investors increases with the level of risk they carry. Should short-term debt be included for an  
13 equity percentage of 41.6 percent, Arizona-American's capitalization is further below that of the  
14 average water utility.

15 Based on the evidence from the samples, Dr. Villadsen estimates a cost of equity for the  
16 benchmark samples at Arizona-American's capital structure to be in the range of 11.0 to 12.5  
17 percent, so that Arizona-American's request for 11.75 percent is equal to the midpoint. Dr.  
18 Villadsen also reviewed recent Arizona decisions and found that the decisions correspond to a  
19 cost of equity of approximately 11.0 and 12.25 percent when applied to an entity with 46.9 and  
20 41.6 percent equity, respectively. She therefore finds that Arizona-American's request for 11.75  
21 percent return on equity is reasonable and full supported by her analysis.

22 REBUTTAL TESTIMONY

23 Dr. Villadsen responds to the testimony submitted by Mr. David C. Parcell on behalf of Arizona  
24 Corporation Commission Staff and by Mr. William A. Rigsby on behalf of the Residential Utility  
25 Consumer Office. Dr. Villadsen continues to believe that 11.75% is an appropriate return for  
26 Arizona-American on equity at 46.75% equity.

27 Mr. Parcell relied on three different samples of water companies, and used versions of the  
28 Discounted Cash Flow ("DCF") method, the Capital Asset Pricing Model ("CAPM"), and the  
29 Comparable Earnings method to arrive at his recommended 10% return on equity for Arizona-  
30 American. The recommendation of Mr. Parcell is too low, because (i) it is at or near the rate at  
31 which an affiliate recently raised debt, (ii) unlike prior Staff testimony, it failed to consider that  
32 Arizona-American's debt ratio is higher than that of the comparable companies, and (iii) it relied  
33 on downward biased data such as a geometric market risk premium for the CAPM, historical  
34 growth rates in its DCF, and regulated entities only in the comparable earnings methodology. In  
35 sum, the recommended 10% return on equity is too low, and does not reflect the Company's cost  
36 of equity.

37 Mr. Rigsby's recommended 8.88% return on equity on 44.8% equity is so low that it is below the  
38 cost at which an affiliate recently issued debt and only slightly above the current yield on  
39 investment-grade public utility bonds. This recommendation violates basic principles of finance,  
40 and would not afford the Company the opportunity to successfully raise equity capital, especially  
41 in a period of increased uncertainty due to the current financial and economic crisis. Further, Mr.  
42 Rigsby fails to take into account that the Company has higher financial risk than the comparable  
43 companies and also makes a number of inappropriate assumptions in implementing both the

1 DCF method and the Capital Asset Pricing Model, which make his estimated 8.88% cost of  
2 equity completely unreliable.

3 REJOINDER TESTIMONY

4 Dr. Villadsen responds to the surrebuttal testimony submitted by Mr. David C. Parcell on behalf  
5 of Arizona Corporation Commission Staff and by Mr. William A. Rigsby on behalf of the  
6 Residential Utility Consumer Office.

7 Both Mr. Parcell and Mr. Rigsby critique Dr. Villadsen's use of American Water's recent debt  
8 issue as a benchmark for Arizona-American's cost of equity. It is the most recent market  
9 information on the cost of capital for the company and therefore highly relevant for the  
10 determination of the company's cost of capital.

11 The ongoing financial crisis has had and continues to have a broad impact on utilities access to  
12 and cost of capital. The drop in stock prices is likely caused by numerous factors including  
13 earnings expectations, investor risk aversion, and the equity risk premium. Mr. Parcell's  
14 surrebuttal mistakenly considers only earnings expectations.

15 Both the Parcell Surrebuttal and the Rigsby Surrebuttal disagree with my critique of their  
16 implementation of the DCF and CAPM methodology. However, neither provided textbook or  
17 other convincing support for the disputed methods. Therefore, I continue to believe my rebuttal  
18 critique was merited.