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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** |
| 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 the**

**REPLY BRIEF**

**by**

**Marshall Magruder**

Arizona Corporation Commission
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This filing has been mailed to parties in the Service List.

Respectfully submitted on this 15th day of May 2009,

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# REPLY BRIEF

by

**MARSHALL MAGRUDER**

**15 May 2009**

In

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

ACC Docket No. W-01303A-08-0227

And

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

ACC Docket No. SW-01303A-08-0227

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## Section 1 – SUMMARY OF THE CASE

### 1.1 Summary of the Case.

This summary provides an overview for each issue presented by this party in this case. Four Issues have continued throughout this case, namely:

a. Issue 1 – **Conservation as a Significant Driver for Water Volumetric rates**. This concerns using realistic price signals in the rate structure design to encourage water conservation. Using lowest rates for the lowest consuming users and highest rates for highest consuming users with multiple price signals to make obvious higher usage has higher costs. The price signals, at break points between rate blocks, must spread across the high usage part of the consumption curve, with ten or more, to make obvious these price change points.

b. Issue 2 – **Capital Expenses for the Tubac Arsenic Removal Facility**. This issue concerns the high cost of this facility and ways to reduce such costs. The Company's cost estimates appear higher that reasonable comparisons with another comparable facility. Other funding sources are being pursued. The point of use approach is less expensive and is a viable option, especially since one is a single purpose facility compared to versatility for the range of potential pharmaceuticals, toxic minerals and other pollutants found in the local water.

c. Issue 3 – **Rate Consolidation for All Arizona-American Water Districts**. All customers receive the same product, that is water, but at significant differences in Service Charges, Rates and Rate structures, various fees and charges, and Rules and Regulations. The continuation of the present rate design process is discriminatory, not fair or reasonable. Consolidation is a goal the Company and all parties agree, but it is the implementation details are where differences occur. A solution was presented to start implementation as part of this rate case.

d. Issue 4 – **Removal of some Rate Case Expenses**. This is a minor rate case cost issue.

### 1.2 Organization of this Reply Brief.

The Brief provides a reply to other party's Post Hearing Opening Brief for each of these issues.

### 1.3 Limitations in this Brief.

References contained herein are to the Post Hearing Opening Briefs by the Company, Residential Utility Consumer Office (RUCO), ACC Staff and Magruder, each will be referred to as "Brief" although variance in names were used in their 1 April 2009 submissions.

## Section 2

## ISSUE NO. 1

## CONSERVATION AS A SIGNIFICANT DRIVER OF WATER VOLUMETRIC RATES

### 2.1 Summary of Issue No. 1.

The results of rate structure design are revenue-neutral for the Company with obvious "price signals" so ratepayers can actually make behavior changes required to reduce their water demands and conserve water. (Magruder Brief, 12)

A rate structure with frequent price changes provides an opportunity so customers can clearly see "price signals" by the proposed ten-tier inverse rate block structure. It has price-breaks at 4,000-gallon intervals for residential (5/8 & 3/4-inch) and the smallest commercial customers. This stair-stepped, increasing rate process is necessary for every rate category, including commercial categories. A nearby water-short company has much higher rates than Arizona-American, especially for its highest consuming ratepayers. (*Ibid*, 12, footnote 5)

The principle used by this party is *that customers who use the least amount of water pay the lowest rates and conversely for the highest consuming customers, the highest rates*. (*Ibid*, 13)

A significant difference between these extremes is an important feature, to show the strength of price to influence consumption. When consolidation is considered, ten or more rate tiered structure can provide important impacts for *fairness and reasonableness*. (*Ibid*)

The lowest rate tiers, with the lowest rates, provide a "low income" ~~measure~~measure, as the company's rate structure has no minimal or low-income rates. (*Ibid*)

No other Party presented a rate structure with significant differences between the lowest to highest rate differences; however, the Staff Alternative Rate Design for Tubac testimony was closest to this party's. None proposed more than two tiers for commercial customers, which means only one break point exists as a price signal that might already have been exceeded or reaching that demand break point is beyond reason. (*Ibid*)

This issue consists of two parts, the Service Charge and the Consumption (volumetric) rates. The Service Charge passes the overall infrastructure fixed costs to customers and the volumetric rates are based on water consumed. The combination of these two must be rate-neutral so the Company's revenue is a fair rate of return on its investment. (*Ibid*, 13)

### 2.2 Reply to Post Hearing Opening Briefs.

#### 2.1.1 Proposed Additional "Price Signal" Breakpoints in the Commodity Rate Structures.

Company Brief.

In section "Tubac Rate Design" the Company stated Magruder proposed "many more rate blocks, with severe inverted block rates" for the Tubac Water District. (Company Brief, 52)

Further, Arizona-American opposed the Magruder proposal and "will respond further in its reply brief." (*Ibid*) *[Note: This makes a reply herein rather challenging.]*

RUCO and Briefs.

Neither discussed additional breakpoints in rate structures.

Magruder Reply.

Magruder testimonies determined a rate structure with a reasonable Service Charge plus multiple tiers with clear, obvious, observable and attainable "price break points" so customers reduce their costs by reducing their consumption. (Magruder Brief, 13)

"The Tubac Water District was used throughout as an example; however, all resultant conclusions and recommendations are company-wide, and specifically only for the six water districts in this case." (*Ibid*, 13, underlined original)

The Company missed this point.

The Magruder-proposed ten-tiered rate block process is for use with ALL rate classes and categories for all six water districts. Each rate class (residential, commercial) and category (by consumption) may have different rate block sizes and rates. (*Ibid,* 12-13)

The Company in all its filings failed to demonstrate any understanding of sending price signals as a way to conserve water. In Tubac and the other water districts herein, proposed residential rates have wide variations and wide differences. (*Ibid,* 20)

The Company does not understand the impact of a "price signal" or how to make meaningful and fair rates to conserve critical water in a desert state that is not sustaining its water table.

At least 100% difference should be used to send price signals between multiple tiers and still be revenue neutral. (*Ibid,* 14) Magruder used 400% for residential and small business rates.

This Party's proposed consumption rates are based on lowering the rates for low volume users and raising the rates for high volume water users. To make this effective, one must ensure the customers can "see" the benefits of lower cost with lower water consumption. These "price signals" must be visible and must be attainable or using the inverse rate block structure has no other major purpose. (*Ibid,* 17, emphasis added)

In Table 1, major differences in the proposed residential rate schedules for the example water district are shown. The same type of differences also exists for the other districts. (*Ibid*, 17, and Table 3)

The Magruder proposed rates are clear, obvious and progressively increase with consumption. NO logical rationale has been presented or may exist for the major differences and variances in volumetric rates and rate blocks being proposed. (*Ibid*, 17)

**Table 1. Present and Proposed Tubac Residential Rate Commodity Tiers and Rate Schedules**
(Per 1,000 gallons)

| Commodity Usage Tiers | **Magruder's Proposed Rates** | Present Rates | Company Initial Proposal | Company Final Proposal | Staff Final Proposal | Staff Alternative | RUCO Final Proposal |
|---|---|---|---|---|---|---|---|
| 0 to 3,000 gallons | **$1.50** | $ 1.89 | $ 3.78 | $ 3.400 | $ 2.67 | $ 1.90 | $ 3.4341 |
| 3,001 to 10,000 gallons | | | | | | | |
| First 4,000 gallons | **$1.50** | $ 1.89 | $ 3.78 | $ 3.400 | $ 2.67 | $ 3.00 | $ 3.4341 |
| 4,001 to 8,000 gallons | **$ 2.00** | $ 2.85 | $ 4.85 | $ 4.800 | $ 4.15 | | $ 4.4062 |
| 8,001 to12, 000 gallons | **$ 2.50** | | | | | | |
| 10,001 to 20, 000 gallons | | | | | | $ 4.00 | |
| 12,001 to 16,000 gallons | **$ 3.00** | | | | | | |
| 16,001 to 20,000 gallons | **$ 3.50** | | | | | | |
| 20,001 to 24,000 gallons | **$ 4.00** | $ 3.41 | $ 4.95 | $ 5.500 | $ 5.25 | $ 6.00 | $ 4.4971 |
| 24,001 to 28,000 gallons | **$ 4.50** | | | | | | |
| 28,001 to 32,000 gallons | **$ 5.00** | | | | | | |
| 36,001 to 40,000 gallons | **$ 5.50** | | | | | | |
| 40,001 gallons and above | **$ 6.00** | | | | | | |

Numerous price-break points are required for a wide range of consumption. As shown in this table, ten tiers or rate blocks were proposed for ALL rate categories. All customers, residential and commercial, should be able to see and <u>be rewarded</u> with lower water usage costs for conserving water in our state. (*Ibid*, 17, original underlined)

The RUCO and Staff rate structure proposals have weak price signals compared to this party. The Staff's Final (Alternative) Rate Structure 4-Tier, for Tubac is the closest proposed to send price signals. A 5-Tier structure proposed for Paradise Valley has such large water volume differences between steps (up to 60,000 gallons) that inhibit any customer to reduce demand by one step to a lower water rate. (*Ibid*, 20-21)

The Company appears to have not considered water conservation important in rate design.

At least 100% difference between lowest and highest rates should be used to send price signals with multiple tiers and remain revenue neutral. Magruder proposed a 400% difference in residential rates, from $1.50/1000 gallons and to $6.00/1000 gallons. (*Ibid,* 14)

Cost of Service is a fixed charge and is not intended to provide customers a "price signal" to encourage water conservation. The Company, RUCO, and Staff have proposed significant increases in this charge. Table 2 has illustrative data for Tubac, the water district with highest The Tubac Cost of Service. These proposals illustrate these wide variations without explanation.

Further, the Cost of Service rate categories should be based only on size of the interconnection and be identical for Residential and Commercial rate types (with same sized connection). Since the amount of water demand is determined by infrastructure size to serve a

customer, there should be NO difference in Cost of Service for residential and commercial customers with the same-size meter connection. (*Ibid,* 15)

The Magruder residential cost of service proposal is for all water districts. (*Ibid,* 14)

**Table 2. Proposed Cost of Service Comparisons (Tubac Water District Example).**

| Customer Type | Rate Category | | Present | Company Initial | Company Final | RUCO Final | ACC Staff Alternative | Staff Final | **Magruder Proposal** | Number of Customers |
|---|---|---|---|---|---|---|---|---|---|---|
| Residential | 5/8 & 3/4-in | F1M1A | $ 19.68 | $32.50 | $ 31.00 | $ 29.53 | $24.00 | $ 32.50 | **$25.00** | 461 |
| | 1-inch | F1M1B | $ 29.63 | $ 48.93 | $ 46.67 | $ 44.45 | $72.00 | $ 48.63 | **$50.00** | 41 |
| | 2-inch | F1M1D | $97.49 | $161.00 | $153.57 | $146.27 | $224.00 | $161.00 | **$100.00** | 3 |
| | 3-inch | F1M1E | $115.65 | $190.99 | $182.17 | $173.52 | $448.00 | $190.99 | **$150.00** | 1 |
| | | | | | | | | | Total Residential Customers | 489 |
| Commercial | 5/8 & 3/4-in | F2M1A | $ 19.68 | $ 32.50 | $ 31.00 | $ 29.53 | $24.00 | $ 32.50 | **$ 25.00** | 47 |
| | 1-inch | F2M1B | $ 29.63 | $ 48.93 | $ 46.67 | $ 44.45 | $72.00 | $ 48.63 | **$ 50.00** | 16 |
| | 1½-in | F2M1C | $ 59.26 | $ 97.66 | $ 93.35 | $ 89.91 | $140.00 | $ 97.86 | **$ 75.00** | 2 |
| | 2-inch | F2M1D | $ 97.49 | $161.00 | $153.57 | $146.27 | $224.00 | $161.00 | **$ 100.00** | 10 |
| | 3-inch | F2M1E | $115.65 | $190.99 | $182.17 | $173.52 | **$448.00** | $190.99 | **$ 150.00** | 4 |
| | | | | | | | | | Total Commercial Customers | 78 |
| Growth | 5/8 & 3/4-in | F1M1A | Same at Residential F1M1A | | | | | | | 10 |
| | | | | | | | | | Total Customers | 549 |

The Company, RUCO and Staff proposed significant Cost of Service differences for customer types. (*Ibid,* 15)

Significant variations in proposed Cost of Service in this example water district vary for small residential/commercial customers. This pales if compared to 3-inch residential/commercial customer change. The Staff Alternative at $448.00 greatly exceeds the $191.00 charge proposed by the others; therefore, this appears to be an error, along with the 2-inch Cost of Service proposed in the Staff Alternative. (*Ibid*, 15)

Significant differences in the basic Cost of Service exist in each water district to provide the same product, to meet the same standards, using the same engineering and operations staffs, and the same administrative personnel. In addition, proposed <u>increases</u> vary from $0.25 for Mohave (Staff) to $12.82 for Tubac (Company Final). (*Ibid,* pp. 15-25, Table 2)

These unstable and unfair fixed charges must be reviewed for consolidation to accomplish long-term leveling. This will eliminate the peaks and valleys in the existing Cost of Service charges, and will greatly improve the public relations for the Company. These cost swings will continue until consolidation is complete, as all water districts require major capital improvements, at various asynchronous times that make these large cost swings. (*Ibid,* 16)

The six water districts in this case have the average monthly consumption for residential customers shown in Table 3. Also shown are present, Company initial and final proposed costs

for the first 1,000 gallons in the First Tier. Except for the Staff's Alternative Rate Design for Tubac, all water district rates use the first 4,000 gallons for the First Tier. (*Ibid*, 18; Table 4, 19)

**Table 3 – Average Residential Consumption and Initial Cost Proposals for First, 1,000 Gallons.**

| Water District | Average Consumer Water Consumption | Proposed Cost per 1000 gallons for First 1,000 Gallons | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | Present | Company Initial | Company Final | RUCO Final | Staff Alternative | Staff Final | Magruder |
| Sun City West | 6,704 gallons | $ 1.35 | $ 2.880 | $ 2.8734 | $ 2.6929 | Same as Staff Final | $2.75 | $ 1.50 |
| Agua Fria | 7,400 gallons | $ 1.53 | $ 2.926 | $ 2.9260 | $ 2.2697 | | $ 1.84 | $ 1.50 |
| Mohave | 8,073 gallons | $ 0.85 | $ 1.471 | $ 1.3190 | $ 1.1944 | | $ 0.88 | $ 1.50 |
| Havasu | 9,705 gallons | $ 1.68 | $ 4.033 | $ 3.4390 | $ 2.2741 | | $ 2.26 | $ 1.50 |
| Tubac | 10,757 gallons | $ 1.89 | $ 3.400 | $ 3.7800 | $ 3.4341 | $ 1.90 | $ 1.89 | $ 1.50 |
| Paradise Valley | 20,493 gallons | $ 1.21 | $ 1.223 | $ 1.2130 | $ 1.3119 | $1.200-$ 1.050 | $ 1.41 | $ 1.50 |
| Total for 6 water districts | 63,132 gallons | $8.51 | $15.9333 | $15.5504 | $13.1771 | | $ 11.0400 | $9.00 |
| Average for 6 water districts | 10,522 gallons | $1.4186 | $ 2.6555 | $ 2.5917 | $ 2.6350 | | $ 1.8400 | $ 1.5000 |

Table 3 provides the average water consumption per residential customers by water district. In general, Sun City West has the lowest consumption at 6,704 gallons per customer, and increasing approximately 1,000 gallons a month, for Agua Fria, Mohave, Havasu, and Tubac at 11,757 gallons per average customer. These are tightly grouped compared to Paradise Valley with an average customer using almost 20,500 gallons per month. (*Ibid*)

There is no correlation between Average Water Consumption and rate schedules. (*Ibid*, 18)

The proposed rates in Table 3 vary from $0.88 for Mohave (Staff) to $4.033 for Havasu (Company Final). The proposed Tubac rates vary between $1.41 (Staff) and $3.78/1,000 gallons (Company Final). There is no logical reason or has any rationale been provided in this case that would lead to such a wide variance. (*Ibid*, 18 and Table 4, 19)

As shown in Magruder Exhibit MM-6, with progressive tiers, the higher usage rates of $6.00 (or capped at $5.00 for largest commercial due to economics of scale) provide considerably more revenue for the Company than the present revenue from water usage. This "extra" revenue is included to cushion an anticipated impact from customer conservation measures to providing adequate revenue for the Company. (*Ibid*, 18)

**Table 4. Sample Tubac Residential Customer Bill Comparing Company and Magruder Total Service Charge including Arsenic Surcharges.**

| Billing Item | Present | Company Original Proposal | | | Magruder Proposal | | |
|---|---|---|---|---|---|---|---|
| | | Charge | Change | | | Change | |
| Cost of Service | $19.68 | $32.50 | + $12.82 | + 62.8% | $ 25.00 | + $5.32 | +25.4% |
| Average Usage | $ 49.46 | $85.44 | + $35.98 | +72.7% | $ 26.50 | - $22.96 | -53.6% |
| Total Bill | $ 69.14 | $117.94 | +$48.80 | + 70.6% | $ 51.50 | - $17.64 | -24.5% |

Average Water Usage = 11,797 gallons

There is also <u>second</u> Cost of Service charge that is indirectly in this rate case planned for Tubac to fund an arsenic treatment plant (Issue 2) with a capital cost of some $2.3 million. The

Basic Cost of Service charge could increase from the present $19.68 to Company's proposed $32.50, shown in Table 4. Add the Company's proposed Arsenic Service Charge of $25.98, for a proposed Total Cost of Service of $68.48 per month. It is doubtful if Cost of Service exceeds $68.48 in Arizona for residential customers. As shown in Table 5 in the next section, this total customer cost increase is 347% higher than the present. This is an excessive rate increase, beyond the customary rate increases usually approved by the Commission. The most fair and reasonable way for all water districts to above new, expensive and necessary capital improvements is through rate consolidation to eliminate unintended consequences for the smallest water districts. (*Ibid*, 18 and Table 5, 19)

**2.3 Conclusions.**

Same as Magruder Opening Brief, paragraph 2.3.

The large variation in the fixed Cost of Service charge must be smoothed out, so the Company can make all prudent capital expenses without causing violent perturbations to its customers. This will lead to a consolidation recommendation later. (*Ibid,* 21)

In summary, the proposed rate structures, other than Staff Alternative and mine, do NOT promote water conservation, in an Active Management Area, where future growth is limited based on the AMA requirements to maintain sustainability in water resources as required by the Santa Cruz Comprehensive Plan, Water Resources Element, where "water supplies are protected and conserved." (*Ibid,* 21)

Water conservation is necessary for a **fair and reasonable** rate structure. The evidence presented remains valid that support this issue. Water conservation and sustainment remain critical State of Arizona objectives and also is an objective of Arizona-American and the Commission. (*Ibid,* 21)

**2.4 Recommendations.**

To have water conservation as a significant driver of the volumetric water rate, the following are recommended:

1. That the lowest residential rate tiers by credited as a mechanism to provide low-income rates without additional administrative overhead. This should result in defining the first rate tier also as the "low-income" or the survival rate level.
2. That a minimum of ten tiers be used for all residential and commercial rate categories. This will require only an adjustment of "how" the revenue requirements will be distributed to the customer rate categories when higher users pay more, lower user pay less.
3. That all residential and commercial customers, with the same water connection size, have identical Cost of Service and be in the same rate categories that are designed to

account for the infrastructure required for service. This should reduce administrative tasks for the Company and make understanding rates easier.

4. That the Commission-determined fair and reasonable company's revenue will be collected and the resultant consumption structure must be revenue-neutral for the Company.
5. That the billing statements make obvious the rate per tier and where that monthly bill lies in the multi-tier structure. This is how the "price-breaks" can be observed and how much less water consumed is necessary to reach then next lower tier.
6. That the smallest residential and commercial rate tiers (at least the first several) identical. This will be advantageous to small businesses that the Company's schedules have shown to typically use less water than the comparable residential rate category.
7. That the fixed Cost of Service variations be minimal and leveled out across all rate payers in each rate category. This will also lead to consolidation of all fixed charges, across all water divisions, to equalize this "fixed" cost.

(*Ibid,* 21-22)

## Section 3

## ISSUE No. 2

## CAPITAL EXPENSES FOR THE TUBAC ARSENIC REMOVAL FACILITY

### 3.1 Summary of Issue No. 2

The Company proposed a $2,300,000 Arsenic Treatment Facility in Tubac to remove Arsenic to meet revised EPA minimums. The Company cost estimates are exceed the market casts for this facility. The Santa Cruz Valley Citizens Council, with the Company, submitted a request through Congresswoman Giffords for federal "stimulus" assistance for the funding of this arsenic removal facility for the 532 customers. If a federal grant is awarded, the facility cost will decrease; otherwise, the Tubac ratepayers would be charged for the resultant prudent costs. (Magruder Brief, 23)

The Company in coordination with the SCVCC has requested requesting federal stimulus assistance through the Arizona Water Infrastructure Facility. The Company stressed the proposed ACRM approach, contrary to rate consolidation issue, addressed by this party. (*Ibid*)

### 3.2 Reply to Post Hearing Opening Briefs.

#### 3.2.1 Arsenic Removal Treatment is Required.

Company Brief.

We must provide arsenic treatment for its Tubac Water Customers. (Company Brief, 52)

RUCO and Staff Briefs.

This issue is not discussed.

Magruder Reply.

The party agrees with this Company position and has always supported arsenic treatment. The "capital expenses for the Tubac Arsenic Treatment Removal Facility" is this issue. (Magruder Brief, 23)

Much earlier in this case, there was doubt as to the validity of the arsenic measurements; however, the Magruder Brief states, "This party has refrained from requesting an arsenic review by the EPA, as suspicions of anomalous readings now seem mute." (*Ibid*)

#### 3.2.2 Arsenic Cost Recovery Mechanism (ACRM) Approved in this Rate Case.

Company Brief.

The Company is currently designing an arsenic treatment facility that should be in service by summer 2010 and requesting the Commission approve ARCM for Tubac Water "essentially" identical to the ARCM previously applied in other Arizona-American water districts. The

Company stated Staff and RUCO support this request. (Company Brief, 52)

RUCO and Staff Briefs.

This issue is not discussed.

Magruder Brief.

The arsenic plant design has not been presented to local ratepayers, in terms of its features, benefits, costs, and architectural landscaping needs that may impact the environment. The Company brief in December 2008 said it would provide this information. (Magruder Brief, 23)

This construction project has not started, is outside the "test year" thus, and does not qualify for rate base treatment. The cost of this plant is unknown and the probability of actual availability of federal or state funds may not be known before completion of this case. (*Ibid*)

A developer's $1 million contribution for the facility is doubtful. (*Ibid,* 24)

The ACC-approved Arsenic Recovery Cost Mechanism (ARCM) process is planned. Costs will be deemed to be prudent before any Arsenic costs can be recovered from ratepayers. (*Ibid*)

Realistic costs of any arsenic treatment plant for Tubac are doubtful with respect to accuracy and validity compared to a similar capacity system next door. (*Ibid,* 25)

### 3.2.3 Cost of Service and Rate Design for Arsenic Treatment.

Company, RUCO and Staff Briefs.

This issue is not discussed.

Magruder Reply.

The impact of the proposed Arsenic charge on customer rates include the Arsenic Cost of Service and a volume usage charges shown in Table 5. It is obvious this is of major concern for the 532 customers in the Tubac servicer area. (*Ibid,* 24 and Table 7)

**Table 5. Impact of Arsenic Charges on Residential Bills.**

| Monthly Usage | Present Bill | AAWC Proposed Rates + Arsenic Treatment Charges (new bill) | **Total Percent Change with Arsenic costs included** |
|---|---|---|---|
| 5,000 gallons | $ 30.09 | $ 94.15 | **312.9%** |
| 10,000 gallons | $ 44.34 | $ 134.10 | **302.4%** |
| 15,000 gallons | $ 58.59 | $ 174.05 | **297.1%** |
| 20,000 gallons | $ 72.84 | $ 214.00 | **293.8%** |

There should never be any ARCM cases or any additional surcharges because they cause significant rate perturbations. All water districts are similar and periodically require major new capital equipment, all expensive. These asynchronous capital spikes level out if spread out across the company. Mr. Hebert's sworn documents clearly show it is patently unfair and not reasonable to have created a discriminatory funding ARCM. (*Ibid,* 25, original underlined)

The potential for federal or state grants or loans may reduce capital expenses and, under the present unconsolidated rate scheme, the severity of the ratepayer's arsenic basic service cost maybe reduced but not the monthly $3.15/1,000 gallon consumption costs. The Company is requesting a 300% rate increase with its proposed ARCM. That's unreasonable. (*Ibid*)

As discussed later, the Company's ARCM process is discriminatory and should not be considered as "reasonable and fair", and should be discarded for future arsenic plants. (*Ibid*)

No prudent decisions concerning the Tubac Arsenic Treatment Facility can be made at this time or during this case. (*Ibid,* 26)

### 3.2.4 Centralized Arsenic Treatment versus Point of Use /Point of Entry.

Company Brief.

The Company stated, "Magruder opposes it because he believes that a point-of-use system would be preferable." (Company Brief, 52)

A point-of-use system initially is less expensive, but more expensive in the long run. (*Ibid.*)

A central plant option treats all water used in the home, but the point-of-use option would treat only water provided for through a spigot at the kitchen sink. (*Ibid,* 52-53)

To ensure compliance, the Company would have to regularly enter every customer residence or business to test the systems and to replace filters. This would be a burden on the Company, but also on our customers. (*Ibid,* 53)

RUCO and Staff Briefs.

This issue is not discussed.

Magruder Reply.

There remains strong support in Tubac for the less costly Point of Use (POU) method of arsenic removal. The Company has yet to provide a convincing Trade-off Study to compare POU versus a "central plant" for this service area. It is reported 100 residences already have POU reverse osmosis systems installed. (Magruder Brief, 24)

The Company does not have experience with POU systems. The Company witness was not conversant with operational details of these systems. The POU systems were pointed out to be rather inexpensive, under several hundred dollars, but were usually used for one kitchen faucet. This witness said a typical home needs about 300 to 500 gallons of "arsenic-free" water a month because between 95% and 97% of residential water delivered would not be ingested by humans. This party questioned why should ALL of the water have arsenic removed when arsenic is not a health hazard for yard water, car wash water, clothes wash water or swimming pools. The witness was concerned about the amount of arsenic in water a human drinks when brushing teeth and showering. (*Ibid*)

This party introduced a Point of Entry (POE) version that provides arsenic-free water for all internal faucets, usually installed near a hot water tank that is more expensive, between $1,100 and $3,000. A POE system overcomes the Company's health concerns (*Ibid.*) but this concept appears foreign to this water company. (*Ibid*)

The Company would not recommend a POE/POU approach. (*Ibid,* 25)

The Company provided a weak defense for its opposition to use of reverse osmosis (RO) in POU or POE systems and continues to recommend a single-element arsenic filtration system for its customers. The much wider-range filtration in RO systems was not considered. The EPA order to remove arsenic is the Company's only concern. (*Ibid*, original underlined)

This party is concerned that longer-term water quality issues concerning other toxic, pharmaceuticals, and hazardous and harmful chemical and biological contaminates in our water may have higher human safety impacts than only arsenic removal. (*Ibid*)

The greater safety margins for the 300 to 500 gallons of water a month potentially ingested by humans, has led this party to now believe a POU or a POE system will be the best long-term solution for water quality. New homes should be plumbed for POE systems. My home was originally plumbed for a POE system over a dozen years ago at almost no additional cost. (*Ibid*)

### 3.3 Conclusions.

The Staff must assess total system capabilities when looking in the future, as the single-purpose capabilities of a dedicated arsenic treatment plant appear obsolete even before starting construction. (*Ibid*)

### 3.4 Recommendations.

Concerning the capital costs of an Arsenic Plant for Tubac, the following are recommended.

1. That no expenses for an Arsenic Treatment Facility for the Tubac Water District be approved in this case. (*Ibid*, 26)
2. That implementation of any ACRM stages or costs is not considered in these proceedings but in another when the supporting facts are known and reviewed. (*Ibid*)
3. That the Basis for ceasing ARCM is considered an issue in the Consolidated Rates, as a single capital project, such as this, is neither fair nor reasonable for a small water district. (*Ibid*)

   That consideration for POU and POE systems remain as viable alternatives for future water filtration. (*Ibid*)

## Section 4

## Issue No. 3

## RATE CONSOLIDATION FOR ALL WATER DISTRICTS

### 4.1 Summary of Issue No. 3

This party supports full rate and fee consolidations including having the Company, RUCO, and ACC Staff submit a single set of Consolidated Rate Schedules, Fees and Rules and Regulations, based on the rates being proposed by each as a later phase in the case for all five water districts and the next Arizona-American rate case all other water districts should be integrated within revised Consolidated Rates and Fees in order to have *fair and reasonable* rates throughout Arizona. (Magruder Brief, 24; 27-28)

In general, all RUCO, Staff and Company all support tiered rate structures and rate consolidation. There were no recommendations against consolidation; however, when and the level or degrees of consolidation are where differences lie. These differences will be the ultimate decision on the Rate Consolidation issue, in my opinion, with the most significant impact on ratepayers than any other issue in this Rate Case. (*Ibid*, 29, original underlined)

### 4.2 Reply to Post Hearing Closing Briefs.

#### 4.2.1 Long-Term Benefits of Consolidation to Customers, the Company, and Shareholders.

Company Brief.

Mr. Townsley testimony stressed the "long-term benefits to customers of consolidation for ratemaking purposes between Arizona-American districts." (Company Brief, 6)

The Company conditionally supports rate consolidation because of "improved rate case efficiency, improving ability to make needed capital investments in smaller districts without imposing burdensome rate increases, improving ability to acquire small troubled water systems, and a desire to bring the tariff structure of water and wastewater utilities more in line with those of other regulated utilities in Arizona, that all support consolidation on a philosophical basis." (*Ibid,* 49)

Mr. Herbert is a witness for AAWC and providing his excellent background shows he is one witness with Company-experience in this matter, and supports consolidation of all financial and operational aspects for all water districts. (Magruder Brief, 31)

RUCO Brief.

A completed and comprehensive consolidation analysis was performed by RUCO for all districts in question other than Paradise Valley. (RUCO Brief, 15)

This analysis resulted in a consolidated Service Charge of $9.59. As usual, the greatest reductions occur for the highest service charge, with less significant increases for those with the lowest service charge which is fairer than the present situation. (Magruder Brief, 31)

In an overall view, using $9.59 provides more "~~rate~~rate "relief" compared to rate "shock", which seems also to be fair and reasonable. Similarly, the proposed Company Service Charges to a Consolidated Service ~~Charge,~~Charge has more "rate "relief" occurs compared to rate "shock." (*Ibid*)

Staff Brief.

The Staff is "supportive of rate consolidation, where it is technically and financially feasible." (Staff Brief, 20)

The Staff did not perform a comprehensive consolidation rate analysis.

Magruder Reply.

This party fully agrees that all customers will definitely benefit with consolidation but for some their rates may increase; however, there are also numerous benefits to the Company as well as administrative costs, fewer tariff rates and associated filings, better company focus, equalization of existing disparities between water districts, lower rate case costs, so the Company can better focus on its customers' need and provide better service and lower overall costs. With reduced costs, shareholder benefits increase with higher dividends. (Magruder Brief, 25)

One-time costs for smaller districts would be absorbed in larger customer district with much less impact than the same one-time cost for a smaller district. There would be one rate case for these six water districts instead of six to thirteen cases now. Additional workloads for the Company, RUCO and ACC Staff would be avoided if only one rate case was being filed. (*Ibid*)

Due to fundamental differences between water and wastewater districts, it appears reasonable for the wastewater districts to be consolidated but separately from the others. (*Ibid*)

For an example of equalization of disparities between different water divisions, assume the following two water districts, using hypothetical numbers to show effects of consolidation is in Table 6. In this example, consolidating increased the Large District's rate by $0.48 and reduced the Tubac District rate by $19.52. Now, is consolidating "fair and reasonable" or not? In this Party's opinion, it is fair and reasonable. In addition to "cost of service" example, the same impacts would apply for the water volume rates. (*Ibid*, 26-27; Table 8, 28)

**Table 6. Example of Consolidation Impacts for a Large and a Small District.**

| Factor | | Tubac District (a) | | Large District (b) |
|---|---|---|---|---|
| 1. Number of customers | | 500 | | 20,000 |
| 2. Service Charge | | $40.00 | | $20.00 |
| 3. Monthly Revenue (fixed) | (1 x 2) | $20,000 | | $400,000 |
| | | | **Consolidated** | |
| 4. Number of Customers | (1a + 1b) | | 20,500 | |

| | | | |
|---|---|---|---|
| 5. Service Charge (3a + 3b)/(1a + 1b) | | $20.48 | |
| 6. Monthly Revenue (fixed) (4 x 5) | | $420,000 | |

In the recent UNS Electric rate case, the Mohave and Santa Cruz County residential and small commercial rates were finally consolidated after five decades. The smaller Santa Cruz County saw an 8% reduction in small business rates while Mohave County rates increased about 2% based just on consolidating rates in each rate category. (*Ibid*)

### 4.2.2 Specific Impacts on Service Charges due to Consolidation.

Company Brief.

Mr. Townsley testimony stressed there are "long-term benefits to customers of consolidation for ratemaking purposes between Arizona-American districts." (Company Brief, 6)

The Company consolidation analysis used Proposed rates, and several different water districts, including some that are not included in this rate case. Still, this gives a picture of relationships using proposed rates. (Magruder Brief, 34)

The Company's determined consolidated service charge was $15.59 for the proposed rates. We see significant decreases for Tubac, Paradise Valley and Havasu, and minor increases for Agua Fria and Sun City West and Mohave Water in Table 7. (*Ibid,* and Table 11, 33)

**Table 7. Changes due to Consolidation on Proposed Service Charges.**

| Water District | Change | Difference in Present Rates | Calculation (Consolidated minus Present) |
|---|---|---|---|
| Mohave | Increase | $ + 3.59 | (15.59-12.00 = +3.59) |
| Sun City West | Increase | $ + 0.59 | (15.59-15.00 = +0.59) |
| Agua Fria | Increase | $ + 0.59 | (15.59-15.00 = +0.59} |
| Havasu | Decrease | $ - 12.41 | (15.59-28.00 = -12.41) |
| Paradise Valley | Decrease | $ - 12.41 | (15.59-28.00 = -12.41) |
| Tubac | Decrease | $ - 16.91 | (15.59-32.50 = -16.91) |

RUCO Brief.

A completed and comprehensive consolidation analysis was performed by RUCO for all the districts in question. (RUCO Brief, 15, Magruder Brief, 32-36)

The RUCO analysis resulted in a consolidated Service Charge of $9.59 for five districts. Table 8 shows in the inequity in service charges that now exist because the service charge cost are not consolidated, with unfair discrimination on customers who receive the same product. As usual, the greatest reductions occur for the highest service charge, with less significant increases for those with the lowest service charge. (Magruder Brief, 31 and Table 10, 33)

**Table 8. Changes due to Consolidation on the Existing Service Charges.**

| Water District | Change | Difference in Present Rates | Calculation (Consolidated minus Present) |
|---|---|---|---|
| Sun City West | Increase | $ + 3.72 | (9.59 - 5.87 = +3.72) |
| Mohave | Increase | $ + 0.84 | (9.59 - 8.75 = +0.84) |
| Agua Fria | Increase | $ + 0.51 | (9.59 - 9.08 = +0.51) |
| Paradise Valley | Increase | $ + 0.07 | (9.59 - 9.65 = +0.07) |

| | | | |
|---|---|---|---|
| Havasu | Decrease | $ - 2.19 | (9.59 - 11.87 = -2.19) |
| Tubac | Decrease | $ - 10.09 | (9.59 - 19.68 = -10.09) |

When comparing Present to the Consolidated Service Charge, one sees the present $9.59 or proposed $15.59, consolidation provides more rate "relief" compared to rate "shock". This is fair and reasonable. Similarly, comparison of the proposed Company to a Consolidated Service Charge, again, more rate "relief" occurs compared to rate "shock." (*Ibid,* 32)

Staff Brief.

The Staff did not calculate a comprehensive Service Charge.

Magruder Reply.

When using the Proposed Consolidate Service Charge, the change for those with lowest rates is much less significant than for those with the highest proposed service charges.

Table 9 shows Basic Service Charges with the present rates and proposed RUCO, Staff and Company proposed rates. These vary from $5.87 to $ 32.50. (*Ibid,* 32 and Table 9)

Mr. Hebert (Arizona-American witness) stated the highest rates see the greater decreases and the lowest rates, the smaller increases when consolidating is borne out here. (*Ibid,* 31)

**Table 9. Consolidated and Unconsolidated Basic Service Charges**
(Residential 5/8 and 3/4-inch Meters)

| Consolidated Service Charge (RUCO) | AAWC Present Basic Service Charge | | | | | |
|---|---|---|---|---|---|---|
| | Agua Fria | Sun City West | Tubac | Havasu | Mohave Water | Paradise Valley[1] |
| **$ 9.59** | **$ 9.08** | **$ 5.87** | **$ 19.68** | **$ 11.78** | **$ 8.75** | **$ 9.65** |
| | **RUCO Proposed Basic Service Charge** | | | | | |
| | **$ 11.87** | **$ 13.81** | **$ 29.34** | **$ 25.66** | **$ 10.30** | **$ 26.68** |

| Consolidated Service Charge (AAWC) | AAWC Proposed Basic Service Charge | | | | | |
|---|---|---|---|---|---|---|
| | Agua Fria | Sun City West | Tubac | Havasu | Mohave Water | Paradise Valley |
| **$ 15.59** | **$ 15.00** | **$ 15.00** | **$ 32.50** | **$ 28.00** | **$ 12.00** | **$28.00** |

| **Consolidated Service Charge (ACC Staff)** | **ACC Staff Proposed Basic Service Charge** | | | | | |
|---|---|---|---|---|---|---|
| | Agua Fria | Sun City West | Tubac | Havasu | Mohave Water | Paradise Valley |
| Not calculated | **$ 14.55** | **$ 15.30** | **$ 28.73** | **$ 24.54** | **$ 9.10** | **$ 28.00** |

### 4.2.3 Specific Impacts on Consumption Rate Charges due to Consolidation.

Company and RUCO Briefs.

The Company and RUCO did not offer any consolidated consumption rates in its Brief for the Final Schedules but did in earlier testimonies.

Staff Brief.

The Staff did not calculate consolidated consumption charges.

Magruder Reply.

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[1] Final Schedules for the Company, ACC Staff, RUCO and Magruder combined the present Paradise Valley 5/8 and 3/4-inch rate categories into one, which is simulated by averaging herein.

RUCO's Mr. Moore consolidated the commodity (volumetric) usage charges by determining a common three-tier rates for residential customers (5/8 & 3/4-inch) and two-tiers for all other customer categories. Table 10 compares this residential rate category. (Magruder Brief, 33; Table 12, 34)

**Table 10. Consolidated and Unconsolidated Existing Commodity Charges.**
(Residential 5/8 and 3/4-inch meters)

| Commodity Usage (at $/1000 gallons) | AAWC Present Rate Design | | | | | |
|---|---|---|---|---|---|---|
| | **RUCO Consolidated Rate** | Agua Fria | Sun City West | Tubac | Havasu | Mohave Water |
| First 4,000 gals | **$1.2443** | $1.5398 | $1.3092 | $1.89 | $1.6802 | $0.85 |
| Next 10,000 gals. | **$2.0757** | $2.2198 | $1.7442 | $2.85 | $2.1852 | $1.30 |
| Over 14,000 gals. | **$2.3270** | $2.6468 | $2.0102 | $3.41 | $2.5000 | $1.50 |

Again, *the water division with the highest rates received the greatest decrease when consolidated, and the water division with the lowest rates the highest rate increases*. (*Ibid,* 34)

The Company also computed a consolidation scenario, with different assumptions when compared to RUCO's analysis. The Company's analysis used Proposed rate, and different water districts, including some not included in this rate case. Still, this gives a picture of relationships using the Company's proposed rates. (*Ibid*)

Table 11 shows consolidated commodity rates compared to the proposed Company's rates; however, without considering the Final Schedules. Again, the *water districts with the highest commodity rates, received the greatest rate reductions, while those with the lowest rates, the smallest rate increases*. (*Ibid*)

It is not feasible to directly compare these "consolidation" analyses. Mr. Moore comprehensive consolidation used <u>present</u> rates, excluded Paradise Valley, and derived common three-tier commodity blocks, to equalize Company return with the Test Year. (*Ibid*, 35)

**Table 11. Consolidated and Unconsolidated Proposed Commodity Charges.**
(Residential 5/8 and 3/4-inch meters)

| Company's Proposed Rate Design | | | | | | | |
|---|---|---|---|---|---|---|---|
| Commodity Usage Blocks (at $/1000 gallons) | **Company's Consolidated Rates** | Agua Fria | Sun City West | Tubac | Havasu Water | Mohave Water | Paradise Valley |
| **First 4,000** | **$1.500** | $2.926 | $2.880 | $3.780 | $4.033 | $1.471 | $1.288 |
| 4,001-10,000 | | $3.463 | | | | $1.625 | |
| **4,001-13,000** | **$3.463** | | | | $4.196 | | |
| 4,001-15,000 | | | $3.171 | | | | |
| 4,001-20,000 | | | | $4.850 | | | $2.233 |
| Over 10,001 | | | | | | $1.744 | |
| **Over 13,001** | **$3.670** | | | | $4.555 | | |
| Over 14,001 | | | | | | | |
| Over 15,001 | | | $3.413 | | | | |
| Over 20,001 | | | | $4.950 | | | |
| 20,001-65,000 | | | | | | | $2.796 |
| 65,001-125,000 | | | | | | | $3.359 |
| Over 125,001 | | | | | | | $3.879 |

The Company's "typical" Consolidated Bills for residential customers are in Table 12 for the Company's proposed rates, different water companies, and other assumptions that make this analysis not suitable to make any decisions in this rate case because it is incomplete and needs correction to reflect the current proposed rates. (*Ibid*; Tables 13 and 14, 35)

**Table 12. Consolidated Proposed Impacts for Typical Residential Bills and Total Revenue.**

| Water District | Typical Bill | Proposed Changes WITHOUT Consolidated Rates | Total Revenue |
|---|---|---|---|
| Tubac | $41.01 | +47.13% rate INCREASE | $0.3 million |
| Havasu | $35.85 | +42.90% rate INCREASE | $0.6 million |
| Mohave | $31.77 | +37.22% rate INCREASE | $1.7 million |
| Agua Fria | $30.09 | +17.75% rate INCREASE | $3.5 million |
| Paradise Valley | $66.94 | +2.95% rate INCREASE | $0.3 million |
| Sun City West | $28.35 | -15.69% rate DECREASE | $1.3 million |
| Water Districts in the Company's Analysis that are ***NOT*** in this rate case. | | | |
| Sun City | $32.26 | +136.00% rate INCREASE | $8.4 million |
| Anthem | $34.15 | +47.74% rate INCREASE | $44.6 million |

The variety of "blocks" in Table 11 show how dysfunctional the existing rate and proposed rate schedules are for this Company. There should be only one block structure for all water districts. (*Ibid,* 36)

First, there is no logic when setting the limits for the rate blocks. The distribution of the water usage is a non-Gaussian (or normal) and more like a chi-squared ($X^2$) distribution, with a fast rising peak closer to zero and a long tail. A chi-squared distribution has its mean or cumulative 50% distribution nearer to the origin, thus when an average customer consumes between 7,500

to 12,000 gallons. The rate structure must have cost "signals" for those near-mean usage customers. (*Ibid*)

Second, second tiers start at 3,001 or 4,001 gallons to 10,000, 13,000, 15,000, and 20,000 gallons. The range for this "second" tier extends from 3,000 to 14,000 gallons, too wide and challenging for a consumer to see the price signal to reach (or reduce demand) the first tier. The chi-squared tail extends for tens to hundreds of thousands gallons with price tiers only in the Paradise Valley after 20,001 gallons, with the last starting at 125,000 gallons. (*Ibid*)

Third, the Company's Consolidated Rate second tier is 9,000 gallons wide. It may be divided to make obvious and reachable blocks for customers to lower water bills by conservation. (*Ibid*)

Fourth, looking at Table 11, one sees 13 different tiers used by six water divisions for the same rate category. I proposed a standard 4,000-gallon blocks in the residential and small commercial rate categories. (*Ibid*)

Furthermore, all larger residential and commercial commodity rate categories have just two tiers. Many small commercial (5/8 and 3/4-inch), such as in the Tubac district, have very similar demand demands (with a lower average) than the residential counterparts. These commercial categories should parallel the residential rate tiers. Multiple tier blocks for all other rate categories should be in the resultant tariff from this rate case. Just like the residential category that is discussed extensively, commercial enterprises can and will always look for ways to lower rates, IF THEY CAN, to a lower tier. As the present and proposed rate structure is now constructed with only two tiers, reaching the first tier rates is nearly impossible unless your consumption is just over the second tier break point. This is *utterly useless*. (*Ibid*)

At least five tiers for larger meters is recommended, with two breakpoints below the chi-squared mean for example near the 35% and 45% points, the third at 5% past the mean (55%), and fourth and fifth, near the 65% and 80% points on the tail. The additional breakpoints on the tail will provide significantly more revenue to the Company in Exhibit M-4. (*Ibid*)

### 4.2.4 Consolidation of Miscellaneous Charges and Fees.

Company, RUCO, and Staff Briefs.

The Company, RUCO and Staff Brief did not discuss miscellaneous charges and fees in their Briefs; however, the Final Schedules presented various charges and fees for the different water districts. Consolidation of these fees and charges was not discussed.

None of these charges and fees ~~appear~~appears isolated by water district; however, the Company is using different rates/fees for the same service at different water districts. If nothing else happens in this rate case concerning consolidation, this is the easiest consolidation step. (*Ibid, 37*)

Magruder Reply.

No standards are used for miscellaneous charges and rates, with significant differences between charges for the same service in different water districts. (Magruder Brief, 19)

Miscellaneous customer costs that should be included and consolidated in this rate case are in Table 13. (*Ibid* and Table 6, 19-20)

It is probable that new water lines will be lengthy in rural areas. This party objects to having existing customers funding ANY such developer's expenses. New customers must fund new development, and not today's ratepayers, for the actual cost or line extensions and meters. Service Line and Meter Installation Charges must also be borne by new customers. (*Ibid*)

Meter Test and Re-reading Meter (when correct) need to account for higher vehicle fuel costs, thus these were increased. Also increased were the cost for a check without specific funds (NSF) to $30.00, a more commonly used fee. The Late Fee charge is raised to a simple 3.0% per month (36.0% APR), the maximum permissible interest rate. The Deferred Payment Financing fee at 1.5% per month (18.0% APR) is half of the Late Fee charge. To obtain deferred financing the ratepayer has committed to makeup unpaid bills to the Company and a lower Deferred Payment Financing fee is fair and reasonable. This could help the Company collect its fees and charges by discouraging higher costs for non-payment. (*Ibid*, 20; Table 6, 19-20)

**Table 13. Present, Proposed, and a Standard for Miscellaneous Charges and Fees.**

| Miscellaneous Customer Cost | Company's | | **Magruder Proposed Charge** | Variations in other water districts' charges and fees (present and proposed) including Staff and RUCO |
|---|---|---|---|---|
| | Present Charge | Proposed Charge | | |
| Establish, Re-establish, Re-connect Fee<br>(Regular hours)<br>(Off hours) | $ 30.00<br>$ 40.00 | $ 30.00<br>$ 40.00 | **$ 30.00**<br>**$ 60.00** | $ 20 to $4 0<br>$ 20 to $ 60 |
| Water Meter Test (if correct) | $ 10.00 | $ 10.00 | **$ 80.00** | $10 to $81 |
| Meter Re-read (if correct) | $ 5.00 | $ 5.00 | **$ 20.00** | $ 5 to $25 |
| Move Customer Meter | NA | NA | **Actual Cost** | NA or Actual Cost |
| Non-Sufficient Funds Check Charge | $ 10.00 | $ 10.00 | **$ 30.00** | $10 to $25 |
| Late Fee Charge | 1.5%/ month | 1.5%/ month | **3.0% /month** | NA to 1.5%/ month |
| Deferred Payment Finance Fee | NA | NA | **1.5% /month** | NA to 1.5% /month |
| Residential Deposit | 2 x average bill | | | 2 x average bill |
| Non-Residential Deposit | 2.5 x average bill | | | 2.5 x average bill |
| Deposit Required (residential or commercial), Interest on Deposit | In accordance with ACC Rule 14-2-403(B) | | | |
| Service Line Charge (Difference based on size of line) | $130 to $6,120 | $156 to $830, Actual | **Actual Cost** | $370 to $1,620 to actual cost |
| Meter Installation Charge (Difference based on size of line) | $370 to $1,630 | $370 to $1,890, Actual | **Actual Cost** | $130 to $6,130 to actual costs (plus $120 for AMR) |

Specific areas that should be consolidated include:

1. General & Administrative (believed to have been completed)
2. Cost of Service and Volumetric Charges with more and standard tiers deployed
3. Arsenic treatment costs (service and volumetric) included in 2 above
4. Taxes, including social security and Medicare, and other Rate Base Costs
5. Service Line and Meter Installation Charge (change all to "actual cost")
6. Establish, Re-establish, and Re-connect fees during regular and off hours
7. Water Meter Test, (if correct) and Re-read the Meter (that is good)
8. Non-Sufficient Funds to check charges and Late fees, Deferred Payment Finance Charge, Residential and Non-Residential Deposit Interest on Deposits (*Ibid, 37)*

**4.2.5 Consolidation of Rules and Regulations.**

Company, RUCO and Staff Briefs.

There were no comments on Rules and Regulations in any of these Briefs.

Magruder Reply.

The Company's Rules and Regulations (R&Rs), submitted, as a part of this rate case, should be consolidated. In respond to a Magruder Data Request, these R&Rs have not been translated into Spanish. (Magruder Brief, 28)

**4.2.6 Impact of White Tanks Plant on Consolidation.**

Company Brief.

The Company's Brief argues that its White Tanks Plant proposal is "fair" and "will mitigate rate shock and enable rate consolidation in the near future." (Company Brief at 19)

The Company continues that if its White Tanks Plant proposal ~~is~~were not approved, it would have to file another rate case to put "the entire White Tanks Plant in rate base." (Company Brief at 19)

The Company also uses the ACC Staff testimony by Mr. Becker who, under usual conditions, would support such a request in the next Agua Fria district rate case. (Company Brief at 19)

The Company concludes that this alternative would result in a "significant future rate increase for Agua Fria customers" and "throw off the consolidation timeline" (see below) (Company at 20)

RUCO Brief.

In summary, RUCO recommends the "Commission should reject the Company's proposal... associated with the White Tank plant in ~~ratebase~~rate base." (RUCO Brief at 4)

Staff Brief.

"The Commission should reject the Company's request to include CWIP in rate base in this case and any associated related adjustments to increase depreciation and property taxes related to inclusion of CWIP in rate base should also be rejected." (Staff Brief at 7)

Magruder Reply.

It issue exists because the rates are NOT consolidated and as a result will be unfair, no matter how determined without consolidation, to the ratepayers in Agua Fria water district. This case can be described as a global "rate shock" due to the extraordinary rate increases proposed by all but this party. (Magruder Brief, 41)

The issue of "when" to include this project should be in accordance with normal rate case procedures with consolidated rates. Since we have multiple and different sized water districts, any capital expense perturbation is unfair to the smaller division, as shown in Table 8. (*Ibid*, 26; Table 8, 29)

This party agrees with the Company on this issue this is unfair to the Agua Fria ratepayers. Only after it is operational should this plant's cost go into a Consolidated rate base in order to be fair to all customers, shareholders, and the Company when the other Arizona-American water districts are integrated into Consolidated Rates and Fees. The prudently assessed impacts of the White Tanks, like all capital projects, must be spread across all ratepayers in a Consolidated ~~Ratebase~~Rate base, as just to those in Agua Fria water district is unfair and not reasonable.

### 4.2.7 Was adequate notice provided in this case to proceed with Consolidation?

Company and RUCO Briefs.

This issue was not addressed.

Staff Brief.

Staff was concerned that notice in the instant case was not adequate to notify affected ratepayers, particularly those customers of the districts that were not included, that a rate increase (or decrease) was possible. (Staff Brief, 20)

Magruder Reply.

The Staff witness states "proper notice be given to customers affected by a rate application" in accordance with Arizona Administrative Code R14-2-105(A) and that this notice has not been given to "all the Company's customers". Staff recommends, "~~rate~~Rate consolidation can not be undertaken in this docket." Further, he states "due process concerns require proper notice be given." (Magruder Brief, 37)

This Rate Case Procedural Order required Notice of these hearing for this case be placed in newspapers and in billing statement for all customers involved in this rate case. This includes customers of all six water districts and one wastewater district that are impacted by this case and excludes other Arizona-American two water districts and four wastewater district customers not impacted by this case. Consolidation for the one-wastewater district has not been considered. Therefore, only the six water districts are being considered for consolidation and all

their customers were properly "noticed" in accordance with the ACC Regulations. The Company also has reported compliance with the Rate Case Procedural Order. (*Ibid*)

This notice included: "The Commission is not bound by the proposals made by Arizona-American, Staff, or any intervenors; therefore, the final rates approved by the Commission may be higher or lower than the rates requested by Arizona-American." (*Ibid*, 38-39)

It appears obvious the Commission may make any changes it deems appropriate and legal as the final result of any and all rate cases. In my opinion, there is absolutely nothing is this notice that would "prohibit" consolidation of these six water districts in THIS rate case. Further, A.A.C. regulations R14-2-105(A) have been met. Therefore, there is no reason why consolidation cannot be implemented based on Notice for these six water companies, without additional "Notice". (*Ibid*, 39)

In this party's opinion, rate consolidation of the six water districts in this case is within the Notice requirements of the A.A.C. and other statutes. All other Company water districts have never been a consideration by this party.

### 4.2.8 All Urge Consolidation to Proceed with Caution.

Company Brief.

Mr. Townsley supports consolidation "as long at consolidation does not cause further financial harm to the Company." (Company Brief, 6)

He also has some concerns with rate consolidation. The practicalities of district consolidation present significant challenges to both the Commission and Arizona-American. For instance, average customer water bills across Arizona-American's systems range from about $12 per month in Sun City to about $70 in Paradise Valley." Some of these "differences are due to net-plant investment and O&M expense per customer between districts. Proposals for the short term are likely to cause significant public and political consternation. Arizona-American will not support consolidation if the result were to delay rate relief, or otherwise harm the Company." (*Ibid,* 49-50)

RUCO Brief.

RUCO "believes the batter approach would be to consider the [consolidation] issue when all of the districts are the subject of a rate case. This would provide the Commission with the opportunity to consider all the factors necessary to make the best decision. These factors include, but are not limited to, the operational and financial information of all the Districts, the interconnectivity of the systems, and the financial impact on each system. It would also mitigate some of the unintended consequences that will result should the Commission make the decision at this time." (RUCO Brief at 15-16)

Staff Brief.

The Staff feels rate consolidation is a complex issue that has both public and policy ramifications and recommends that before undertaking rate consolidation, the Commission establish certain criteria regarding public health and safety, proximity, economics of scale and rate shock. (Staff Brief, 20)

For Arizona-American, with differing rates among its districts, rates for some customers will decrease while rates for others will increase for others. (*Ibid*)

Before undertaking consolidation, the Company would have to undertake significant public outreach to educate its customers on the issue, something that did not happen within the confines of the instant case. (*Ibid*)

Staff recommends that the Commission carefully consider all aspects and impacts that could result from consolidation in an effort to avoid unintended consequences. (*Ibid*)

Staff testimony addressed areas where work remains before rate consolidation, including:

1. How to deal with different number of, and break point for, rate tiers across the districts.
2. How to account for differing uses of water for irrigation in different districts, particularly in the Paradise Valley Water District.
3. Whether to consolidate commercial rates at the same time.
4. Whether returns on customer classes as a result of cost of service studies are or should be the same in the different districts.
5. How to maximize public input, including whether to hold workshops.
6. How to educate the public about the pros and cons of rate consolidation.
7. How Staff, RUCO, and other parties would participate in the public process.
8. Whether to flash cut to consolidated rates or to phase them in.
9. Whether to consolidate sewer rates at the same time that water rates are consolidated.
10. What economics of scale would result from ~~consolidation.~~consolidation? (Company Brief, 50)

These criteria are sound and should be evaluated during a consolidation application review. (*Ibid,* 40)

Magruder Reply.

This party agrees but some of these concerns have been overtaken by events. Going through all of these from Company, RUCO to Staff, we see the following:

a. Financial harm. First, rate structure variations are all revenue neutral. Rate consolidation should not impact revenue and do financial harm.
b. Average water bill differences. These differences are mild when compared to the variations in rates being proposed in this case, see Table 1 at 10, Table 2 at 11, Tables

3 and 4 at 13, Table 5 at 16, Table 7 at 21, Tables 8 and 9 at 22, Table 10 at 23, Tables 11 and 12 at 24, and Table 13 at 26 that show much more significant variations without any rationale in this case.

c. Net plant investment differences. These are due to many factors, but as indicated by Mr. Herbert, consolidation is the only solution to smooth out high swings in rates. "The cost of specific programs should be shared by all customers rather than burdening those of the affected area. Rate increases will be more stable and major increases in specific tariff groups will be avoided. "(Magruder Brief, 29)

d. O&M expense differences. These are due to many factors, but as indicated by Mr. Herbert, consolidation is the only solution to smooth out high swings in rates. (Magruder Brief, 29)

e. Public and political consternation. This company presently has a terrible reputation by its ~~customers,~~customers; mostly because of the extremely high rate changes requested in its rate cases. Personally, I doubt if it could be worse, so concerns about "consternation" are understandable but in reality mute. Therefore, since consolidation will "smooth out" and "equalize" the bothersome peaks and valleys ratepayers now perceive, there could be no better time than the present to consolidate from this view point. (*Ibid*, 40)

f. Rate relief timing. This company perceives that "any" delay in obtaining the increased rates requested in this case will have terrible consequences involving reduced spending on capital projects, personnel reductions, and equipment maintenance due to losing parent company and shareholder support. This case has taken over a year so far with new rates not expected prior to September 2009. In my opinion, a few additional months to really settle the unjust and unfair rates now being implemented are worth the longer-term benefits for shareholders, customers, company integrated work, and regulatory agencies.

g. Consolidate when all of the districts are the subjects of a rate case. At present, 5 of 7 water districts are represented, required Company revenues and test year expenses adjudicated, and necessary financial basis determined, a requirement prior to determine how to collect this revenue. Rate consolidation is revenue neutral. To expend hundreds of thousands of dollars in a future rate case, manpower that has been used in this case, and the necessary audits at some future date, is not cost-effective and delays ~~be~~are benefits of consolidation. There is no need to have all 7 water districts in the same rate case to consolidate these 5 districts. The proposed result will be one large water district (of the 5 herein) that will consolidate with the remaining two later. Three entities will be in the second rate case, not 7, again with consolidation benefits already incorporated for

the original 5 districts. Thus, the addition of two smaller districts, as shown time and time again in my analyses, to the larger district will result in less impacts on the larger district and greater on the smaller ones, as they converge into one integrated water company. The cost of 7 rate cases is greater than to consolidate 3 rate cases.

h. All districts in one case provide an opportunity to consider all the factors necessary to make the best decision. By having a two-step consolidation approach, as just explained above, does not mean nor imply "all" operational and financial factors are considered but over two cases (this one and one for the remaining districts), not in one larger future and much more expensive rate case.

i. Consideration of interconnectivity of systems is necessary for consolidation. This involves expenses of connecting to different water districts but is not an essential element of rate consolidation. Both the Company's Mr. Hebert and Staff agree that interconnectivity is NOT required for consolidation, but is a nice to have feature, if possible. (Magruder Brief, 31 and 39)

j. Unintended consequences of consolidation. First, all decisions may have such consequences; however, the Staff has listed at least 10 such considerations that are discussed below. (Company Brief at 50)

k. Commission ~~establishe~~establishes certain criteria regarding public health and safety, proximity, and economics of scale and rate shock. Pubic health and safety criteria will not change with consolidation. Proximity, as indicated in "I" above, is not a factor in consolidating. Economics of scale is a benefit for many parties, should be a positive outcome; however, having the Commission pre-determine this as a "criteria" for consolidation will not be known until after the consolidation plan is finished. Rate shock occurred long ago, ~~then~~and then the Company submitted its original and revised applications. Any ~~customer~~customer, who has a proposed rate increase of over 15%, will have rate shock, at least 80% of the customers in these five districts. Only through rate consolidation will "rate shock" be diminished.

l. Some customers will have rate increases and others decrease with consolidation. As shown, the degree of change is related to the customer base size. Larger divisions will have smaller changes, smaller divisions larger changes, with the resultant changes more beneficial for the smaller divisions as rates become smoother for all.

m. Company needs to take significant public outreach prior to consolidation. The public is presently furious and ~~ill-informed~~ill informed about utility rates, not only water, but communications, electric, and gas rate structures. The terms used for each are all different and very confusing as additional "mechanisms" and surcharges only add

confusion. Very few understand the fundamentals of the process and rate determination mechanisms used by the Commission, as this is my fifth rate case, in a continuum of learning, I'm in the fifth grade with graduation a long time away. Extensive public outreach has problems in that some small factor maybe blown out of proportion. For example, the Magruder proposed rates will decrease the majority of these on Sun City West who are the loudest objectors to consolidation and rate tiers I have proposed. Even after explaining, during breaks in this case, understanding that the resultant is lower rates is not understood. Facts need to be published in billing statements that are clear, understandable showing impacts. Educating the public to accept change is challenging and may never be effective.

n. Number of breakpoints and tiers (1). This issue is the heart of consolidation. Many tiers are necessary due to varying demands. Price signals are required. Consumption levels in each district are drivers. As accomplished by RUCO, this can be developed in a fair and reasonable manner.

o. Irrigation water differences (2). Arizona-American is a water company, not an agriculture irrigation district, and as such, is required to deliver safe, potable water. Irrigation water should not be a separate rate category unless used for agriculture, but integrated in the residential/commercial rate categories. The same goes for "fire" water.

p. Consolidate residential and commercial at the same time (3). This party feels that the company's revenue requires both to ~~the~~ be consolidated at the same time. In fact, there many ~~beare~~ some trades between these two rate classes when consolidating rates.

q. Cost of Service at water district or consolidated level (4). As strongly advocated by the Company's rate structure witness, Mr. Herbert, cost of service must be integrated across the entire customer base, not for each small, individual entity, in order to be fair and reasonable. (Magruder Brief, 31)

r. Maximize public input and decide to hold workshops (5). This is a Company decision but will add to rate case costs. See "m" above.

s. Educate the public about the pros and cons of rate consolidation (6). In my opinion, only as small number of the public will understand this, as stated in "m" above.

t. Participation of Staff, RUCO and other parties in the pubic process (7). Unless prohibited by statue, all ~~knowledgable~~knowledgeable-parties should participate.

u. Flash-cut or phase in consolidated rates (8). As is clear in Mr. Herbert's writing, without consolidation, rates are NOT FAIR. Fairness requires remediation of unfair, unconsolidated rates. The multi-phase approach took 50-years for a recent electric rate consolidate, with a half-century of unfair rates.

v. Consolidate sewage and water together or separately (9). As these are different businesses, separate consolidation cases are appropriate.

w. Economics of Scale due to Consolidation (10). See "k" above.

**4.2.9 When and How to Consolidate.**

Company Brief.

Because of the complexities and potential for unintended consequences, the Company's position is that rate consolidation must be analyzed though a proceeding focusing solely on consolidation issues. (Company Brief, 51)

The Company intends to do the following in a separate and nearly parallel process with its Next Rate Case:

1. Open a separate Rate Consolidation Docket including all of its districts focusing solely on rate consolidation.
2. Request the Commission to re-open this Rate Case and the Next Rate Case under A.R.S §40-252, solely for the purpose of re-examining the rate design consistent with resolution of the Rate Consolidation Docket.
3. If a new rate design ~~is~~were ordered as part of the Rate Case Docket, the A.R.S. §40-252 procedure would allow the final order in this 2008 Rate Case and the final order in the Next Rate Case to be amended solely to adjust rate design.
4. The Commission must rely on the summation of the individual districts' revenue requirements found in the 2008 Rate Case Order and in the Next Rate Case Decision as a basis for new rate design consolidating rates in some or all districts.
5. This procedure would allow the Commission to fully examine Rate Consolidation as a basis for a new rate design consolidating rates in some or all districts.
6. This procedure would allow the Commission to fully examine Rate Consolidation while at the same time allow the Company to implement new rates in each of its divisions on an unconsolidated basis, necessary in the interim to ensure the Company's continued financial health and stability.
7. The Company is willing to support the above actions as best as possible in a manner consistent with completion of the Next Rate Case and Rate Consolidation by December 2010. However, the Company can only control the timing of initial application filings; it has only limited influence on subsequent procedural dates. (Company Brief, 51)

RUCO Brief.

In this case, the Commission is considering only 7 of the 13 water and wastewater districts. From RUCO's perspective, this does not make sense to consider only 7 districts at this time.

RUCO believes the better approach would be to consider the issue when all districts are the ~~subject~~subjects of a rate case to provide the Commission the opportunity to consider all the factors necessary to make the best decision. (RUCO Brief, 15-16)

Staff Brief.

The Staff recommendation in Mr. Abinah's testimony is that

> "The Commission order Arizona-American, in its next rate case, to propose detailed rate consolidation and/or system interconnection plans where the Company believes it is technically and financially feasible." (Magruder Brief, 40)

Staff defines "rate consolidation", also known as Single Tariff Prices (STP) as

> "The use of a unified rate structure for multiple utility systems that are owned and operated by a single utility, but that may not be contiguous or physically interconnected." (*Ibid*)

Similar to the Company's Mr. Herbert, we see Mr. Abinah support consolidation even if the water districts are not contiguous or interconnected. In fact, Staff feels that rate consolidation or STP even when not physically interconnected. (*Ibid*)

During Mr. Abinah's oral testimony he suggested that a 12 to 18 month plan be developed leading toward consolidation in one rate case for all districts. Under ~~cross examination~~cross-examination, it appears this is a bit optimistic as this party urged not to spend 50 years consolidate his electric company. He is and rightfully concerned about unintended consequences including analysis of these factors during a consolidation application review, to include as minimum criteria:

a. Public health and safety.
b. Proximity and location.
c. Community of interest.
d. Economies of scale/rate case expense.
e. Price shock and mitigation including a low income program
f. Public policy.
g. Other jurisdictions and municipalities. (Magruder Brief, 39-40)

[These factors were discussed above]

Magruder Reply.

In general, this party supports the Company's position in its Brief.

Specific areas that should be consolidated include:

1. General & Administrative (completed)
2. Cost of Service and Volumetric Charges so that more tiers be deployed
3. Arsenic treatment costs
4. Taxes, including social security and Medicare
5. Service Line and Meter Installation Charges (change all to "actual cost")
6. Establish, Re-establish, and re-connect fees during regular and off hours

7. Water Meter Test (if correct) and Re-read the Meter (that is good)

8. Miscellaneous Charges and Fees including Non-Sufficient Funds to check charges and Late fees, Deferred Payment Finance Charge, Residential and Non-Residential Deposit Interest on Deposits. (Magruder Brief, 37)

In addition, the Company's Rules and Regulations (R&Rs), submitted as part of this rate case, should be consolidated into one document, and also made available in Spanish. (*Ibid*)

The published works by the Company's witness, Mr. Paul Herbert, should be used as a foundation for consolidation. (*Ibid,* ¶4.2.3.1, 29-31)

This is not a single or a selected group of water districts issue. All water districts should be consolidated into a single tariff for all water districts and one single tariff for all sewage water districts throughout the entire Company. (*Ibid,* 29)

In general, all RUCO, Staff and Company testimonies all support tiered rate structures and rate consolidation. There were no recommendations against consolidation; however, when and the level or degrees of consolidation are where differences lie. (*Ibid*)

First, Mr. Herbert uses "rate equalization" instead of "consolidation" defined as follows:

> "Rate equalization or single tariff pricing is the use of the same rates for the same service rendered by a water company regardless of the customer's location." (*Ibid*)

Second, Mr. Herbert made very clear the basis for his definition of "rate equalization" (consolidation) as follows:

> "Rate equalization is based on the long-term rate stability which results from a single tariff, the operating characteristics of the tariff's groups, the equivalence of services offered, the cost of service on a tariff group basis, and the principle of gradualism." (*Ibid*)

Third, Mr. Herbert explained how rate equalization provided long-term stability for several areas, that also defines the situation here including the arsenic and White Tanks issues in Arizona, as follows:

> "Utility customer rates are dependent on the total expenses and rate base of the utility and the amount of the commodity which the utility sells. Changes in rate base, particularly, as the result of the Safe Drinking Water Act, have significant potential for adversely impacting the rates for certain areas within a utility.
>
> "The ability to absorb the cost of such projects over a larger customer base is a compelling argument in support of rate equalization. Capital programs will never be uniform in the several operating areas, even over periods of 5 to 10 years. <u>The cost of specific programs should be shared by all customers rather than burdening those of the affected areas. Rate increases will be more stable and major increases in specific tariff groups will be avoided</u>."[2] [Underlined for emphasis] (*Ibid*)

The impacts that Mr. Herbert's approach would have on this case include:

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[2] *Ibid*. 19 at 28 to 20 at 7. [Ex. 3]

- Consolidate all capital and other costs into one account, shared equally using one set of rate categories for all customers.
- This would "equalize" or level out, the ups/downs in all Arizona-American water districts.
- This reduces the rate complexity in these six very divergent, non-coordinated, and discombobulated rate cases to one rate base and case for all customers.
- By combing ledgers into a consolidated ledger, accounting would be easier; Company's administrative costs lower, and thus reduce long-term ratepayer costs. (*Ibid*, 29-30)

In summary, this approach presents a **fair and reasonable** methodology to share capital and other costs across all similar customers. If Consolidated Rates were fully implemented, as recommended by Mr. Herbert, all customers and the Company benefit. The Commission and RUCO also benefit by being able to concentrate on one set of books instead of many. (*Ibid,* 30)

Separation of "water" and "waste water" into two tariffs is assumed. (*Ibid*)

Mr. Hebert's "rate equalization" process considers *similarities* to consider when handling the various operating characteristics in the various water districts. Mr. Herbert discusses this in terms of *similarities*, as follows:

> "There are many similarities in the manner in which the several areas [such as Arizona water districts] are operated. All the systems pump their treated water through transmission lines to distribution areas that include mains, booster pump stations and storage facilities. All of the areas rely on a centralized work force for billing, accounting, engineering, administration, and regulatory matters. All of the areas rely on a common source of funds for financing working capital and plant construction. Inasmuch as the costs of operation are related to functions in which the operating characteristics are the same, the use of equal rates is supported." (*Ibid,* original underlined)

Mr. Herbert has shown O&M activities, in general, are similar for the long-term, thus consolidation is appropriate. Many of these functions are already consolidated by Arizona-American; however, they are then "de-consolidated," using traditional separate division-oriented formulae, to allocate these costs back to various water and sewage water divisions. (*Ibid*)

His explanation of how equivalence of offered services supports consolidation by providing directly applicable evidence those noncontiguous service areas, such as the Arizona-American districts, should consolidate rates, by stating:

> "The use of the same rates in a utility with noncontiguous service areas is supported by the equivalent service rendered in each area. Although there would be considerable debate with respect to the equivalency of the service rendered to different customer classifications, there is no question that the service rendered to a residence in one area is the same as the service rendered to a residence in another area. Residential customers are relatively consistent in their uses of water: cooking, bathing, cleaning and other sanitary purposes, and lawn sprinkling. If customers use water for the same purposes, the service offering is the same and should be priced accordingly. Thus, from this perspective, there is no basis for charging different prices to customers in different areas." [Underlined for emphasis] (*Ibid*, original underlined)

Mr. Herbert resolves if variances in allocated cost of tariff groups warrant the use of separate rate schedules as follows:

> "No, they do not. Charging one group of customers' higher rates because they may be served by a newer plant whose original cost exceeds that of other plants as a result of inflation is *not logical*. The concepts previously discussed outweigh this consideration and justify the goal of moving toward a single tariff. The electric industry reflects such concepts when it serves customers in geographically dispersed areas. A kilowatt-hour delivered in one area has the same price as a kilowatt-hour delivered in another area despite the fact that cost of service studies could be performed to identify differences in the cost of providing service to customers classes in different regions." (*Ibid*, 30-31)

There is recent Arizona precedence for Mr. Herbert's comments concerning consolidation of electric rates. In the UNS Electric rate case, the residential and small business rates in Mohave and Santa Cruz County were consolidated, to eliminate five decades of higher rates in the smaller county, as I testified there "<u>is no valid basis for continuing separate rates</u>." (*Ibid*, 31)

This water rate case has exactly the same issue but is compounded by many different tariffs.

Other Cost of Service considerations that Mr. Herbert state support rate consolidation:

> "The Company [including Arizona-American] has taken a number of steps in recent years to centralize and consolidate its operations. Common costs which must be assigned or allocated to each operating area to establish tariff group revenue requirements include management fees, corporate headquarters costs, office costs, customer service costs, depreciation expense developed on the basis of Company-wide depreciation rates and income tax expense based on total Company financing and tax provisions. The allocation of common costs, while reasonable, are subject to judgment and may not result in the development of tariff group revenue requirements which reflect precisely the cost of serving each area." (*Ibid*)

Mr. Herbert discusses how a *single tariff will result in higher rate increases in areas where the rates are lower*. Conversely, a *single tariff will have smaller rate increases in areas where rates are higher*. <u>This balancing, equalizing or consolidation, makes rates fair and reasonable</u>. (*Ibid*, original underlined)

In summary, Mr. Herbert summary supports this rate equalization analysis and suggests it be done using gradualism principles, that is, over several rate cases. He specifically stated:

> "Rate equalization is appropriate for New Jersey-American. Such pricing is supported by considerations of the benefits of sharing the impact of capital programs on a Company-wide basis, the significant majority of common costs, the equivalent service rendered, electric industry precedent and the per capita income of affected communities. The best interests of the customers are served through gradualism by continuing to implement rate equalization during this case and in subsequent cases." (*Ibid*)

**4.3 Conclusions.**

With respect to his concerns, Mr. Townsely is first and foremost concerned about any short-term delay. As a ratepayer, it is the long-term cost for quality service that impacts ratepayers than the Company's financial conditions.

It is my opinion, that RUCO, Staff and the Company can produce Consolidated Rate Schedules for review and comparison, as a separate effort, after this case concludes. The Company's Closing Brief position on this is appropriate. This provides at least three independent views for review, cross-examination, and full-disclosure in public hearings according to a new consolidated rate case schedule.

Concern is about the public and political impacts of Consolidation are, in my opinion, minor when compared to the proposed gains by the Company. Public relations damage has occurred. This case has a record number of water company customer complaints. The public couldn't be more upset than they are right now.

This party considers "consolidation" to means equalize or make level, all elements involved in efficiently running this business. All rate cases end with a determination of a fair and reasonable rate of return for the Company based on a total revenue stream from the ratepayers. The total revenue requirements must be raised from customers, with fixed (service cost) and variable (volumetric rates) customer charges for different rate classes based on "meter" size.

It is concluded that the following are necessary, to most effectively consolidate:

1. Consolidate all "fixed" charges into one Service Charge for each customer category, with one customer category for each meter class, combining residential and commercial rate classes.

2. Consolidate all "variable" or volumetric rates in to one set of rates for each customer category for each meter class. An inclined reverse block rate structure, with adequate number of blocks be developed to ensure all customers can "see" and have an opportunity to reduce consumption by reaching the next lower rate block. At least ten such blocks should be designed; including lower rates for the lowest rate block and significantly higher rates for highest consumption customers in each rate category as a water conservation measure. There should be at least a 100% difference between the lowest and highest rates in each rate category. The lowest rate block should be described for Lower Income customers and publicized as such.

3. Consolidate all miscellaneous "charges and fees" into one schedule for all customers.

4. Consolidate "rules and regulations" into one streamlined, easy to read, document in English and Spanish, available for customers during initial interviews, the web, and in all offices.

5. Consolidate all revenue into one consolidated account (retaining water districts accounting is encouraged) when presenting future rate cases. Revenue will be determined for the consolidated account and not allocated to water districts as a rate making measure.

6. Consider completing the ISO 9000 (Quality Management) qualification process for all divisions with an aim to integrate all company policies and practices, and consider qualifying under ISO 14000 (Environment Management) as a bonus. The additional funds for this are embedded in the "consolidation" incentive part of this rate case to assist this effort.

This party does not support the SBC process recommended by the Company as SBC is NOT understood by ratepayers, sets up additional accounting procedures, and finally this Commission has recently resolved a most challenging and grueling experience in eliminating the SBC by a major electric utility. It was an ugly show that neither I nor anyone else who wants Arizona-American to be successful would wish on their worst enemy. The SBC recommendation is a partial solution when a complete "accounting reset" must be accomplished that will improve Arizona-American. The Test Year plus equipment changes provides the Company the solid foundation and basis right now to start the Consolidation process. Don't wait for later, it maybe too late.

**4.4 Recommendations.**

I strongly urge the Commission

1. Order this rate case be re-opened to review consolidated financial data for Consolidated Rates and order the Company to consolidate all aspects of these six water districts immediately after the rates being proposed are approved for implementation, and

2. To require the unconsolidated water divisions in a future rate case to fully consolidate with the Company, as a single fully integrated company instead of individual inefficient smaller, uncoordinated, unconsolidated companies, and

3. To Increase the Company's ROI at 1 to 2 percentage points, as a bonus, above what it would normally award in this case to reflect the higher risk and potential additional benefits to help reward the Company reorganize into a better entity and become ISO 9000 certified.

Without #3 above, in my opinion, the energies necessary to respond effectively to these demands may have less importance to upper management as success has smaller reward.

By making bold, objective and obviously beneficial changes now, consolidation will improve the entire company, and all ratepayers will benefit in the long-term.

The present situation is deplorable, almost dysfunctional and is surely not impressive to potential investors, actual shareholders and today's nervous financial community.

A strong, united, and more efficient consolidated operation attracts investors, while continuation of the present situation may continue to repel them.

I support such action as a result of this rate case with periodic status reports to the Commission and parties as to "lessons learned" so early mistakes in the consolidation are transparent and the best corrective action measures, with support by the Staff, as necessary, to make Arizona-American Water Company the best in Arizona and the Western United States.

## Section 5

## Issue No. 4

## RATE CASE EXPENSES

### 5.1 Summary of Issue No. 4.

The Company removed from its rate case costs the $10,000 requested for witness training but then added another $10,000 to its Rate Case expenses to respond to a question from a Commissioner concerning consolidation. This is not a new, unexpected expense.

### 5.2 Reply to Post Hearing Closing Briefs.

Company Brief.

Witness training expenses were removed from rate cases expenses and reallocated "to the districts remaining after the Company revised its application to include seven districts instead of the original 10 districts." (Company Brief, 43)

RUCO and Staff Briefs.

None of these Briefs discussed this issue.

Magruder Reply.

Mr. Broderick's Rebuttal stated "rate case expense does not include any expenses for witness training." (Magruder Brief, 44)

### 5.3 Conclusions.

This appears like a *quid pro quo* with the above $10,000 for witness training. (*Ibid*)

Rate Consolidation is an AWC policy. Arizona-American should be looking for ways to consolidate rates when submitting a rate case. Because there was a request to look at Rate Consolidation, there should be no new expenses to provide a clear answer to this concern. (*Ibid*)

As a ratepayer, I expect the most efficient businesses processes to always be embedded into company practices and policies and, of course, the Company should always be looking forward to provide the best service and cost-effective solutions. As concurred by the Company, Rate Consolidation has definite advantages for the Company, consumer and Commission. (*Ibid*)

Therefore, adding additional cost in this rate case to comply with the Company's business practice has no basis. (*Ibid*)

### 5.4 Recommendation.

It is recommended to deny this $10,000 for rate case costs requested during rate case. (*Ibid*)