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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

Arizona Corporation Commission

DOCKETED

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

JUN 16 2009

DOCKETED BY  
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IN THE MATTER OF THE APPLICATION OF  
ARIZONA-AMERICAN WATER COMPANY FOR  
AUTHORITY TO INCUR LONG-TERM DEBT  
THROUGH THE WATER INFRASTRUCTURE  
FINANCE AUTHORITY OF ARIZONA.

DOCKET NO. WS-01303A-09-0152

DECISION NO. 71168

ORDER

Open Meeting  
June 11, 2009  
Phoenix, Arizona

BY THE COMMISSION:

Having considered the entire record herein and being fully advised in the premises, the Arizona Corporation Commission ("Commission") finds, concludes, and orders that:

\* \* \* \* \*

FINDINGS OF FACT

1. On March 25, 2009, Arizona-American Water Company ("AAWC" or "Company") filed an application with the Commission for authorization to execute a loan agreement with the Water Infrastructure Finance Authority of Arizona ("WIFA").<sup>1</sup>

2. AAWC is a for-profit Class "A" Arizona public service corporation that provides water service to approximately 100,000 customers and wastewater service to approximately 50,000 customers in parts of Maricopa, Mohave and Santa Cruz Counties, Arizona. The Company's Tubac water district, which is the subject of the application in this case, provides water service to approximately 532 customers in Santa Cruz County.

3. On May 5, 2009, the Company filed an affidavit of publication verifying that it

<sup>1</sup> This application was filed to take advantage of federal "stimulus" funds provided under the American Recovery and Reinvestment Act of 2009 ("ARRA"), the distribution of which is being administered by WIFA for capital projects undertaken by water and wastewater utilities in Arizona.

1 published notice of its application on April 26, 2009, in *The Green Valley News and Sun*, a  
2 publication of general circulation in the Tubac area.

3 4. On May 13, 2009, the Commission's Utilities Division ("Staff") issued a Staff Report  
4 recommending approval of the application subject to certain conditions.

5 5. On May 14, 2009, Staff filed an Amended Staff Report to correct a typographical error  
6 contained in the original Staff Report.

7 6. On February 17, 2009, the ARRA went into effect. WIFA's *Supplemental 2009 ARRA*  
8 *Intended Use Plan* shows that the ARRA authorizes WIFA to provide an additional subsidy on loans,  
9 which can include forgivable principal and/or additional interest rate subsidies. In addition, the  
10 *Supplemental 2009 ARRA Intended Use Plan* provides that projects that receive ARRA funds would  
11 need to be capable of moving forward rapidly and, hence, expedited regulatory consideration is  
12 appropriate.

13 7. In its application, AAWC requested a WIFA loan in the amount of \$2,300,000 to  
14 finance an arsenic removal project for the Tubac water district that is needed to comply with current  
15 federal arsenic maximum contaminant levels ("MCL"). The federal MCLs require that arsenic levels  
16 not exceed 10 parts per billion ("ppb").

17 8. According to the Staff Engineering Report, the Company's Tubac water district  
18 currently utilizes three wells that contain varying levels of arsenic. Based on 2007 samples, Well No.  
19 2.1 contained 24 ppb; Well No. 4.1 contained 36 ppb; and Well No. 5.1 contained 16 ppb of arsenic.  
20 Under the arsenic remediation plan proposed by AAWC, water would be transported via a new 4,900  
21 foot, 12-inch main from Well No. 4.1 to a centralized media arsenic removal treatment plant located  
22 at the Well No. 5.1 site. Once this is accomplished, Well No. 2.1 would be taken out of service, and  
23 water from Well Nos. 4.1 and 5.1 would be treated for distribution to customers. Major components  
24 of the proposed plant include two 9-foot diameter, by 5-foot high, arsenic removal vessels  
25 manufactured by Severn Trent. The treatment plant would be designed to treat 500 gallons per  
26 minute ("GPM"), and the Company plans to alternate treatment between the two wells, each of which  
27 has a flow rate of 500 GPM. AAWC's estimated costs, as set forth in the Staff Report, are as  
28 follows:

	<b>Project Description</b>	<b>Estimated Cost (\$)</b>
1	<b>Arsenic Treatment Plant &amp; Transmission Line Planning &amp; Design</b>	
2	Hydraulic modeling study	20,786*
3	Design of a 500 GPM Arsenic Removal Facility & 4,900' transmission line	258,138*
4	Bidding Services	8,900*
5	Reimbursable items (prints, permit fees, title report fees, etc.)	8,500*
6	Construction Administration	53,700*
7	<b>Subtotal</b>	<b>350,000</b>
8	<b>Arsenic Treatment Plant Construction</b>	
9	Media	75,000*
10	Plant installation, piping, vessel transportation, earth work, concrete work including footing installation, backwash water holding basin installation, retaining basin installation, etc.	340,000*
11	<b>Subtotal</b>	<b>415,000</b>
12	<b>Transmission &amp; Distribution Line Construction</b>	
13	Installation of 4,900' 12" PVC between Well #5.1 and Well #4.1	550,000*
14	<b>Purchase of Arsenic Treatment Vessels</b>	
15	Two 9'-Diameter, 5'-deep vessels (manufactured by Severn Trent)	150,000*
16	<b>Land Acquisition</b>	
17	Purchasing easement for transmission line project	30,000*
18	<b>Other</b>	
19	Including AFUDC, internal labor, overhead (labor & general)	455,000*
20	<b>Contingency</b>	
21	Contingency (18%)	350,000*
22	<b>Total</b>	<b>2,300,000</b>

Note: \*Tax is included.

9. Staff indicates that based on its existing Tubac district customer base of approximately 590 customers<sup>2</sup>, AAWC has adequate storage and well production to serve its existing customer base and reasonable growth. However, Staff expressed concern that the operation of the system at a maximum of 500 GPM, with the proposed alternating well plan for arsenic treatment, would leave the system short of storage capacity. Therefore, Staff recommends that the Company be required to install a minimum of 500,000 gallons of additional storage capacity by no later than April 30, 2010, as a condition of approval of the application in this case.<sup>3</sup>

10. Staff indicates that there are currently four delinquent compliance issues for AAWC related to Decision No. 70209 (March 20, 2008). However, the Staff Report indicates that the

<sup>2</sup> As indicated above, AAWC's application states that its Tubac water district serves 532 customers. However, the Staff Report indicates that data submitted by the Company shows 588 customers as of December 2008.

<sup>3</sup> On June 1, 2009, Staff filed an Amended Staff Report recommending that this condition be deleted, based on additional information provided by the Company.

1 Company has now submitted the delinquent items for Staff's review.

2 11. AAWC requests that the Commission authorize it to secure WIFA financing in an  
3 amount not to exceed \$2,300,000. Due to an anticipated \$1,150,000 of forgivable principal, pursuant  
4 to WIFA's authority under its *Supplemental 2009 ARRA Intended Use Plan*, the Company expected  
5 repayable indebtedness of \$1,150,000, with an anticipated 20-year amortizing loan and an interest  
6 rate of 6.0 percent per annum.<sup>4</sup>

7 12. According to Staff, as of December 31, 2008, the Company's capital structure  
8 consisted of 14.9 percent short-term debt, 46.5 percent long-term debt, and 38.6 percent equity.  
9 Including Advances In Aid Of Construction ("AIAC") and net Contributions In Aid Of Construction  
10 ("CIAC"), AAWC's capital structure consisted of 9.0 percent short-term debt, 27.9 percent long-term  
11 debt, 23.1 percent equity, 28.6 percent AIAC and 11.4 percent CIAC.

12 13. Staff calculated a pro forma capital structure reflecting issuance of a \$2,300,000,  
13 twenty-year amortizing loan, at an interest rate of 6.0 percent per annum, and determined that  
14 AAWC's capital structure would be comprised of 14.9 percent short-term debt, 46.8 percent long-  
15 term debt and 38.4 percent equity.

16 14. Staff's financial analysis shows that as of December 31, 2008, the Company had a  
17 Times Interest Earned Ratio ("TIER") of 0.52, a Debt Service Coverage ("DSC") ratio of 1.25, and a  
18 Cash Coverage Ratio ("CCR") of 2.24.<sup>5</sup> The pro forma TIER, DSC and CCR for AAWC, assuming  
19 issuance of the 20-year WIFA loan in the amount of \$2,300,000, at an interest rate of 6.0 percent per  
20 annum, would be 0.52, 1.24, and 2.21, respectively. According to Staff, the pro forma DSC shows  
21 that cash flow from operations is sufficient to cover all obligations, including WIFA's requirement to  
22 fund a Debt Service Reserve Fund equal to 20 percent of debt service.

23 <sup>4</sup> According to Staff, the current base interest rate on a WIFA loan is 6.0 percent, and is calculated by using the current  
prime rate of 3.25 percent plus 2.75 percent.

24 <sup>5</sup> TIER represents the number of times earnings cover interest expense on short-term and long-term debt. A TIER greater  
25 than 1.0 means that operating income is greater than interest expense. A TIER less than 1.0 is not sustainable in the long  
26 term but does not mean that debt obligations cannot be met in the short term. DSC represents the number of times  
internally generated cash will cover required principal and interest payments on short-term and long-term debt. A DSC  
27 greater than 1.0 indicates that operating cash flow is sufficient to cover debt obligations. A DSC less than 1.0 means that  
debt service obligations cannot be met by cash generated from operations and that another source of funds is needed to  
28 avoid default. CCR represents the number of times internally generated cash covers required interest payments on short-  
term and long-term debt. A CCR greater than 1.0 means that cash flow from operations is greater than interest expense.

1           15.     Arizona Administrative Code ("A.A.C.") R18-15-104 requires WIFA borrowers to  
2 pledge their revenue sources to repay the financial assistance. A.R.S. § 40-285 requires public  
3 service corporations to obtain Commission authorization to encumber certain utility assets. Staff  
4 states that the statute serves to protect captive customers from a utility's act to dispose of any of its  
5 assets that are necessary for the provision of service, and thus, it serves to preempt any service  
6 impairment due to disposal of assets essential for providing service. Staff states further that pledging  
7 assets as security typically provides benefits to the borrower in the way of increased access to capital  
8 funds or preferable interest rates, and it is often an unavoidable condition of procuring funds for small  
9 or financially stressed entities.

10           16.     Staff concludes that issuance of the proposed debt financing for the purposes stated in  
11 the application is within the Company's corporate powers, is compatible with the public interest, is  
12 consistent with sound financial practices and will not impair its ability to provide service. Staff  
13 recommends authorizing AAWC to incur debt in an amount not to exceed \$2,300,000, for a period of  
14 18-to-22 years, pursuant to a loan agreement with WIFA that provides for 50 percent of the principal  
15 amount to become forgiven upon compliance with the ARRA.

16           17.     As a condition of approval, Staff recommends that the Company:

- 17
- 18           a.     be authorized to engage in any transactions and to execute any  
19 documents necessary to effectuate the authorizations granted  
20 herein;
- 21           b.     be authorized to pledge its assets in the State of Arizona pursuant  
22 to A.R.S. § 40-285 and A.A.C. R18-15-104 in connection with the  
23 WIFA loan;
- 24           c.     that the authorization to incur debt granted by this Decision  
25 terminate on December 31, 2012;
- 26           d.     be required to use its best efforts and to act in good faith to comply  
27 with all the requirements of the American Recovery and  
28 Reinvestment Act of 2009 and all requirements of WIFA in order  
to obtain the 50 percent of forgivable principal;
- e.     be required to install, at a minimum, an additional 500,000 gallons  
of storage capacity and submit the Arizona Department of  
Environmental Quality ("ADEQ") Certificate of Approval of  
Construction prior to April 30, 2010;
- f.     file with Docket Control, as a compliance item in this docket,  
copies of the loan documentation within 60 days of the execution  
of any financing transaction authorized herein;

- 1 g. file with Docket Control as a compliance item in this docket by
- 2 December 31, 2010, copies of the Certificates of Approval of
- 3 Construction issued by the ADEQ for the arsenic treatment plant
- 4 and transmission mains; and
- 5 h. that the Commission take the regulatory measures it deems
- 6 appropriate due to any detrimental consequences to ratepayers that
- 7 may result from the Company's failure to use best efforts and act
- 8 in good faith to comply with the ARRA that results in a reduction
- 9 in the amount of the loan that would otherwise qualify as
- 10 forgivable principal.

11 18. Staff recommendations are reasonable and should be approved.

12 **CONCLUSIONS OF LAW**

13 1. AAWC is a public service corporation within the meaning of Article XV of the

14 Arizona Constitution and A.R.S. §§ 40-285, 40-301, 40-302, and 40-303.

15 2. The Commission has jurisdiction over AAWC and of the subject matter of the

16 application.

17 3. Notice of the application was given in accordance with the law.

18 4. The financing as approved herein is for lawful purposes within AAWC's corporate

19 powers, is compatible with the public interest, with sound financial practices, and with the proper

20 performance by AAWC of service as a public service corporation, and will not impair AAWC's

21 ability to perform the service.

22 5. The financing approved herein is for the purposes stated in the application, is

23 reasonably necessary for those purposes and such purposes may not be reasonably chargeable to

24 operating expenses or to income.

25 6. Staff's recommendations are reasonable and should be adopted.

26 **ORDER**

27 IT IS THEREFORE ORDERED that Arizona-American Water Company is hereby authorized

28 to incur long-term indebtedness in an amount up to \$2,300,000 pursuant to a loan agreement with

WIFA, under which 50 percent of the principal amount would become forgivable principal upon

compliance with the American Recovery and Reinvestment Act of 2009, at an interest rate not to

exceed the current WIFA subsidized rate at the time the loan is executed, for the purpose of funding

an arsenic treatment plant and related facilities as described in the application.

1 IT IS FURTHER ORDERED that Arizona-American Water Company shall use best efforts  
2 and act in good faith to comply with all requirements of the American Recovery and Reinvestment  
3 Act of 2009 and all requirements of WIFA in order to obtain 50 percent of the principal amount as  
4 forgivable principal.

5 IT IS FURTHER ORDERED that if Arizona-American Water Company fails to use best  
6 efforts and to act in good faith to comply with the ARRA, resulting in a reduction of the amount of  
7 the loan that qualifies as forgivable principal, the Commission shall take the regulatory measures it  
8 deems appropriate, including but not limited to disallowing recovery for ratemaking purposes of the  
9 amount of the loan that would otherwise have qualified as forgivable principal.

10 IT IS FURTHER ORDERED that the finance authority granted herein is expressly contingent  
11 upon Arizona-American Water Company's use of the proceeds for the purposes stated in its  
12 application and approved herein.

13 IT IS FURTHER ORDERED that Arizona-American Water Company is authorized to pledge  
14 its assets in the state of Arizona pursuant to A.R.S. § 40-285 and A.A.C. R18-15-104 in connection  
15 with the loan approved herein.

16 IT IS FURTHER ORDERED that Arizona-American Water Company is authorized to engage  
17 in any transactions and to execute any documents necessary to effectuate the authorizations granted.

18 IT IS FURTHER ORDERED that Arizona-American Water Company shall file with Docket  
19 Control, as a compliance item in this docket, copies of all executed financing documents related to  
20 this authority within 60 days after the date of execution.

21 IT IS FURTHER ORDERED that Arizona-American Water Company shall file with Docket  
22 Control, as a compliance item in this docket, by December 31, 2010, copies of the Certificates of  
23 Approval of Construction issued by ADEQ for the arsenic treatment plant and transmission mains.

24 IT IS FURTHER ORDERED that that the authorization to incur debt granted by this Decision  
25 shall terminate on December 31, 2012.

26 ...

27 ...

28 ...

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

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

5 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

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8 CHAIRMAN

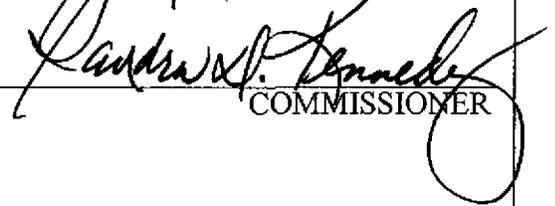


COMMISSIONER

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10 COMMISSIONER

COMMISSIONER



COMMISSIONER

11  
12 IN WITNESS WHEREOF, I, MICHAEL P. KERNS, Interim  
13 Executive Director of the Arizona Corporation Commission,  
14 have hereunto set my hand and caused the official seal of the  
15 Commission to be affixed at the Capitol, in the City of Phoenix,  
16 this 16th day of June, 2009.

17   
MICHAEL P. KERNS  
INTERIM EXECUTIVE DIRECTOR

18 DISSENT \_\_\_\_\_

19 DISSENT \_\_\_\_\_

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1 SERVICE LIST FOR: ARIZONA-AMERICAN WATER COMPANY

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