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AZ CORP COMMISSION
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BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF ARIZONA WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY, AND FOR ADJUSTMENTS TO ITS RATES AND CHARGES FOR UTILITY SERVICE AND FOR CERTAIN RELATED APPROVALS BASED THEREON.	DOCKET NO. W-01445A-08-0440 **NOTICE OF FILING WITNESS SUMMARIES**

Pursuant to the Procedural Order dated November 4, 2008, Arizona Water Company ("Company"), an Arizona corporation, hereby submits this Notice of Filing Wtiness Summaries in the above-referenced matter. The Company expects to call the following as witnesses on Monday, August 31, 2009, and Tuesday, September 1, 2009 and attach their testimony summaries herewith.

1. William Garfield,
2. Fredrick Schneider,
3. Joseph Harris, and
4. Joel Reiker.

Arizona Corporation Commission
DOCKETED

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The testimony summary for the Company's final witness, Dr. Thomas Zepp, is not included in this filing. It will be filed on Friday, September 4, 2009, as he is not expected to testify until Tuesday, September 8, 2009.

DATED this 27th day of August, 2009.

ARIZONA WATER COMPANY

By: ______________________

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An original and thirteen (13) copies of the foregoing were delivered this 27th day of August, 2009 to:

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A copy of the foregoing was hand-delivered this 27th day of August, 2009 to:

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ARIZONA WATER COMPANY

Docket No. W-01445A-08-0440

Summary of Testimony of William M. Garfield

Mr. Garfield is the President of Arizona Water Company (the "Company"). Mr. Garfield holds a bachelor of science degree (with honors) in Thermal and Environmental Engineering from Southern Illinois University, and has taken post-graduate coursework at Arizona State University in Civil Engineering, including hydrology, water and wastewater treatment, and statistics. He is a member of Tau Beta Pi (a national honorary engineering society), the American Water Works Association, serving on that association's Water Meter Standards Committee, and the Arizona Water Association (formerly known as the Arizona Water and Pollution Control Association). Mr. Garfield also serves on the Board of Directors of the Water Infrastructure Finance Authority of Arizona, and is currently the Chairman of the Water Management Subcommittee of the Pinal Active Management Area Groundwater Users Advisory Council. Mr. Garfield has been employed by the Company since 1984.

Mr. Garfield prepared direct, rebuttal and rejoinder testimony on behalf of the Company in this case. His pre-filed testimony addresses (i) the general need and justification for the Company's rate application; (ii) factors affecting the Company's ability to earn a reasonable return on its invested capital; (iii) a historical perspective and resulting benefits achieved through adjuster mechanisms; (iv) risks faced by the Company in its business; (v) the purpose and benefits achieved through rate consolidation; (vi) existing and planned uses of Central Arizona Project ("CAP") water; and (vii) comments raised by the IBEW as they relate to the Company's employees subject to a collective bargaining agreement.

General Basis and Justification for the Company's Rate Application

Mr. Garfield explains that due to increased investments in utility plant, increases in operating and maintenance expenses, and increased risk that the Company faces, the Company's revenues are insufficient to cover such expenses and provide a reasonable return on its invested capital.

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Factors Affecting the Company's Ability to Earn a Reasonable Return on Its Invested Capital

Mr. Garfield identifies the addition of $100 million of new utility plant throughout its three operating groups, which consist of the Company's Northern, Eastern and Western Groups. Of the new plant added since the Company's last rate applications were approved by the Commission, the Company has experienced a 33.9 percent (33.9%) increase in rate base on a companywide basis. With a certain amount of cost recovery established through arsenic cost recovery mechanisms ("ACRMs"), there has been no opportunity for the Company to increase its revenues to reflect its increased investment in utility plant or its cost of providing public utility service throughout its service areas.

Mr. Garfield also explains that the Company's operating and maintenance expenses have increased significantly since the Company's prior rate cases, including purchased power, fuel, purchased water and other operating and maintenance expenses. In addition, Mr. Garfield testifies that a significant amount of the Company's utility plant has been funded through increased long-term debt, which has greatly increased the Company's interest expense, and such increased debt increases risk to the Company.

Mr. Garfield explains that the Company needs to invest $19 million utility plant annually in order to keep up with infrastructure replacements and other plant improvements needed to ensure reliable service. The Company will have to defer or delay such needed water system improvements unless the results of the current rate application provide an opportunity to earn a reasonable rate of return on its investment and to provide a means of recovering increasing operating and maintenance expenses.

Historical Perspective of and Benefits Achieved by Adjuster Mechanisms

Mr. Garfield testifies about the Company's history of adjuster mechanisms approved by the Commission for purchased power and purchased water, the administrative efficiencies achieved through such adjusters, the inherent fairness and equity achieved by such adjusters reflecting both increases and decreases in narrow categories of such costs, and the positive effect that such adjuster mechanisms have on mitigating the attrition effects such increased costs have on the Company's financial condition. He further testifies about the long-term use of its Monitoring Assistance Program ("MAP") surcharge mechanism, which has been in place and operating efficiently for many years, as another example of the types of mechanisms the Commission has approved that work very well.

Mr. Garfield provides additional testimony about the effects and volatility of purchased fuel on the Company's financial condition, the tremendous increase in fuel costs over a relatively short period of time, and identifies and proposes a purchased fuel adjuster mechanism to account for changes in fuel costs.

Mr. Garfield proposes a broad-based attrition adjuster mechanism ("AAM") as an alternative to purchased power, purchased water and purchased fuel adjuster mechanisms. He discusses the advantages that an AAM would have over single-cost adjuster mechanisms, including less frequent companywide annual filings, administrative efficiencies achieved, and consumer protections achieved through the use of an earnings test, such as that used in the Company's ACRM surcharge applications.

Mr. Garfield concludes his testimony on adjuster mechanisms by showing how adjuster mechanisms will help to provide the Company an opportunity to earn a reasonable return on its investments, while still providing incentives to manage its costs, which otherwise could not be achieved without such adjuster mechanisms. Lacking adjuster mechanisms, Mr. Garfield testifies that more frequent rate applications would be necessary, but even with that, the regulatory lag, which has only worsened in Arizona in recent years, will prevent the Company from having the opportunity to earn a reasonable return on its investments.

<u>Risks Faced by the Company in its Business</u>

Mr. Garfield testifies about risks that it faces due to: (i) the small size of the majority of its water systems; (ii) changing regulations and unfunded mandates for new drinking water standards; (iii) increasing operating and maintenance expenses without adjuster mechanisms; (iv) delays in setting new rates; (v) more costly and complex rate applications; (vi) its treatment as a Class A utility even though most of its systems would be classified as Class B or lower; (vii) increased need and cost to perform advanced planning and fund infrastructure in rapidly growing areas; (viii) shift by regulators and consumer advocates to shift the cost of service from ratepayers to the Company; and (ix) increased push by regulators to drive rate of return on investments to lower levels. In addition, Mr. Garfield testified about the detrimental effects that decreased sales to the Company's two largest industrial users will have on the Company's overall revenue requirements as these users have indicated by their efforts to conserve water.

<u>Purpose and Benefits of Rate Consolidation</u>

Mr. Garfield testifies about the purpose and benefits achieved through rate consolidation. He identifies five groups of the Company's water systems proposed for consolidation in this matter. These five groups of systems included the following: (i) Superstition and Miami; (ii) Casa Grande, Coolidge and Stanfield; (iii) Rimrock, Pinewood and Sedona; (iv) Lakeside and Overgaard; and (v) Bisbee and Sierra Vista. Mr. Garfield provides testimony about the increased administrative, operational and regulatory efficiencies; lowered costs; rate stability; economies of scale; increased financial viability; improved affordability; improved and simplified billing; and more gradual changes in rates achieved through rate consolidation.

Existing and Planned Uses for CAP Water

Mr. Garfield testifies about the Company's existing and future planned uses of CAP water; its compliance with Commission Decision No. 68302 through its submittal of a Central Arizona Project Water Use Plan to the Commission Staff on December 31, 2006; and revisions to the Company's Pinal Valley Water System Planning Area and Master Plan.

Responses to the IBEW's Comments on Layoffs, Customer Growth and Health Care Costs

Mr. Garfield testifies about the Company's recent layoffs, customer growth and how the Company has dealt with rising health care costs.

ARIZONA WATER COMPANY

Docket No. W-01445A-08-0440

Summary of Testimony of Fredrick K. Schneider

Mr. Schneider is the Vice President of Engineering for Arizona Water Company ("the Company") and has held that position since August 2007. He holds a Bachelor of Science degree in Hydrology from the College of Engineering and Mines at the University of Arizona in Tucson. Mr. Schneider has been a registered professional engineer in the State of Arizona since 1995. He is also an Arizona Department of Environmental Quality certified water and wastewater operator. He is a member of the American Water Works Association, Water Environment Federation, and the Arizona Water and Pollution Control Association.

Mr. Schneider prepared direct, rebuttal and rejoinder testimony on behalf of the Company in this case. His pre-filed testimony discusses the Company's planning and budgeting process for the construction of plant additions and improvements for the Company's three groups, interconnection of the Company's Superstition and Pinal Valley water systems, status of the Pinal Valley and White Tank Surface Water Treatment Plants and the Company's Tank Maintenance Accrual Account.

Key issues discussed in detail by Mr. Schneider are as follows:

ADWR Compliance for Superior and Oracle

The Company has completed all of the necessary requirements to bring these two water systems into full compliance with the Arizona Department of Water Resources (ADWR). ADWR has acknowledged such by issuance of their Water Provider Compliance Status Report for these two systems. The document states that ADWR "anticipates a complete and satisfactory resolution regarding this matter in the near future". Unfortunately, although the Company has satisfactorily completed all required items, it has no control over the timeframe in which ADWR issues its final finding of compliance.

Lost and Unaccounted Water

The Company administers a comprehensive program for managing water loss. Although several systems currently have water losses in excess of 10%, those systems are faced with unique circumstances. There are seven primary factors that affect water loss within the Company's eighteen water systems. Those factors are (1) age of water mains, (2) system pressures, (3) length and diameter of pipelines, (4) soil composition, (5) non-surfacing leaks, (6) seasonal population increases/decreases and (7) economic barriers. For example, in some cases, water must be pumped many miles from the source of supply at extremely high pressures. Other systems experience large changes in seasonal use and freezing winter temperatures resulting in ruptured service lines and meters. Others have waterlines that are as old as the State of Arizona itself.

Under these circumstances, a significant capital investment will be required to reduce lost water to a level below 10%. This investment will be comparable in magnitude to the federally mandated arsenic treatment plants the Company constructed, which have cost more than $34 million. To address these types of infrastructure problems, other jurisdictions have implemented a Distribution System Improvement Charge or DSIC, which generates funds for replacement of aged plant. Benefits of the DSIC program include more efficient and timely investment of capital, significant progress in replacing aging infrastructure, enhanced service quality, and reduction of water lost through leaks. Such programs typically include protections for customers such as limits on the amount of incremental revenues that can be collected, exclusion of capital projects that are revenue producing, and true-up mechanisms.

In summary, the systems that are experiencing higher water losses have unusual or unique circumstances, which Staff has ignored. Staff has also not acknowledged the fact that capital improvements needed to achieve Staff's recommendations would cost many millions of dollars. Forcing the Company to construct the improvements needed to achieve Staff's water loss goal will result in substantial rate increases for customers unless a DSIC or similar funding mechanism is authorized.

Plant Held for Future Use

Staff has recommended excluding certain wells and other utility from the Company's rate base because they are not currently being used. As described in detail in Mr. Schneider's rebuttal testimony, these plant items are plant held for future use. The plant was used to provide utility service in the past, and will be needed to ensure reliable service in the future. The Company has specific plans for placing the plant in service in the near future, and there are valid financial and operating reasons why this plant is not currently in service. Therefore, the plant meets the Commission's used or useful criteria, as set forth in A.A.C. R14-2-103(a)(3)(h), for being included in rate base.

ARIZONA WATER COMPANY

Docket No. W-01445A-08-0440

Summary of Testimony of Joseph D. Harris

Mr. Harris is the Vice President and Treasurer of Arizona Water Company ("the Company") and has been so since 2007. He holds a Bachelor of Science degree in Accounting from Eastern Illinois University in 1981 and is a Certified Public Accountant in the State of Illinois. He is a member of the American Institute of Certified Public Accountants.

Mr. Harris prepared direct, rebuttal and rejoinder testimony on behalf of the Company in this case. His pre-filed testimony (1) provides an overview of the filing, (2) advocates the reintroduction of Purchased Power and Water Adjuster Mechanisms for the Company's Eastern and Western Groups and the introduction of a Purchased Fuel Adjuster Mechanism in all groups, (3) recommends the weighted cost of capital, (4) discusses how the Arsenic Cost Recovery Mechanism ("ACRM") surcharges and underlying plant have been handled in this case, (5) discusses the consolidation in several systems, and (6) addresses the Commission's required change in depreciation methodology for the Company's Northern Group system.

Overview of the Filing

In his direct testimony, Mr. Harris discusses the circumstances leading to the filing of the instant application for rate adjustments, which is based on operating results and investment in its Northern, Eastern and Western Group water systems for the adjusted test year 2007. As of December 31, 2007, the Company served 83,800 customers. The current rates were approved in Decision Nos. 64282, 66849 and 68302 for the Northern, Eastern and Western Groups respectively. The current ACRM surcharges were approved in Decision Nos. 70169, 70191, 70702, 70834, 70962 and 70963 for Superstition, San Manuel, Casa Grande / Stanfield, Sedona, Rimrock and White Tank.

Mr. Harris states that investment in needed utility plant and operating costs have increased dramatically. Rate base in the Northern Group has increased by $16,252,341 or 98.5% since its current rates were approved in 2001. In the Eastern Group rate base has increased $27,097,864 or 75.4% and in the Western Group by $28,701,213 or 123.4% since rates were set in 2004 and 2005, respectively. Operating expenses have likewise increased dramatically, with costs rising $2,723,914 or 51.4% in the Northern Group, $3,294,757 or 25.1% in the Eastern Group and $5,134,060 or 58.5% in the Western Group since rates were previously established.

Automatic Adjustment Mechanisms

Mr. Harris discusses purchased power costs for the Company, noting that since the Company's Purchased Power Adjuster Mechanism ("PPAM") was eliminated in Decision No. 66849 in the Eastern Group, power costs for that group have risen by some $224,000. Mr. Harris notes that the Company's largest power providers, Arizona Public Service and Salt River Project, have filed 13 base or power supply adjuster increases in the past four years. Power costs represent a significant operating expense, accounting for nearly 18% of all operating expenses the price of which is beyond the Company's control.

Similarly, purchased water costs represent a significant operating expense for some systems, including Ajo, where it accounts for nearly 50% of operating expenses, and San Manuel where it accounts for more than 30% of operating expenses.

As an alternative to the re-introduction of the PPAM or PWAM for the Eastern and Western Groups, the Company proposes an Attrition Adjustor Mechanism ("AAM"). The AAM would be a broad-based adjuster based on the Consumer Price Index and would be limited by a cap and earnings test. This mechanism would help the Company minimize the effects of earnings erosion caused by increases in operating costs, and allow the Company an opportunity to actually earn its authorized rate of return.

Weighted Cost of Capital

Mr. Harris also addresses the Company's capital structure and its proposed weighted cost of capital, which is 9.81%, and sponsors the Company's D Schedules. At the end of the 2007 test year, the Company (on a companywide basis) had long-term debt totaling $40 million at an average embedded cost of 6.96%. Mr. Harris explained that the Company would be issuing $35 million of long-term debt in the third quarter of 2008 and estimated that it would have an interest rate of 7.70%.

In rebuttal, the Company revised its capital structure to give full effect to the $35 million long-term debt issuance. In its revised capital structure the Company (on a companywide basis) has long-term debt totaling $75 million at an average embedded cost of 6.83% and short-term debt of $7.3 million at a cost rate of 3.0%. The Company's capital structure now contains approximately 46% common equity, as opposed several years ago, when more than 70% of the Company's capital structure was common equity. The revised weighted cost of capital is 9.20%

ACRM Surcharges and Post Test Year Plant

Mr. Harris addresses the Company's pending ACRM applications for the Sedona, Rimrock, White Tank, Casa Grande and Stanfield systems. All arsenic-related plant additions included in these pending ACRM applications were included as Post Test Year plant in the rate case. Additionally, the related arsenic treatment O&M expenses, such as media replacement or regeneration costs; media replacement or regeneration service costs and waste media or regeneration disposal costs, were included as pro forma adjustments.

Mr. Harris further discusses the need for future arsenic treatment plant and proposes that the Company be allowed to recover the costs of those future plants under the ACRM mechanism. Mr. Harris noted that a provision of the pending ACRM applications was for the recovery of deferred O&M costs which would not be fully recovered prior to a decision in this case. The Company proposes that it be allowed to continue the ACRM surcharge to fully recover those deferred costs.

Staff, in its surrebuttal testimony, recommended that the Commission approve a new ACRM for the Sedona and Superstition systems based upon the conditions set forth in Decision No. 66400. Further, Staff agreed that the Company's proposal concerning the recovery of deferred O&M costs is reasonable and is consistent with Decision Nos. 70702, 70834 and 70962.

Mr. Harris, in his rejoinder testimony, advocates the removal of the system-specific limit that Staff has placed on new ACRM filings, and cited new or expanded arsenic treatment facilities in Casa Grande and noted that arsenic levels in ground water supplies is not static and wells that do not need arsenic treatment today may require it in the future.

System Consolidation

In his direct testimony, Mr. Harris discusses the Company's proposal for consolidating rates and accounting information for several of the Company's water systems. In his discussion, Mr. Harris notes that many of the Company's water systems are small Class C and D water systems and are particularly vulnerable to any utility plant investment or expense spikes. Through consolidating these small systems into larger rate groups, these increases are spread over a large base thereby smoothing rate increases.

The Company is proposing the following full consolidations:

Superstition and Miami; and
Lakeside and Overgaard

The Company is proposing the following phased consolidations:

Casa Grande, Coolidge and Stanfield;
Bisbee and Sierra Vista; and
Sedona, Rimrock and Pinewood.

Staff, in its direct testimony, supported the Company's groupings for consolidation purposes but proposed full consolidation for Casa Grande/Coolidge/Stanfield and Sedona/Rimrock/Pinewood. The Company, in rebuttal, discusses its concern with the conflicting price signal that would result from fully consolidating these systems, which leads to large rate decreases in Stanfield, Pinewood and Rimrock. Additionally, residential customers in Sedona would be unduly burdened with rates that are in excess of their cost of service.

RUCO filed its rate design in surrebbutal and advocates a companywide base charge with varying commodity rates by system. Under RUCO's proposal, no systems would be consolidated. Instead, the Company would be required to maintain separate books and accounting records for each system, and file separate information for each system in connection with rate cases, eliminating the benefits of consolidation. RUCO offers this requirement to prevent the Company from engaging in "over-building" any particular system. Mr. Harris notes that the Company has had consolidated systems (Sedona/Valley Vista, Casa Grande/Tierra Grande, Lakeside/Pinetop Lakes and Apache Junction/Superior) for a number of years, and neither RUCO nor Staff has taken the position that the Company has engaged in over-building any of the systems and there is no evidence of any such over-building.

Depreciation Methodology

Mr. Harris discusses the depreciation rates currently authorized for the Northern Group, the Meter Shop and the Phoenix office. Mr. Harris advocates implementing the depreciation rates by plant account that were authorized in the Company's Eastern and Western Groups in Decision Nos. 66849 and 68302, respectively, on a companywide basis.

ARIZONA WATER COMPANY

Docket No. W-01445A-08-0440

Summary of Testimony of Joel M. Reiker

Mr. Reiker is the Manager of Rates and Regulatory Accounting for Arizona Water Company ("the Company") and has been so since 2007. Mr. Reiker holds a Bachelor of Science degree in global business with a specialization in financial management from Arizona State University School of Management. He has attended various educational programs and classes on public utility and regulatory issues, including the National Association of Regulatory Utility Commissioners ("NARUC") and the Institute of Public Utilities' Regulatory Studies program at Michigan State University. He is a member of the Society of Utility and Regulatory Financial Analysts and is a Certified Rate of Return Analyst.

From 1999 to 2005, Mr. Reiker was employed by the Commission as a Staff Rate Analyst in the Utilities Division during which he provided recommendations on behalf of Staff regarding rate of return, mergers and acquisitions, divestitures, financings, and affiliated interests issues. On occasion, he acted as arbitrator in disputes brought before the Utilities Division. Subsequently, he was employed by American Water Works Service Company as Senior Regulatory Analyst.

Mr. Reiker prepared direct, rebuttal and rejoinder testimony on behalf of the Company in this case. His pre-filed testimony addresses several issues and specific adjustments including the development of rate base, working capital requirement, and net operating income for the Company for the historical twelve month period ending December 31, 2007. Mr. Reiker also sponsors the calculation of the associated increase in gross revenue requirement, as well as the Company's cost of service study, and proposed rate design for each system. Additionally, he addresses the Company's need for purchased power and purchased water adjuster mechanisms, or in the alternative, an attrition adjuster mechanism.

Mr. Reiker addresses the effect of Staff's and RUCO recommended level of revenues on the Company's 2008 pro forma operating results. He concludes that under Staff's and RUCO proposed rates in this proceeding, the Company will not earn the its authorized rate of return, and will have an interest coverage ratio that is lower than that of the four publicly traded water utilities studied by Staff in its cost of equity analysis. Additionally, Mr. Reiker concludes that the Company may have difficulty issuing additional long-term debt if Staff's or RUCO's proposed level of revenues is adopted in this proceeding.

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In 2008, the Company experienced a 760 million gallon, or 6.47% reduction in water sales from adjusted test year levels. This represents $2.4 million in unrealized revenues at the Company's proposed rates. Included in this drop in sales is a 49% reduction in construction water sales, representing $586,591 in unrealized revenues at proposed rates. Also in 2008, Abbott Laboratories, the Company's largest industrial customer, reduced the amount of water it purchased from the Company by approximately 18% compared to the test year. Frito Lay, the Company second largest industrial customer, reduced the amount of water it purchased from the Company by nearly 9% compared to the test year. These reductions represent unrealized revenues at proposed rates of $120,973 and $22,044, respectively. Reductions in usage along with further increases in operating expenses are likely to necessitate the filing of new rate case sooner than the Company otherwise would, absent the approval of the various adjuster mechanism requested by the Company in this proceeding.

The Company only accepts those adjustments to rate base proposed by Staff and RUCO that are related to plant that the Company found should have been previously retired. Further, the Company proposes adjustments to the accounting entries to properly reflect the retirement of plant in service. All remaining plant items that Staff recommends be disallowed are either currently in service, or have been identified as property held for future use and should be included in rate base under a definite plan for such use.

The Company does not accept RUCO recommendation that post test year plant not mandated by the government be excluded from rate base. RUCO has provided no evidence suggesting that including post test year plant in rate base results in excess returns to equity investors or otherwise results in unfair rates.

The Company does not accept Staff's and RUCO's exclusion of the equity cost component of working capital. The Company is indifferent to the inclusion of operating income in the cash working capital component of working capital. However, if the Commission includes one component of operating income in working capital, such as the debt component (as Staff and RUCO recommend), then all operating income components should be included.

The Company does not accept Staff's proposed adjustment to tank maintenance expense and its recommendation that the Company cease using the reserve-accrual method of accounting for tank maintenance expense. Staff proposes to normalize over three years an expense that only occurs at intervals of seven and 14 years. This is a wholly inappropriate method of normalizing an expense that does not occur on an annual basis. Further, Staff's three-year normalization includes calculation errors and understates the true level of costs incurred by the Company. The Commission has approved the Company's reserve-accrual method of accounting for these costs since at least 1960, and no legitimate basis to depart from this practice has been given.

The Company does not accept Staff's recommendation to adjust expense accounts 663 (Operations – T&D Meters) and 673 (Maintenance – T&D Mains) using a three-year average. Staff singled out these accounts and failed to consider other areas of change that, if measured as to their impact, would have the opposite income effect. These other areas include the significant reduction in water usage from adjusted test year levels and the rate increases sought by the Company's two largest purchased power providers, which should become effective later this year. Further, Staff proposes to disallow a portion of the costs related to reducing lost and unaccounted for water, while at the same time recommending that the Company incur additional expenses related to reducing lost and unaccounted for water.

The Company doesn't accept Staff's and RUCO adjustment to eliminate the Company's proposed conservation adjustment. Neither party has provided evidence that the implementation of increasing block rates does not result in reduced residential usage. On the contrary, the Company provided multiple statistical analyses indicating that residential customers in those systems where increasing block rates are currently in effect have in fact reduced usage.

Staff applied the incorrect CIAC amortization rates in developing its proposed revenue requirement in this proceeding. The theoretically correct CIAC amortization rate, and the rate currently approved by the Company, is 2.00%. Staff's proposed CIAC amortization rates are different in every system and reflect plant accounts that do not typically include contributed plant. If Staff's proposed CIAC amortization rates are approved, contributions will be amortized sooner than the plant that was contributed will be fully depreciated, and the Company will be deprived of cash flow in the near-term that is need to maintain and improve its systems and reduced lost and unaccounted for water.

The Company does not accept RUCO's proposed adjustment to payroll expense based on a normalized level of test year overtime hours. RUCO has not shown that the total number of overtime hours, or the overall level of payroll expense incurred during the test year, is any different than the amounts required to provide service during the period in which new rates will be in effect. RUCO also ignores other areas of change, as mentioned above, which would have the opposite income effect of its adjustment.

Mr. Reiker responds to Abbott Laboratories witness Mr. Chasse, and explains why the Commission should not increase the level of revenues allocated to the industrial class, or impose an increasing block rate design on industrial customers in this proceeding. Industrial customers are already paying rates that are significantly higher than cost, and economics tells us that these customers are already encouraged to reduce the amount of water they use. In fact, both Abbott and Frito Lay have significantly reduced the amount of water they purchased from the Company and plant to reduced consumption even further.

The Company accepts Staff's recommended adjustments to its cost of service study, which indicates that commercial and industrial customers are paying rates in excess of their cost of service.

Staff's proposal to further increase rates charged to industrial customers is unfair given they are currently paying rates that are approximately 40% higher than cost. Further, Staff's proposal to impose a further price signal on industrial customers in the form of an increasing block rate design is unnecessary given industrial customers are already paying rates significantly higher than cost. As stated previously, economics tells us that these customers are already encouraged to reduce the amount of water they consume.

Staff's typical bill increases ignore the fact that customers in various systems are currently paying the arsenic cost recovery mechanism surcharge and purchased power adjuster mechanism surcharge. As a result, Staff's typical bill increases in these systems bear no relationship to the actual increases (and decreases) that customers will experience.