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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

DOCKETED

OCT -9 2009

COMMISSIONERS

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

DOCKETED BY	nr
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IN THE MATTER OF THE APPLICATION OF YARNELL WATER IMPROVEMENT ASSOCIATION, INC., AN ARIZONA NON-PROFIT CORPORATION, FOR AUTHORITY (1) TO ISSUE EVIDENCE OF INDEBTEDNESS IN AN AMOUNT NOT TO EXCEED \$767,000.00 IN CONNECTION WITH (A) THE CONSTRUCTION OF WATER SYSTEM INFRASTRUCTURE IMPROVEMENTS AND (B) REPAYMENT OF EXISTING DEBT; AND (2) TO ENCUMBER ITS REAL PROPERTY INTERESTS AND WATER SYSTEM INFRASTRUCTURE AS SECURITY FOR SUCH INDEBTEDNESS.

DOCKET NO. W-02255A-09-0258

DECISION NO. 71298

ORDER

Open Meeting  
 October 8, 2009  
 Phoenix, Arizona

BY THE COMMISSION:

On May 22, 2009, Yarnell Water Improvement Association, Inc. ("Company" or "Applicant") filed with the Arizona Corporation Commission ("Commission") an application requesting approval in order to obtain long-term financing and to encumber the Company's property as security for the debt ("Application").

Subsequently, the Company filed supplemental exhibits to its Application.

On July 14, 2009, the Company filed certification that it had provided public notice of its Application requesting Commission approval to incur long-term debt.

On September 17, 2009, Staff filed a memorandum with regard to the Company's Application and recommends approval by the Commission

\* \* \* \* \*

Having considered the entire record herein and being fully advised in the premises, the Commission finds, concludes, and orders that:

**FINDINGS OF FACT**

1  
2 1. Pursuant to authority granted by the Commission, Applicant is an Arizona non-profit  
3 corporation engaged in the business of providing water service in an area approximately 30 miles  
4 southwest of Prescott in Yavapai County, Arizona.

5 2. On May 22, 2009, the Company filed an Application requesting Commission approval  
6 to incur long-term debt in an amount not to exceed \$1,300,000 in the form of a United States  
7 Department of Agriculture, Rural Development ("USDA-RD") loan and grant. The USDA-RD will  
8 administer the loan on behalf of the Rural Utilities Service ("RUS"). The Company is also requesting  
9 authority from the Commission to encumber its real property interests and water system infrastructure  
10 as security for the indebtedness arising from the long-term debt.

11 3. With its Application, the Company is seeking the Commission's approval for what the  
12 Company expects will be designated as forgivable principal in the amount of \$533,000 coupled with  
13 \$767,000 of repayable debt. The Company will use the funds to pay off existing long-term debt  
14 approved by the Commission that funded the cost of the construction of the water system in 1974 and  
15 1975.<sup>1</sup> The balance of the funds will be utilized for improvements to Applicant's system as follows:  
16 Project No. 1 –to repair and replace valves; Project No. 2 –to replace fire hydrants; Project No. 3 –to  
17 reline storage tanks; Project No. 4 –to install an on-site generator; Project No. 5 –to replace water  
18 lines; and Project No. 6 –to replace the Company's telemetry system.

19 4. On June 20, 2009, Applicant published notice of its Application in this matter in the  
20 *Courier*, a newspaper of general circulation in Prescott, Yavapai County, Arizona.

21 5. The Commission has not received any comments or protests in response to the public  
22 notice provided by the Company with respect to the Application herein.

23 6. The source of the RUS funding for the Company's plan to pay off existing debt and to  
24 make improvements to its system is the American Recovery and Reinvestment Act of 2009  
25 ("ARRA") enacted by the United States Congress in February 2009. The ARRA authorizes an  
26 additional subsidy for loans and improvement projects. Companies such as the Applicant that qualify

27  
28 <sup>1</sup> According to the Company's balance sheet dated December 31, 2008, the outstanding balance on these loans is \$268,931.

1 for such funds are required to move forward rapidly to secure expedited regulatory approval.

2       7.       On September 17, 2009, the Staff Memorandum was filed recommending approval of  
3 the Company's Application to obtain a loan from USDA-RD/RUS, in an amount not to exceed  
4 \$1,300,000 consisting of \$533,000 for forgivable principal and long-term indebtedness in the amount  
5 of \$767,000 for a term of 38 to 42 years and with an interest rate not to exceed 3.75 percent *per*  
6 *annum*.

7       8.       Staff projected that the Company's current rates authorized in Decision No. 70698  
8 (January 20, 2009) would generate \$61,344 of operating income and would provide the Company  
9 with a 22.31 percent operating margin to enable it to meet its obligations.

10       9.       In Decision No. 70698, the Commission found that the \$61,344 in operating income  
11 would enable the Company to meet its long-term debt resulting from earlier loans which had been  
12 approved by the Commission when the utility system was built in the mid 1970s.

13       10.       Staff's engineering section reviewed the proposed plant improvements and related  
14 costs and stated that the estimated project costs provided by the Company projected at \$446,200  
15 appear to be reasonable and appropriate for the construction improvements described hereinabove.  
16 However, Staff indicated that it was not making any "used and useful determination from which any  
17 conclusion should be inferred for rate making or rate-base purposes."

18       11.       According to Staff's Memorandum, as of December 31, 2006, which was the test year  
19 that was used in arriving at the Company's rates authorized in Decision No. 70698, the Company's  
20 capital structure consisted of 7.4 percent short-term debt, 46.5 percent long-term debt and 46.1  
21 percent equity.

22       12.       Staff projects that a *pro-forma* capital structure which reflects a draw down of the  
23 \$1,300,000, utilizing a 40-year amortizing loan will result in the Company having a capital structure  
24 of 1.2 percent short-term debt, 83.9 percent long-term debt and 15.0 percent equity.<sup>2</sup> Staff stated that  
25 it typically recommends that a non-profit water utility maintain capital structures with a minimum of  
26 30 percent equity as appropriate to provide a balance of cost and financial risk for regulated utilities  
27

28 <sup>2</sup> Staff's analysis treats the \$533,000 of forgivable principal as long-term debt.

1 and ratepayers. However, in this instance, Staff concludes that the proposed capital improvements  
2 and the forgivable principal arising from the grant opportunity warrant authorization of the proposed  
3 debt despite the resulting highly leveraged capital structure.

4 13. Staff points out that the Company is required to secure Commission approval pursuant  
5 to A.R.S. § 40-285 in order to encumber the Company's real property and other utility assets used to  
6 provide service to its customers to protect them from the utility's disposing of any assets that are  
7 necessary for the provision of service. By pledging its assets, the Company is providing security to  
8 the USDA-RD/RUS in order to provide benefits to its customers by increasing access to capital funds  
9 with low interest rates which will enable the Company to better serve ratepayers.

10 14. The Debt Service Coverage ("DSC") ratio represents the number of times internally  
11 generated cash will cover required principal and interest payments on long-term debt. A DSC ratio  
12 greater than 1.0 indicates that operating cash flow is sufficient to cover debt obligations. A DSC ratio  
13 less than 1.0 means that debt service coverage cannot be met from operations and that another source  
14 of funds is needed to avoid default.

15 15. Staff analyzed the Company's *pro forma* impact of drawing down the proposed long-  
16 term debt of \$1,300,000, and found that it results in a DSC of 1.41 which indicates that the Company  
17 will have adequate cash flow to meet its obligations.

18 16. The Staff Memorandum indicates that the Company has no delinquencies with respect  
19 to the Commission's compliance requirements.

20 17. Staff's Engineering Report indicates that the Company is providing water which meets  
21 the requirements of the Safe Drinking Water Act.

22 18. Staff further indicates that the Arizona Department of Water Resources has  
23 determined that the Company is currently in compliance with departmental requirements governing  
24 water providers and/or community water systems.

25 19. Based on Staff's review and analysis, Staff concluded that the proposed financing as  
26 recommended by Staff is for lawful purposes, within the Company's powers as a corporation,  
27 compatible with the public interest, consistent with sound financial practices and will not impair the  
28 ability to provide public service. Staff further recommended:

- 1 • that the Commission approve the Company entering into a long-term loan with  
2 USDA-RD/RUS for a period not to exceed 42 years in an amount not to  
3 exceed \$1,300,000 which provides for \$533,000 of the principal amount to  
4 become forgiven upon the Company complying with the ARRA of 2009 and  
5 USDA-RD;
- 6 • that the Company be authorized to pledge its real property and utility assets  
7 pursuant to A.R.S. § 40-285 in connection with the USDA-RD/RUS loan;
- 8 • that the Company use its best efforts and act in good faith to comply with all  
9 requirements of the ARRA of 2009 and all requirements of the USDA-  
10 RD/RUS in order to obtain the \$533,000 of forgivable principal;
- 11 • that the Commission take the regulatory measures it deems appropriate due to  
12 any detrimental consequences to ratepayers that may result from Applicant's  
13 failure to use best efforts and act in good faith to comply with the ARRA of  
14 2009 that results in a reduction in the amount of the loan that would otherwise  
15 qualify as forgivable principal;
- 16 • that any authorization to the Company to incur debt granted in this proceeding  
17 terminate if not exercised prior to December 31, 2012;
- 18 • that the Company be authorized to engage in any transaction and to execute  
19 any documents necessary to effectuate the authorizations granted herein;
- 20 • that the Company file, within 60 days of the execution of any documents  
21 related to this transaction, with the Commission's Docket Control, as a  
22 compliance item in this docket, a copy of the executed loan documents; and
- 23 • that the Company file, by December 31, 2012, with the Commission's Docket  
24 Control, as a compliance item in this docket, copies of the Arizona Department  
25 of Environmental Quality ("ADEQ") Certificates of Approval of Construction  
26 ("AOC") for Project No. 1 (repair and replacement of valves), Project No. 2  
27 (replacement of fire hydrants), Project No. 3 (reline storage tanks), and Project  
28 No. 5 (replace water lines).

20. Staff's recommendations herein are reasonable and should be adopted.

### CONCLUSIONS OF LAW

1. The Company is a public service corporation within the meaning of Article XV of the  
Arizona Constitution and A.R.S. §§ 40-285, 40-301 and 40-302.
2. The Commission has jurisdiction over the Company and of the subject matter of the  
Application.
3. Notice of the Application was given in accordance with the law.
4. Staff's recommendations are reasonable and should be adopted.
5. The encumbrance approved herein is for the purposes stated in the Application and is  
reasonable and necessary for those purposes.
6. The financing approved herein is for lawful purposes within the Company's corporate

1 powers, is compatible with the public interest, with sound financial practices, and with the proper  
2 performance by the Company of services of a public service corporation, and will not impair the  
3 Company's ability to perform that service.

4 7. The financing approved herein is for the purposes stated in the Application and is  
5 reasonably necessary for those purposes, and such purposes are not wholly or in part, reasonably  
6 chargeable to operating expenses or to income.

7 **ORDER**

8 IT IS THEREFORE ORDERED that the Application of Yarnell Water Improvement  
9 Association, Inc. for authority to contract with the USDA-RD/RUS for long-term debt not to exceed  
10 \$1,300,000, which provides for \$533,000 of the principal amount to be forgiven upon compliance  
11 with the American Recovery and Reinvestment Act of 2009 and the requirements of the USDA-  
12 RD/RUS at an interest rate not to exceed 3.75 percent *per annum* and for a period no longer than 42  
13 years, shall be, and is hereby, approved.

14 IT IS FURTHER ORDERED that Yarnell Water Improvement Association, Inc. shall use its  
15 best efforts and act in good faith to comply with all of the requirements of the American Recovery  
16 and Reinvestment Act of 2009 and all requirements of USDA-RD/RUS in order to obtain the  
17 \$533,000 of forgivable principal.

18 IT IS FURTHER ORDERED that such authority is expressly contingent on Yarnell Water  
19 Improvement Association, Inc.'s use of the proceeds for the purposes set forth in its Application.

20 IT IS FURTHER ORDERED that Yarnell Water Improvement Association, Inc. is hereby  
21 authorized to pledge its real property and utility assets as security for the USDA-RD/RUS loan as  
22 described hereinabove.

23 IT IS FURTHER ORDERED that Yarnell Water Improvement Association, Inc. is hereby  
24 authorized to engage in any transactions and to execute any documents necessary to effectuate the  
25 authorization granted hereinabove.

26 IT IS FURTHER ORDERED that Yarnell Water Improvement Association, Inc. shall file,  
27 within 60 days of the execution of the loan documents, with the Commission's Docket Control, as a  
28

1 compliance item in this docket, copies of all executed documents associated with the financing  
2 authorized herein.

3 IT IS FURTHER ORDERED that the financing approved herein shall not guarantee or imply  
4 any specific treatment of any capital addition for rate base or rate making purposes.

5 IT IS FURTHER ORDERED that Yarnell Water Improvement Association, Inc. shall file, by  
6 December 31, 2012, with the Commission's Docket Control, as a compliance item in this docket,  
7 copies of the ADEQ Certificates of Approval of Construction for Project No. 1 (repair and  
8 replacement of valves), Project No. 2 (replacement of fire hydrants), Project No. 3 (reline storage  
9 tanks), and Project No. 5 (replace water lines).

10 IT IS FURTHER ORDERED that any authorization granted herein with respect to the long-  
11 term debt not utilized by Yarnell Water Improvement Association, Inc. as of December 31, 2012,  
12 shall terminate.

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

14 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

15   
16 CHAIRMAN

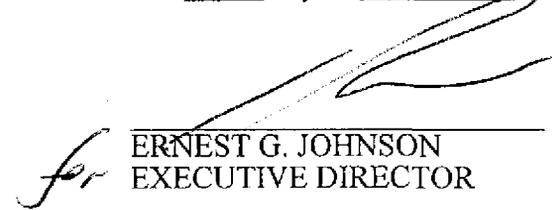
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16 COMMISSIONER

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20 IN WITNESS WHEREOF, I, ERNEST G. JOHNSON  
21 Executive Director of the Arizona Corporation Commission,  
22 have hereunto set my hand and caused the official seal of the  
23 Commission to be affixed at the Capitol, in the City of Phoenix,  
24 this 9th day of October, 2009.

24   
25 ERNEST G. JOHNSON  
26 EXECUTIVE DIRECTOR

26 DISSENT \_\_\_\_\_

27 DISSENT \_\_\_\_\_

28 MES:db

1 SERVICE LIST FOR: YARNELL WATER IMPROVEMENT ASSOCIATION, INC.

2 DOCKET NO.: W-02255A-09-0258

3  
4 Sheila B. Schmidt  
5 GUST ROSENFELD P.L.C.  
6 201 East Washington Street, Suite 800  
7 Phoenix, Arizona 85004-2428  
8 Attorneys for Applicant

9  
10 Janice Alward, Chief Counsel  
11 Legal Division  
12 ARIZONA CORPORATION COMMISSION  
13 1200 West Washington Street  
14 Phoenix, Arizona 85007

15  
16 Steve Olea, Director  
17 Utilities Division  
18 ARIZONA CORPORATION COMMISSION  
19 1200 West Washington Street  
20 Phoenix, Arizona 85007

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