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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission
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COMMISSIONERS

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

IN THE MATTER OF THE APPLICATION OF FAR WEST WATER & SEWER COMPANY, AN ARIZONA CORPORATION, FOR APPROVAL OF INTERIM RATES AND CHARGES.

DOCKET NO. WS-03478A-08-0608

DECISION NO. 71447

OPINION AND ORDER

DATES OF HEARING:	April 6, and 7, 2009, and May 12, 13, 14, and 21, 2009
PLACE OF HEARING:	Tucson, Arizona
DATE OF PUBLIC COMMENT:	March 5, 2009
PLACE OF PUBLIC COMMENT:	Yuma, Arizona
ADMINISTRATIVE LAW JUDGE:	Jane L. Rodda
APPEARANCES:	Mr. Jay Shapiro, FENNEMORE CRAIG, on behalf of Applicant;
	Ms. Michelle Wood, Staff Attorney, on behalf of the Residential Utility Consumer Office; and
	Mr. Kevin Torrey and Ms. Robin Mitchell, Staff Attorneys, Legal Division, on behalf of the Utilities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

On December 19, 2008, Far West Water & Sewer Company ("Far West" or "Company") filed with the Arizona Corporation Commission ("Commission") an emergency application for the immediate implementation of interim rates for sewer service, which rates would be effective until a decision has been issued on the Company's application for permanent rate increase.

The Company had filed an application for permanent rates on August 29, 2008, in Docket No. WS-03478A-08-0454. By Procedural Order dated December 10, 2008, the permanent rate case was set for hearing to commence on July 29, 2009. Following the filing of the emergency rate application, by Procedural Order dated January 23, 2009, the proceedings in the permanent rate case were suspended pending the conclusion of the emergency case.

Summary of Request

The Company is seeking an emergency rate increase designed to produce additional revenue of $2,161,788 on an annual basis. The Company claims its request would result in a zero Operating Income.[1] The requested increase would be a 101.95 percent increase over current sewer division revenues.[2] The Company argues that all three of the conditions identified in Arizona Attorney General Opinion 71-17, which establishes the guidelines to determine when an "emergency" exists for the purpose of approving interim rates, are present, or threatened, in this case.

Far West asserts that it cannot pay its debts as they come due. Far West projects that in 2009, the Company will have a cash flow deficit of over $6.4 million. It states that it has invested more than $18 million in improvements in the last three years, which are not yet included in rate base, and is paying debt service on more than $20 million in new debt used to pay for these improvements. Far West states it is unable to complete the sewer system improvements necessary to comply with its October 2006 Consent Order with the Arizona Department of Environmental Quality ("ADEQ"). The Company claims it has been unable to raise the additional capital needed to pay for the cost overruns related to its sewer system renovation project. Thus, the Company asserts that it is insolvent, as it cannot complete the plant to comply with the Consent Order and cannot obtain permanent rate relief to address its severe cash flow shortage. Far West states that because it cannot make the necessary improvements to its water and wastewater utility systems, its ability to maintain safe and reliable water and sewer service in doubt.

RUCO argues that the Commission should deny the request for interim rates because, on a total company basis, the Company has sufficient funds to meet its operating expenses and debt service. RUCO argues that shortfalls in the Company's capital budget for construction work in progress are not appropriately charged to ratepayers.[3] According to RUCO, the Company is not

[1] Far West Closing Brief at 1.
[2] Ex A-3 Bourassa Rebuttal at 2.
[3] RUCO Reply Brief at 1.

insolvent and there is no emergency. RUCO's analysis of the Company's relevant financial ratios indicates that the Company actually has a better cash flow now than it did in 2007.

Staff believes that when Far West is viewed as a whole, the Company's existing rates are sufficient to allow it to remain financially solvent and to provide reasonable funds for unexpected events or contingencies until the conclusion of the permanent rate case.[4] Staff argues the Company's request for interim rates is unfair to ratepayers and would only aggravate the Company's financial situation. Staff advocates that the only viable solution to the Company's need to complete its sewer renovation project is an infusion of equity. In the event the Commission determines that there is an emergency, Staff offers an alternative recommendation that would provide the Company with interim relief in the amount of $972,150, a 46.3 percent revenue increase, to be spread evenly among all customer classes.

Background Events

Far West is located in Yuma County and provides water utility service to approximately 15,000 customers and sewer utility service to approximately 7,300 of those customers. In the past ten years, the Company's service area experienced a period of tremendous growth. In 1998, Far West provided service to 8,400 water customers and 260 sewer customers. By 2005, Far West served 5,500 sewer customers. The shareholders of Far West are sisters Paula Capestro and Sandy Braden. Mr. Andrew Capestro is married to Paula Capestro and has been overseeing the Company during its sewer renovation project. Mr. Capestro does not receive compensation for operating the Company but does receive compensation when he performs services as a lawyer for the Company.

By its own admission, the Company was not able to keep up with the growth in its service area.[5] The Company came to have seven independently operating "package-type" treatment plants across its service territory. The Company's plants are known as Palm Shadows, which has a current average flow of 263,000 gallons per day ("gpd"); Section 14, with a current average flow of 102,000 gpd; Marwood, with a current average flow of 306,000 gpd; Del Oro, with a current average flow of 180,000 gpd; Del Rey, with a current average flow of 14,000 gpd; Villa Royale, with a current

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[4] Staff Closing Brief at 2.
[5] Far West Closing Brief at 4.

average flow of 10,000 gpd; and Seasons, with a current average flow of 73,000 gpd.[6]

Following customer complaints about odors and effluent quality, ADEQ investigated Far West's sewer operations.[7] On March 10, 2006, ADEQ entered into a Consent Order with Far West with respect to the Del Oro treatment facility. In that Consent Order, Far West was required to make short, medium and long-term measures to address operational, maintenance, capacity and permitting deficiencies associated with the Del Oro plant.[8]

In April 2006, after the Del Oro Consent Order, Far West states that it hired Coriolis, an engineering firm, to perform a "comprehensive review of the entire utility, water and sewer" including addressing the issues of the wastewater plants.[9] Far West claims, however, that before Coriolis could prepare a comprehensive engineering study, the Company had to address the issues surrounding the Del Oro treatment plant.[10] Far West claims it had to find a way to treat approximately 300,000 gpd at the Del Oro Plant, and with the assistance of Coriolis, was able to locate a temporary treatment facility. Far West was able to install the temporary plant at the Del Oro location and have it in operation prior to the deadline in the ADEQ Consent Order.[11] Far West states its next priority was solving a system wide odor problem, which resulted in the Company injecting bioxide chemicals throughout the system and installing carbon filters.[12]

According to the Company, Coriolis found that Far West had many more issues besides the Del Oro Treatment Plant, including issues facing the water division.[13] After addressing the deficiencies at the Del Oro Plant and the odor problems, the Company states it then proceeded to address longer-term goals of designing a water and water system, which would allow the Company to "get ahead of the curve and get this in a more management position."[14] Because the Company did not have proper plant inventories or maps of its systems, and had a hard time locating facilities for repair and maintenance and keeping track of customers, Coriolis recommended that Far West engage

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[6] Ex A-17, Wastewater flows at 2.
[7] Ex RCUO -1, Finance Application Docket No. WS-03478A-07-0442, Ex 3, ADEQ Consent Order.
[8] Ex R-1, attachment 3.
[9] Far West Closing Brief at 5 and 6.
[10] Far West Closing Brief at 6; Tr. at 660-670.
[11] Tr. at 355-56; 670.
[12] Far West Closing Brief at 6; Tr. at 660-670.
[13] Far West Closing Brief at 6; Tr. at 660-61.
[14] Tr. at 688.

in a mapping project and purchase new billing software.[15]

According to Far West, Coriolis determined that all of Far West's wastewater plants, except the Marwood plant, required major modifications. The engineers opined that Far West had too many treatment plants for the size of its service area. Far West claims that the hodgepodge of treatment plants was the result of the rapid development, with individual developers building the plant capacity that they needed for their individual developments and then contributing the plant to Far West.[16] In addition, the treatment systems were not working properly and could not easily be made to work properly.[17] Problems with the wastewater treatment plants included inadequate aeration in the tanks, and inadequate mechanisms for handling sludge and removing effluent. As a result, Far West's treatment plants were not meeting the applicable nitrogen requirements and were sometimes exceeding turbidity and fecal coliform limits.[18]

Coriolis designed a sewer renovation project which involves expanding the Section 14 plant, from a capacity of 150,000 gpd to 1.3 million gpd,[19] closing the Palm Shadows plant and diverting the flows that had been going to Palm Shadows to Section 14 for treatment. [20] The Palm Shadows plant would be decommissioned and converted to a lift station.[21] The Del Oro plant would be expanded from a capacity of 300,000 gpd[22] to 495,000 gpd, and the Villa Del Rey and Villa Royale flows would be diverted to the new Del Oro plant, and the Villa Del Rey and Villa Royale plants would be closed.[23] The temporary plant currently installed at Del Oro would be moved to the Seasons plant, which would expand that capacity from 70,000 gpd to 150,000 gpd.[24] In addition, some of the flows currently treated at the Marwood plant would also be diverted to the Section 14 Plant.[25]

In July 2006, the Company obtained the first of two bridge anticipation notes ("BANs"). The

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[15] Tr. at 683-84.
[16] Tr. at 673.
[17] Tr. at 664.
[18] Tr. at 665.
[19] Phase 1 expands Section 14 to 681,000 gpd, and Phase II increases the capacity to 1.3 mgpd.
[20] Tr. at 729-730.
[21] Tr. at 776.
[22] Del Oro is currently operating as a temporary plant with a capacity of 300,000 gpd.
[23] Ex A-19 at 2.
[24] Ex A-20.
[25] Tr. at 730

first BAN, was in the amount of $11.1 million, and was secured by the pledge of the shareholders' stock in Far West. The purpose of the first BAN was to allow Far West to begin funding the costs of the system-wide improvements, including design and engineering costs.

On October 25, 2006, Far West entered into a second Consent Order with ADEQ, which order superseded the first. The new Consent Order required Far West to apply for new or amended aquifer protection permits ("APPs") for the Del Oro, Seasons and Section 14 plants, as well as closure permits for the Villa Royale, Villa Del Rey and Palm Shadows plants. The Company was required to submit APP applications relating to these projects within 30 to 90 days. The Company met the deadlines for these submissions.[26]

On December 31, 2006, Far West closed on a second BAN for $17.7 million, which was secured by a pledge of the shareholders' stock. The purpose of the second BAN was to pay off the first BAN and provide additional funds to cover the costs of the ongoing water and sewer system renovation. Far West states that Coriolis' goal was to complete its work for Far West by February 2007.[27] Far West's shareholders used the BANs to continue the procurement process and begin construction. Far West determined that it would order plant prior to receiving ADEQ approval of the APPs.[28] The Company believed that they could start ordering equipment as long as it did not hook it up until after it received the APP approvals from ADEQ.[29]

In the Second Consent Order, ADEQ directed Far West to cease all construction-related activities, including procuring equipment until the APPs were issued.[30] Far West states that it tried to convince ADEQ to allow it to proceed at its own risk with construction activities, but ADEQ would not agree.[31] All construction and most procurement activities stopped until ADEQ issued the APPs. Far West states that it took ADEQ 18 months to issue all of the permits.[32]

During the period ADEQ had the APPs under review, Far West states that it undertook activities that did not require ADEQ permits, such as preparing sites for the renovation projects and

[26] Tr. at 799-821.
[27] Tr. at 734-35.
[28] Tr. at 478.
[29] Tr. at 478.
[30] Tr. at 477-78, 735-738.
[31] Tr. 477-78, 735-738.
[32] Tr. at 736.

preparing the long-range engineering study. Far West states that it also sought permanent financing for the system improvements. The Company obtained a commitment for the issuance of Industrial Development Authority ("IDA") bonds through the Yuma County IDA in the amount of $32.5 million.[33] The projects included in the request included "the acquisition, construction and installation of improvements to Far West's wastewater treatment plants and drinking water treatment system."[34]

The IDA financing required Commission approval and on July 26, 2007, Far West filed a Financing Application with the Commission.[35] Far West concluded that under its existing rates it might not be able to support a Financing Application with the Commission for the entire $32.5 million,[36] and thus, reduced its IDA funding request to a little more than $25 million.[37] The $25 million was intended to allow Far West to pay off an existing WIFA loan in the amount of $4.45 million (as required by the IDA bondholders), pay off the second BAN and construct the sewer system upgrades once ADEQ approved the APPs. Far West's Financing Application sought authority to "(1) issue evidence of indebtedness in an amount not to exceed $25,215,000 . . . for the purpose of constructing sewer system infrastructure improvement needed to ensure safe and reliable utility service and comply with the two Consent Orders between the Company and the Arizona Department of Environmental Quality ("ADEQ") and for the repayment and consolidation of certain existing debt, which was incurred by the Company on a short-term basis for similar purposes."[38] On October 30, 2007, in Decision No. 69950, the Commission authorized Far West to obtain the IDA financing.

The Company notes that in making its Financing Application with the Commission it stated that a portion of the IDA funds would be used to repay and consolidate the outstanding debt, which debt had been used in part for water system improvements. The Company states that by the time the IDA funds were taken down, the Company had already spent nearly $1 million to improve its water system, and had committed to spend roughly $1.8 million on water system related improvements.

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[33] Ex A-24; Tr. at 1040.
[34] Ex A-24; Tr. at 1037 and 1040.
[35] Docket No. WS-03478A-07-0442.
[36] Tr. at 1040-1045.
[37] Ex A-8 and Ex A-12.
[38] Ex R-1 at 1.

Far West states that it inadvertently omitted requesting authority to finance improvements to the water system as well as the sewer projects falling outside those improvements strictly necessary to comply with the Consent Order, when it requested financing authority from the Commission. It claims that the omission was its oversight, and that it never intended to act in a manner that was contrary to Decision No. 69950.[39]

Far West closed on the IDA bonds on or about December 13, 2007.[40] The Company incurred approximately $1.3 million in costs and fees to obtain the IDA bonds, which were paid from the bond proceeds. After paying off the $4.45 million WIFA loan, and the second BAN in the amount of $17.7 million, $8.5 million remained from the IDA bond proceeds to fund the construction project.

By mid-2007, the effluent ponds at the Palm Shadows plant had ceased to percolate, and the Company began to incur the costs of hauling effluent from the Palm Shadows treatment plant to the City of Yuma facilities. Far West utilized its affiliate, H&S Developers, a real estate development company, owned by the principals of Far West, to deliver the effluent from the Palm Shadows plant to the City of Yuma for disposal at a monthly cost of approximately $45,000, including the costs paid to the City. Far West states that by using H&S Developers, it was able to reduce its costs of hauling this effluent.[41]

In August 2008, ADEQ issued the last of the APPs and other approvals necessary for Far West to proceed with its wastewater treatment plant renovation project.[42] At this time, Far West began seeking bids for the project. Far West states that from the time it obtained the bonds and the time when it was able to bid the project, prices had increased dramatically, including prices for plastic and plastic piping, metals, electronics, and mechanical equipment, and the dollar had also lost significant strength against the Canadian dollar, which increased the cost of the membranes.[43] Far West asserts that additional costs resulted from requirements imposed in the ADEQ permits, including the construction of vadose wells.[44] Far West has identified total "cost overruns" over its

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[39] Tr. at 1035-38, 1041; Far West Closing Brief at 12, fn 66.
[40] Ex. A-12.
[41] Tr. at 984-85.
[42] Far West Closing Brief at 13; Tr. at 92, 97, 736.
[43] Tr. at 738-39.
[44] Tr. at 526-27. Vadose wells are used to recharge effluent into the aquifer. See Tr. at 725-26.

original estimates of approximately $4.5 million.[45]

Far West states that when it became aware of the amount of increased costs associated with the sewer improvement project, it tried to find additional funds to complete the project.[46] Mr. Capestro testified that by September 2008, the Company had a loan commitment from Wells Fargo Bank for an additional $5 million.[47] In late September 2008, however, ADEQ announced that it was filing a lawsuit against Far West for past violations and in October 2008, it was generally apparent that the national banking system was in trouble. Mr. Capestro testified that as a result of these two events, Wells Fargo withdrew its loan commitment.[48] Mr. Capestro claims Far West continued to seek additional funding by means of loans to the Company or its shareholder, but these efforts were unsuccessful.[49] In the meantime, the Company states it was incurring costs for equipment and construction and was rapidly depleting the remaining funds available from the IDA financing.

Far West estimates that it requires additional funds for the materials and labor necessary to complete the various plant projects as set forth below:[50]

	Open Invoices	Required to Complete	Total
Section 14 Phase 1 to 681,000 gpd	$2,416,002	$224,416	$2,540,418
Del Oro Phase 1 to 300,000 gpd	786,213		786,213
Seasons (not including electrical and mechanical – no contract at this time)	16,724	79,735	96,459
Palm Shadows	131,994	145,348	277,342
Del Rey and Royale		74,236	74,236
Total	$3,350,933	$523,735	$3,874,668
Section 14 Phase II to 1,300,000 gpd		$330,000	$330,000
Del Oro Phase II to 495,000 gpd		418,928	418,928

[45] Tr. at 616, Ex R-28.
[46] Far West Closing Brief at 14.
[47] Tr. at 313, 489, 528.
[48] Tr. at 489.
[49] Tr. at 311-13, 567-69, 618.
[50] Ex A-11.

Total	________	$748,928	$748,928
Grand Total	$3,350,933	$1,272,663	$4,623,596

Far West's Position

The Company requests a $2,161,788 revenue increase, which is a 101.95 percent increase over adjusted sewer division Test Year 2007 revenues. The Company states that its requested increase is premised on generating sufficient operating revenue to service the IDA debt and allow Far West to achieve zero Operating Income for its sewer division.[51]

Far West provided schedules which indicated that as of April 2009, it owed more than $3.3 million to vendors for equipment and construction of plant associated with the wastewater treatment renovations it states are necessary to comply with the Consent Order.[52] In addition, the Company claims it will need an additional $1.27 million to complete the renovation project.[53]

Far West provided evidence that by December 2008, when it filed its emergency request, it owed vendors nearly $2 million, and claimed that it was struggling to keep up with its operating expenses. At the hearing, Mr. Capestro testified it owes the Yuma Mesa Irrigation District ("YMID") $100,000 for purchased water, and $318,281 to Yuma County for property taxes.[54] The Company states that it has a projected cash flow shortage in excess of $6.4 million for 2009.[55] The Company argues that because it can no longer pay its debts as they come due in the ordinary course of business, Far West is insolvent.[56]

Far West asserts that it cannot complete the sewer renovations necessary to comply with the Consent Order. The Company claims that project vendors, who are owned significant sums for equipment already delivered, will not finish installation and start-up of the plant until they are paid.[57] Mr. Capestro testified that the shareholders infused $400,000 in capital to pay critical expenses, but claims to have depleted the shareholders' personal resources; and although they are willing to pledge

[51] Ex A-2, Bourassa Direct at 4.
[52] Ex. A-9.
[53] Ex A-11.
[54] Ex. A-1, Capestro Rebuttal at 3-7, Ex. A-5.
[55] Ex. S-3.
[56] Tr. at 122, 983, 898, 1132-33, 1231-33.
[57] Ex A-1 at 4; Tr. at 99.

stock or make personal guaranties, they have not been able to raise either equity or debt in sufficient sums to complete the project.[58]

Currently, Far West states that its wastewater system does not meet regulatory requirements and as a result its ability to maintain safe and reliable sewer service is in doubt.[59] Far West feels in limbo, unable to complete the project, while continuing to spend $45,000 to transport the effluent from the Palm Shadows plant to the City of Yuma for disposal. The Company also asserts that its inability to address needed water system improvements is problematic, and it is unknown how long water system improvements can be deferred without service problems.[60] The Company believes that if creditors force it into bankruptcy, the situation will worsen precipitously. The Company argues the constant threat of service interruptions is sufficient to warrant emergency relief.

Far West's proposal would have the interim rates effective until the Commission issues a decision in the Company's permanent rate case, and in the event the permanent rate case established rates that are less than the interim rates, the difference would be subject to refund with appropriate interest.[61] Far West claims its requested interim rate increase is intended to provide funds to pay the monthly debt service on the IDA bonds and achieve a 0.0 percent operating margin. The Company states that monthly debt service plus reserve payments on the IDA loans is $201,096.61, and at this time, the debt service amounts are not included in the Company's sewer rates. Far West argues that an interim rate increase equivalent to the debt service requirement would immediately free up that amount of funds which would be used to complete the treatment plant renovations.[62] In addition, the Company believes that the additional revenue stream would allow Far West to work out payment plans with vendors that want their bills paid before they will start-up the new plant.[63] The Company believes also that the additional revenue stream will give lenders comfort that Far West can make payments on a loan for the amount needed to finish the treatment plant renovations and comply with the Consent Order. Once the plant is in service, the Company states it will be able to obtain

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[58] Tr. at 570; 641-42.
[59] Far West Closing Brief at 18.
[60] Far West Closing Brief at 18.
[61] Far West Closing Brief at 18.
[62] Tr. at 566, 635, 983.
[63] Tr. at 540-541, 569, 887, 934.

permanent rate relief and earn a return on its investment.

Far West argues that its requested relief is authorized under Arizona law and within the scope of the Commission's regulatory authority. The Company argues that pursuant to Attorney General Opinion 71-17, interim rates may be authorized "as an emergency measure when sudden change brings hardship to a company, when the company is insolvent, or when the condition of the company is such that its ability to maintain service pending a formal rate determination is in serious doubt."[64] Far West asserts that while Attorney General Opinions are not binding, the Arizona Court of Appeals has cited with approval and followed this opinion.[65] Far West also argues the Commission may grant interim rates, when the Commission is unable to grant permanent rate relief within a reasonable time.[66]

Far West argues that RUCO's argument that capital investments are a shareholder responsibility is an over-simplification. Far West asserts that Far West cannot pay its day-to-day operating expenses due in large part to the debt service on the IDA bonds, on which it has been making monthly payments in excess of $200,000 for more than 18 months. Far West argues there is nothing wrong with the Commission issuing interim rate relief to help a utility complete a major construction project, citing Decision No. 61833 in which the Commission granted interim relief to Far West to secure financing for a water treatment plant, and Decision No. 53909 (January 30, 1984) that granted APS emergency rates "because severe cash flow restraints associated with extensive construction projects."

Far West claims that it agrees that the Company-wide cash flow should be considered, and that on a company-wide basis, its cash flow analysis shows that the Company will have a $6 million shortfall in 2009.[67] The Company states it has presented evidence that due to the problems of its sewer division, it cannot make critical improvements to its water infrastructure nor pay the full amount due for purchased water, or pay its company-wide property taxes.[68] Far West thinks that

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[64] Op. Att'y Gen. 71-17, at 50.
[65] *RUCO v. Ariz Corp. Comm'n*, 199 Ariz. 588, 591, 20 P.3d 1169, 1172 (App. 2001); *Scates v. Ariz Corp. Comm'n*, 118 Ariz. 531, 535, 578 P.2d 612, 616 (App. 1978).
[66] Op. Att'y Gen. 71-17 at 50.
[67] Ex S-3, Tr. at 1115.
[68] Far West Reply Brief at 6.

Staff and RUCO are distorting the severity of the company-wide crisis by focusing on the success of the water division. The Company states that on a stand-alone basis, the water division lowered the 2009 operating losses from nearly $3 million in the sewer division to under $1 million on a company-wide basis. Without the water division, Far West states it could not operate, nor could it have borrowed the money to make the improvements to the sewer division.[69]

The Company does not disagree that using a TIER or DSC analysis was appropriate to evaluate the financing application.[70] Far West argues, however, that it is also appropriate to consider other ways to evaluate the financial condition of the business in the context of its application for emergency relief. The Company argues that it cannot pay its bills as they come due and for the purposes of determining its solvency, whether the expenses are "above the line" or "below the line" is irrelevant because either way, Far West must pay these expenses.[71] Far West believes that Staff and RUCO place too heavy a reliance on the 2006 financial data used in the financing application and are ignoring current financial data that show a severe financial crisis. The Company refutes RUCO's claim that the ratios indicate that the Company's financial position has improved according to the financial ratios. Far West asserts that RUCO ignores the rate increase granted in 2007, and that since 2006, the Company has cut back on top management and other expenses in its control in an attempt to conserve cash.[72] Far West asserts that these cut-backs are not sustainable over time as its ability to maintain safe and reliable service will suffer. Far West argues the mere improvement in the TIER and DSC does not mean the Company is in better financial condition as the Company has provided evidence that the financial metrics mask the real cash flow problems that currently exist. Far West notes that in 2007, when the financing was approved, the Company was not late in paying its property taxes, or its water provider for Colorado River water or in paying refunds under its main extension agreements, and was not paying over $40,000 a month to dispose of effluent from its Palm Shadows facility, nor did it owe vendors more than $3 million.

In response to RUCO's claims of mismanagement and miss-spent funds, the Company argues

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[69] Ex A-3, Bourassa Rebuttal at 11-12; Tr. at 894, 972.
[70] Far West Reply Brief at 7.
[71] Far West Reply Brief at 8.
[72] Tr. at 537; Far West Reply Brief at 8-9.

that RUCO can criticize the Company's decisions only with the benefit of hindsight, and that such claims do not provide a basis to deny the interim relief.[73] Far West argues that the time to determine fault for the current financial crisis is during the prudency review in the Company's general rate case, but that the focus in the current proceeding is to determine if there is an emergency and whether emergency rates are warranted.

Far West claims Staff's remedy of obtaining an equity infusion is unrealistic, as the current shareholders do not have any more capital to invest and securing a private equity placement is highly unlikely given the Company's financial condition, that it has never paid dividends to shareholders, and reaching a positive return on investment is likely several years away.[74]

Finally, Far West argues the interim relief is not inequitable to ratepayers. It claims that it is simply asking that ratepayers start providing revenue to pay debt service on plant that the Company had to build in order to provide service to its customers.[75] The Company claims it will not earn a return as a result of the relief sought.[76]Absent the emergency relief, the Company argues the ratepayers are in the same sinking boat as the shareholders. Moreover, the Company states the interim rates are subject to refund so that ratepayers are fully protected when permanent rates become effective, which it argues makes the emergency rate relief far more equitable than the alternatives, including bankruptcy relief.

The Company seeks interim revenue of $2,161,788, an increase of 101.95 percent over 2007 adjusted test year revenues. The Company's current and proposed interim rates are set forth below:

	Current	Proposed	Increase	% Increase
Residential	$21.75	$45.54	$23.78	109.3
RV Park, per space	5.44	11.40	5.96	109.5
Commercial	43.50	91.18	47.68	109.6
Effluent (per acre foot)	325.85	325.85	0	0

[73] Far West Reply Brief at 12-14.
[74] Far West Reply Brief at 16.
[75] Tr. at 535.
[76] Tr. at 535-36, 612; Emergency App at 2; Bourassa Direct at 1-4.

Under these proposed rates, residential customers would see a monthly increase of $23.84, or 109.6 percent over current rates.[77]

RUCO's Position

First, RUCO argued that Far West's Application for Interim Rates is legally deficient on its face because the Company did not assert in its application that it was insolvent. RUCO noted that in the Emergency Application the Company asserted that an immediate increase in revenue was necessary to ensure that the Company did not become insolvent and unable to continue providing utility services to its customers. RUCO argued that the Company is entitled to receive interim rate relief when it can demonstrate that 1) an emergency exists; 2) a bond is posted guaranteeing refund if interim rates are *higher than final* rates determined by the Commission; and 3) the Commission undertakes to determine final rates after making a finding of fair value. However, RUCO argued that because the Company did not argue that it was currently insolvent, unable to provide service, or suffered from a sudden change resulting in hardship, its application was insufficient to grant relief and interim rates should be denied.[78]

Furthermore, RUCO argues the evidence presented in this proceeding shows that the Company is not insolvent. RUCO believes that the Company's ability to meet debt service and operating expenses should be evaluated on a company-wide basis, and not determined based on the operating results of the sewer division alone. RUCO argues that because the Company applied for the IDA bonds on a total company basis, the cash flows of both the water and sewer divisions should be available to satisfy the debt service. RUCO notes that the Company used $6.3 million of the IDA bonds to pay off a WIFA loan in the amount of $4.4 million and for water infrastructure projects unrelated to the ADEQ Consent Orders in the amount of $1.9 million.[79] RUCO asserts that because the water division received $6.3 million from the proceeds of the IDA bonds, its cash flows should be included in the determination of the Company's ability to meet debt service.

In addition, RUCO argues that the Company has sufficient cash flow to meet its operational expenses and its debt service and is not insolvent. RUCO calculated that Far West had free cash flow

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[77] Ex A-2 at 7-8.
[78] RUCO Initial Closing Brief at 2.
[79] Ex R-31; Tr. at 1074-1076.

of $674,756 in 2007 and $939,066 in 2008, after annual interest and principal payments.[80] RUCO asserts that when its witness, Mr. Rigsby, calculated the Company's cash flow, he included the payment of $326,702 in property taxes and $1,925,000 for principal and interest payments.[81] The Company claims that it is unable to pay $100,000 to the YMID for 2,500 acre feet of water. [82] RUCO states the Company has acknowledged that the additional 2,500 acre feet are not used.[83] RUCO asserts that this additional water is not used and useful and thus, the unpaid bill should not be considered in determining the Company's cash flow needs. RUCO claims that if the Company had prioritized operational expenses and debt service, it would not be facing shortfalls. According to RUCO, "poor planning on the part of Far West's management team does not constitute an emergency necessitating approval of the Company's request for a 101 percent increase in rates from ratepayers."[84]

Furthermore, RUCO questions why if cash flow is so tight, the Company's affiliates are not paying for amounts owing to Far West. According to RUCO, Far West's affiliate, H&S Developers, owns three golf courses, which as of February 2009, owed $253,172 for water.[85] Although Mr. Capestro testified that the unpaid golf course bills are setoff by work H & S Developers does for Far West, RUCO believes the financial statements refute that claim. According to RUCO, if Far West had applied a set off as suggested, H&S Developer's unpaid golf course bills would not be recorded as a Far West account receivable.[86]

RUCO claims that the DSC and TIER are the appropriate means to evaluate the Company's ability to meet operating expenses and debt service. RUCO states that when it approved Far West's application to borrow $25 million in IDA bonds, the Commission relied on TIER and DSC ratios to determine if the Company could meet its debt service requirements. RUCO asserts the DSC and TIER ratios from 2007 and 2008 indicate that Far West has the ability to cover its IDA bonds debt obligations. RUCO's witness testified that when Far West submitted its financing application, its pro

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[80] RUCO Initial Closing Brief at 6.
[81] Ex R-2; WAR-1.
[82] Tr. At 486.
[83] Id.
[84] RUCO Reply Brief at 7.
[85] Tr. At 164-171.
[86] RUCO Reply Brief at 8.

forma DSC was 1.15 and its TIER was 0.50. RUCO calculated that on a consolidated basis, the Company had a DSC of 1.35 and TIER of 0.77 in 2007 and DSC of 1.49 and TEIR of 0.89 in 2008.[87]

RUCO argues that using liquidity ratios, as contained in the Company's testimony, to analyze the Company's cash flows are not appropriate because they are based on the balance sheet which includes non-utility related liabilities and assets such as fines, restitutions and penalties. RUCO argues that regardless of which ratios are used, however, the ratios indicate that the Company has an improved financial condition since the finance application in 2007.[88]

RUCO argues that the Company's cash flow analysis is flawed. First, RUCO argues that the Commission should not consider extraordinary expenses resulting from the Company's mismanagement. RUCO notes that Mr. Bourassa, the Company's witness, testified that on a total Company basis in 2008, Far West lost $972,000 and had a positive cash flow of only $13,058.[89] RUCO's witness, Mr. Rigsby, testified that the Company had free cash flow of $674,756 in 2007 and $939,066 in 2008, after annual interest and principal payments.[90] RUCO states that the major difference between Mr. Bourassa and Mr. Rigsby is the treatment of extraordinary expenses. RUCO notes that typically, these expenses are "below the line" expenses and not collected from ratepayers. The bulk of the extraordinary expenses are attributable to hauling effluent from the Palm Shadows plant to the City of Yuma facilities. In 2007 and 2008, the Company spent $347,446 and $501,363, respectively, to collect and haul the effluent.[91] The Company spent $130,398 and $132,107 for legal fees in 2007 and 2008, respectively, associated with the defense of the Company's former president who was prosecuted in connection with the death of Company employees who were overcome by gasses in a confined space due to inadequate training and supervision.[92] RUCO asserts that the construction of percolation ponds on non-percolating soils which has led to the expense of hauling effluent from the Palm Shadows plant or the poor management that led to the death of an employee should not become the burden of ratepayers. RUCO believes these expenses result from the

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[87] Ex R-3 at 15. Schedule WAR-1.
[88] Tr. at 1059. RUCO Initial Closing Brief at 6-7.
[89] Ex A-3.
[90] Ex R-3 at 15, WAR-1; RUCO notes that Staff witness, Gerald Becker, estimated the Company's free cash flow for 2009 as $781,792.
[91] Ex R-18 and Ex R-19.
[92] Ex A-3, Exhibit 1.

mismanagement and negligence of Far West management. RUCO presented evidence that Far West hired the engineer that designed the Palm Shadows plant and that Far West applied for the permits for that plant, and furthermore, that the developer of the area, Palm Shadows Partnership, was related to Far West, in that Mr. Brent Wiedman, who was president of Far West at the time, was a director of H & S Developers and also a partner in Palm Shadows Partnership.[93] RUCO argues that the shareholders' inability or unwillingness to cover extraordinary expenses does not render the Company insolvent.[94]

Even though RUCO believes the extraordinary expenses should not be considered to determine if Far Wet has sufficient cash flow, Mr. Rigsby calculated the 2008 cash flow including the effluent disposal expense of $501,363 and excluding the below the line interest income. RUCO determined that after factoring in these expenses, the 2008 financial statements produce a DSC of 1.23 and TIER of 0.58. RUCO states these ratios are higher than those the Commission relied on in Decision No. 69950 when it approved the IDA financing. Thus, RUCO asserts, regardless of whether the extraordinary expenses are considered or not, the Company has more cash flow available now than it did in 2007.

RUCO also argues that complying with the ADEQ Consent Order does not constitute an emergency. RUCO asserts that capital investment is the responsibility of shareholders and should not be used as a basis for determining interim rates.[95] RUCO notes the Company spent $3.7 million on non-ADEQ required sewer and water projects,[96] and that this amount is roughly equal to the amount the Company owes in accounts payable. RUCO believes that the Company misspent the funds, and had it not, it would have sufficient funds available to complete the remaining work. RUCO notes that when the Commission approved the IDA financing, it authorized the indebtedness for three specific purposes: 1) sewer system improvements necessary to comply with ADEQ Consent Orders; 2) to retire a 1999 WIFA loan; and 3) to retire other short term debt incurred in December 2006 to undertake emergency sewer plant upgrades and improvements necessary to comply with the

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[93] RUCO Reply Brief at 5.
[94] RUCO Initial Closing Brief at 7.
[95] RUCO Initial Closing Brief at 10.
[96] RUCO Initial Closing Brief at 11.

requirements imposed by ADEQ.[97] RUCO believes the Commission should deny the request and is adamant that ratepayers should not be required to pay a 101 percent increase in interim rates to subsidize the shareholders' poor decision-making.

RUCO disputes an implication in the Company's testimony that the capital budget shortfalls were due to increased construction costs, when in RUCO's view, the Company's problems result primarily from its failure to abide by Decision No. 69950. RUCO notes that the Company used $1,883,593 of the IDA bond proceeds to fund water-related projects (including Design and Construction of the 4th Street Water Main Project) which were not priorities authorized by the Commission's order.[98] RUCO notes as well that the Company spent $357,059 on software programs for asset management and mapping, billing and fuel dispensing, and $379,487 on a Fortuna Road improvement project which was not an ADEQ mandated project.[99] By using these funds on "non-priority" projects, RUCO states the Company did not have these funds for the ADEQ sewer projects.

RUCO also believes that shareholder greed contributed to the Company's difficulties. RUCO argues that the Company designed the Section 14 plant to a capacity of 2.0 million gallons per day ("mgpd"), and built it to a capacity of 1.3 mgpd. RUCO asserts the Company spent $420,000 to engineer the expansion of the Section 14 plant from 1.3 mgpd to 2.0 mgpd.[100] RUCO notes that ADEQ did not mandate that the Section 14 plant be built at a 1.3 mgpd capacity, but accepted the Company's offer to build at that capacity.[101] RUCO believes that under ADEQ rules, the design flow of the plant only needs to cover current flows and any previously granted "capacity assurances."[102] According to RUCO, the evidence shows that the combined flows of the Palm Shadows and Section 14 plants are 274,000 gpd, which begs the question why the Company would design the new plant to 1.3 mgpd. RUCO asserts that the Company designed the new Section 14 plant to accommodate future development, and that Far West affiliates own many of the future real estate developments in the area.[103] RUCO also questions why Far West drew on IDA loan funds between August 19, 2008

[97] Decision No. 69950 at 2; Ex R-1 (Financing Application in Docket No. WS-03478A-07-0442).
[98] Ex A-8 at 7.
[99] Tr. at 773-74.
[100] Tr. at 513-14.
[101] Tr. at 446-447.
[102] RUCO Reply Brief at 13-14.
[103] RUCO Reply Brief at 14.

and September 8, 2008, after the Company learned that there would be a capital budget short-fall, to expand the Section 14 plant from 671,000 gpd to 2.0 million gpd, The Company spent $200,000 to purchase land from an affiliate to construct vadose recharge wells. RUCO notes they also drew on IDA loan funds for this purpose in October 2008, after the Company supposedly learned of the capital budget shortfalls.

RUCO alleges that although the ADEQ Consent Order mandated little change to the Marwood plant, the Company made significant expenditures to redirect Marwood flows to Section 14 in order to free capacity at Marwood to accommodate new development by the shareholders in the Marwood service area.[104] RUCO notes the Company used $607,381 of the IDA funds to develop the Paula Street Lift Station to redirect flows from Marwood to Section 14.[105]

RUCO notes further that prior to the ADEQ Consent Order, the Del Oro plant had a design flow of 300,000 gpd. Pursuant to the Consent Order, the Del Oro plant had to absorb 40,000 gpd redirected flows from the Del Rey and Villa Royale plants. According to the Company, the total average monthly flow at Del Oro under its new permit is 127,500 gpd, and yet, RUCO argues the Company redesigned Del Oro for a flow of 495,00 gpd.[106] The additional flow capacity will allow the addition of 1,780 new residences.[107] RUCO argues the costs for future expansion should fall on the subdivision developers, and not on current ratepayers.

RUCO asserts that the Far West shareholders have put their own interests above that of ratepayers. RUCO states that at the same time it encountered capital budget overruns and owes $3.4 million on accounts payable to project vendors, it made large payments to H & S Developers and its shareholders. According to RUCO, in 2007 Far West paid affiliates $1,462,684, and $920,651 in 2008 for accounts payable and a long-term loan owed to shareholders.[108]

Finally, RUCO argues there is no precedent established by Decision No. 61833, in which the Commission authorized interim rates to allow the Company to borrow funds to build a water treatment plant, or Decision No. 70667, in which the Commission granted APS interim rates to

[104] RUCO Reply Brief at 16.
[105] Ex A-8.
[106] Ex R-21 at 16.
[107] Ex R-12.
[108] RUCO Reply Brief at 18; Ex A-18; Tr. at 1189.

ensure its access to capital funds to develop renewable resources, that would compel approving interim rates in this case. RUCO argues the Commission decides each case on the record before it.

Staff's Position

Staff argues that although the Company provided financial statements that indicate the Company's sewer division had a loss of $2,161,788 in 2007, the Commission should look at the combined water and sewer results to determine whether there is an emergency. Staff asserts that a negative net income does not necessarily represent an emergency because non-cash expenses are considered in calculating net income.

Staff does not believe that the circumstances of this case "demonstrate the existence of an emergency, either current or pending, which would justify the requested relief."[109] Staff states that in 2007 when the Company sought authority to borrow the $25 million, Staff's analysis indicated that with the additional debt, the Company would have a TIER of 0.50 and a DSC of 1.15. Staff asserts that based on its analysis in the 2007 financing docket, Far West has the ability to remain financially viable until the Commission is able to conclude a permanent rate case. Staff believes it is inappropriate to view the financial health of only a single division of the company when determining the Company's overall financial health. Staff notes that whether Staff agrees or not that it was proper to use part of the $25 million in borrowed funds for water system improvements, there is little doubt that the funds were used for the benefit of both systems.

Staff argues that the only solution to the Company's current dilemma is for Far West to obtain a capital infusion to finance the remaining projects.[110] Staff notes that Far West currently only has approximately 7 percent equity in its capital structure. Staff believes that it is the Company's inadequate capitalization that has contributed to its current financial difficulties. Staff notes the Company has testified that it has been unable to find another lender because potential new lenders are unwilling to accept a second position in the Company's assets. In Staff's view, given the value of the Company's assets and the amount of debt they already secure, there is no equity remaining to provide security to a new lender,[111] and that even if the Commission were to authorize added revenue

[109] Staff Closing Brief at 5.
[110] Staff Closing Brief at 9.
[111] Staff Closing Brief at 8.

streams, it is highly unlikely that any bank will lend more money to the Company based on the financial statements presented at the hearing. Staff believes that if the Company's assertions are accurate, it cannot afford more debt. Staff argues that granting the requested relief would only increase the financial risk, and the Commission should act now to stop the Company from incurring additional debt. Staff believes it is patently unfair to ratepayers to treat them as guarantors of the Company, by bailing out the shareholders from the financial mess they have created.

Moreover, Staff argues that the Company should not come to the Commission seeking assistance to complete the wastewater improvement projects, at the expense of ratepayers, when it admitted that it used funds from the IDA funding on projects not related to the ADEQ Consent Order. Staff alleges that the Company has placed its own needs above those of the ratepayers. Staff notes that while it has funding needs of $4,623,566 (for past due invoices and necessary to complete the project), it paid H&S Developers $330,000, to pay back an advance so that Far West could hire Coriolis, and that in 2008, Far West paid off $920,000 in accounts payable and $571,244 for loan re-payment to affiliated companies.[112] In 2008, Staff notes that accounts receivable from H&S Developers increased by approximately $200,000, that is, it did not collected these funds from H&S. Thus, Staff calculates that of approximately $1.7 million of cash, that could have been used to comply with the Consent Order, paid to H & S Developers.[113]

Staff argues that Far West could accumulate the sums necessary to make the initial $400,000 down payment to the GE/Zenon that the Company believes would be sufficient to complete the project, from operational savings.[114] Staff believes that the Company would not have had its cash flow difficulties if it had not had to expend approximately $500,000 a year in sludge removal from the Palm Shadows plant. Staff believes it ironic that had GE/Zenon been paid and the Palm Shadow's plant been completed, Far West would have avoided the costs of hauling the effluent.

Staff states that the Company's current financial stress is the direct result of mismanagement of the IDA bond funds, and that had the Company limited its projects to those associated with the

[112] Tr. at 561.
[113] Staff Reply Brief at 3.
[114] Staff Reply Brief at 4.

ADEQ Consent Order, then the current situation would not have arisen.[115]

Although Staff does not believe the Far West situation is an emergency warranting interim rate relief, in the event the Commission found an emergency, Staff's analysis shows that instead of the Company's proposed increase of $2,161,788, an increase of $972,150, or 46.3 percent, would provide the Company with a projected net income of zero.[116] Staff states that with a net income of zero and non-cash expenses of $1,423,338, Far West would have adequate funds available for unexpected events/contingencies.[117]

Staff's alternative rates are set for below:

	Current	Proposed	Increase	% Increase
Residential	$21.75	$31.23	$9.48	43.6
RV Park, per space	5.44	7.81	2.37	43.6
Commercial	43.50	62.47	18.97	43.6
Effluent (per acre foot)	325.85	467.92	142.07	43.6

If the Commission finds interim rates to be warranted, Staff further recommends that: the Company maintain records that show the revenue generated each month by the interim rates authorized herein be segregated from all other revenue; that the rates be subject to refund plus interest; that the interim rate be subject to refund pending the Decision resulting from the 2008 Rate Case that has been filed but is presently suspended; that the Company post a bond or letter of credit with the Commission in the amount of $300,000, prior to implementing the emergency rate increase authorized in this proceeding;[118] the Company be directed to file, within 30 days of the Decision, a revised rate schedule reflecting the interim rate increase with Docket Control, as a compliance item in this docket; and that the Company notify its customers of the revised rates, and their effective date, in a form acceptable to Staff, by means of an insertion in the Company's next regularly scheduled billing.[119]

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[115] Staff Reply Brief at 4.
[116] Ex S-1 at 4.
[117] *Id.*
[118] Staff states that this amount is approximately 30 percent of the annual rate increase being approved, and Staff estimates that if approved, the interim rates would be in effect for approximately 12 months.
[119] Ex S-1 at 5.

Analysis and Resolution

The Company operates seven wastewater plants, all of which had deficiencies.[120] ADEQ entered into two Consent Orders with the Company in 2006, and directed Far West to bring all seven of its wastewater treatment plants into full compliance with ADEQ regulations. To achieve compliance, Far West determined to undertake extensive improvements to its wastewater system. Because the Company did not have sufficient funds to make the improvements without additional capital, the Company applied for authority to borrow $25,215,000. The Commission authorized the Company to borrow the funds for the purpose of completing the sewer system improvements necessary to comply with the ADEQ Consent Orders; to retire an existing WIFA loan in the amount of $4,686,466; to retire short-term debt incurred in December 2006 which was used to undertake emergency sewer plant upgrades and improvements necessary to comply with the ADEQ Consent Orders; to establish a $0.9 million debt service reserve fund; and pay $1.3 million in issuance costs.[121]

In December 2008, when it filed this emergency application, the Company asserted that it had essentially depleted the proceeds of the IDA loans, but that none of the projects had been completed. The Company estimates that an additional $4.6 million is needed to complete the improvements.[122] Although aspects of the project are close to completion, to date, Far West has not been able to negotiate with vendors to complete the work necessary to bring the project on-line. Far West believes it can complete the project if it can make a down payment on the amounts owed and show vendors an improved cash flow.

As part of its ratemaking authority, the Commission has the power to authorize interim rates when (1) there is an emergency; (2) a bond is posted by the utility to guaranty a refund to customers if the interim rates paid are higher than the final rates determined by the Commission; and (3) the Commission sets final rates based on the fair value of the utility's property."[123] An emergency exists "when sudden charge brings hardship to a company, when the company is insolvent, or when the

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[120] See Engineering Report, Docket No. WS-03478A-05-0801 (Financing Application).
[121] Decision No. 69950 at 2-3 and 5.
[122] Ex A-11.
[123] *RUCO v. ACC*, 20 P.3d 1169, 1173 (App. 2001).

condition of the company is such that its ability to maintain service pending a formal rate determination is in serious doubt."[124]

The Company offers evidence that it is insolvent as it cannot pay its bills as they come due and cannot complete the wastewater improvement plant that is necessary to comply with the ADEQ Consent Order. The Company presented evidence that it owes $3,350,933 to vendors on the sewer project and $318,281 to Yuma County and $100,000 to the YMID. Based on paying past due payables of $3,400,000, it projects a deficit cash flow of $6.4 million in 2009.

Despite the sums owed by the Company, neither Staff nor RUCO believe that Far West's circumstances constitute an emergency warranting interim relief. They assert that the Company's financial statements and financial metrics indicate that the Company has sufficient cash flow to continue operating until a permanent rate case can be completed. Both Staff and RUCO argue that neither the extraordinary expenses associated with hauling the effluent from the Palm Shadows plant, nor the costs of completing the sewer renovation project should be factored into the cash flow analysis. Staff and RUCO believe that the Company mismanaged the IDA bond funds by using them on projects not required to comply with the Consent Order and has put the interests of shareholders and affiliates over those of ratepayers and contractors. In addition, RUCO's investigation has raised serious questions about how much of the sewer renovation project was engaged in to serve existing customer and commitments, and how much was to serve future growth.

In 2008, on a Company-wide basis, Far West experienced operating income of $1,441,403, and a net loss of $809,863 on total income of $7,857,117.[125] The water division had net income of $1,766,803 and the sewer division had a net loss of $2,576,667.[126] With non-cash expenses of $1,423,338, the Company had a positive cash flow of $613,475 in 2008. The Company's inability to pay its obligations is traceable to its large capital improvement project and past due payables are overwhelmingly related to construction invoices. If not for the demands of the construction project, the Company would have had sufficient funds to pay its Property Taxes and the YMID. Far West's cash flow from operations is adequate to meet its on-going operating expenses, including its debt

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[124] Att'y Gen Op. 71-17 at 13.
[125] Ex-A-3, Exhibit 1.
[126] *Id.*

service.

Based on its current revenues and operating expenses, we agree with Staff and RUCO that there does not appear to be an emergency as the Company has the financial ability to continue providing service. However, the Company cannot complete the sewer renovation project and come into compliance with the ADEQ Consent Orders without an infusion of capital. Attempts to find new sources of debt or equity have been unsuccessful. Given the Company's high leverage and ongoing disputes with ADEQ, it would appear to be an unlikely candidate to receive additional debt or equity capital. Having depleted its options for additional debt and its ability to obtain additional capital from the shareholders, Far West turns to its ratepayers for a bailout.

The Company claims that if ratepayers can provide an additional revenue stream of $2.1 million, it will be able to complete the sewer projects necessary to comply with the ADEQ Consent Order. The additional requested revenue is not sufficient, however, to complete the projects in the near term, as the Company estimates the project will cost $4.6 million to complete. The Company suggests that the additional cash flow will allow it to obtain another loan, or at least convince its contractors to complete the project in return for partial payments on the amounts already owed. The Company has not submitted a loan commitment or agreement from its creditors, but merely the hope that if it approaches its vendors with a better cash flow that the vendors will agree to perform additional work for the Company. It is far from certain that the Company's plan would succeed. Based on the Company's performance to date in managing this project, we find little in the record that would allow a conclusion that it is even more likely than not to succeed. We are concerned that if the Commission approves the Company's request, ratepayers would end up paying more and still not receive the benefit of a complete and working wastewater treatment plant or a viable company.

Looking at the Company as a whole, and based on all of its activities, including its construction project, the Company has not paid its obligations as they come due. Thus, expanding the analysis beyond normal operations, the Company is insolvent, which is one of the conditions that can support an application for interim rate relief. For the reasons set forth below, however, we do not find it in the public interest to grant the requested interim relief at this time. Although the Company may be insolvent, the unpaid bills are overwhelmingly attributable to the construction project. The

Company has a positive cash flow from operations. This is not a case of operating expenses having increased so much that the Company cannot continue to provide service pending a traditional rate case. Neither is it a case of a sudden change that results in hardship. The Company's compliance deficiencies have been an issue for years, and the fact that the final construction budget increased in August 2008 after ADEQ approved the APPs was a foreseeable occurrence resulting from the delay.

We are concerned, however, about the public safety implication of this Company continuing to operate wastewater treatment plants with operational deficiencies. It is extraordinary to consider a request to have ratepayers to pay up front to construct utility plant. In was extraordinary in 1999 when we authorized interim rates in Decision No. 61833 for Far West to construct its water treatment plant. The circumstances of that 1999 case are distinguishable from those here, as at that time, we found a clear ratepayer benefit from allowing the Company to borrow the funds from WIFA to complete the plant. That ratepayer benefit is not obvious in the current case.

Current management has given us little comfort that with the funds they have requested, they would be able to complete the project or use ratepayer funds to the benefit of the ratepayers. Company projections assume continued pay down of affiliate payables. The shareholders claim to have exhausted their personal ability to contribute equity to Far West, but have not explained or demonstrated whether the Company's affiliates, including H & S Developers, could not and should not act as a source of capital. Before we can authorize the implementation of the interim rates, we would need the Company to provide proof, by means of audited financial statements, that neither the shareholders nor affiliate companies are able to provide the additional capital that they are requesting from ratepayers. In addition, we would need a plan that specifies the terms under which the Company's contractors would agree to complete the project. That being said, the additional $2.1 million requested by the Company, which results in a greater than 100 percent increase for ratepayers, is not reasonable. Although we reserve judgment on what, if any interim rate increase could ultimately be found in the public interest, we believe that Staff's recommended alternative position, which results in an increase of approximately $972,000, is more reasonable and in-line with prior Commission practice in analyzing interim requests.

Although the Company was reluctant to prioritize the projects, we believe that certain projects are more critical than others and could be completed first. By prioritizing the project, the Company may be able to complete the plant improvements without needing the entire $4.5 million at once. For instance, the Phase I of Section 14 plant is critical because it will take the flows from the malfunctioning Palm Shadows plant. Phase II of the Section 14 and Del Oro upgrades account for $1.2 million of the remaining $4.6 million, but it is not clear that these upgrades must be made immediately. The Company must devise a more detailed plan for how it can bring these plants on-line with realistic and reasonable assumptions.

Without additional information, we cannot find that interim relief is in the public interest.

This proceeding has raised the issue of whether the current management is able to manage the completion of the project. Consequently, we direct Staff to conduct an investigation and formulate a recommendation to the Commission whether it is in the public interest to have an interim operator appointed for the Company. One of the witnesses for the Company testified that he believed ADEQ had lost trust in the Company and was consequently unwilling to allow the Company latitude in commencing construction prior to the final approval of the APPs. Based upon the testimony and evidence presented in this case, this Commission has lost confidence in the Company's current management's ability to complete the sewer construction project and operate the company to the benefit of the ratepayers. The Company has engaged in many transactions with affiliates and there has not been adequate investigation whether the sums paid were fair and arms length. An interim manager, if one can be found, may be able to do much to restore the confidence of vendors and the Company's regulators.

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

FINDINGS OF FACT

1. On December 19, 2008, Far West filed with the Commission an emergency application for the immediate implementation of interim rates for sewer service, which rates would be effective until a Decision has been issued on the Company's application for permanent rate increase.

2. The Company filed an application for permanent rates on August 29, 2008, in Docket

No. WS-03478A-08-0454. By Procedural Order dated December 10, 2008, the permanent rate case was set for hearing to commence on July 29, 2009.

3. On January 13, 2009, Staff filed a Response to the emergency rate application. Staff also filed a Motion to Suspend Time Clock in the permanent rate case.

4. On January 20, 2009, Far West filed a "Motion to Consolidate; Combined Response to Staff's Motion to Suspend Time and Request for Scheduling Order." Far West filed its Request in both the emergency and permanent rate case dockets.

5. On January 21, 2009, RUCO filed in both dockets its "Response to Staff's Request to Suspend the Time Clock and the Company's Response."

6. On January 22, 2009, a Procedural Conference convened for the purpose of scheduling the interim rate case. Far West, Staff and RUCO appeared through counsel. RUCO, already an intervener in the permanent rate case, moved to intervene in the interim matter. Neither Far West nor Staff objected, and RUCO was granted intervention in the interim case.

7. By Procedural Order dated January 26, 2009, issued in Docket No. WS-03478A-08-0454, the proceedings in the permanent rate case were suspended pending the conclusion of the emergency case.

8. By Procedural Orders dated January 26, 2009, and January 28, 2009, in the interim rate docket, the hearing for the interim request was set to commence on April 6, 2009, at the Commission's Tucson offices, a schedule for pre-filed testimony was established, the March 5, 2009 public comment meeting in the permanent rate case in Yuma was expanded to include the interim rate request, and Far West was directed to provide public notice of the interim proceeding.

9. On March 11, 2009, Far West filed a Notice of Filing Certification of Publication and Proof of Mailing, indicating that notice was mailed to customers on February 17, 2009, and published it the *The Sun*, a newspaper of general circulation in Yuma, Arizona, on February 19, 2009.

10. On March 19, 2009, intervention was granted to Seth and Barbara Davis, residential customers of the Company.

11. The Commission received a great number of customer responses in opposition to both the interim and permanent rate requests. In addition, on March 5, 2009, the Commission convened a

Public Comment meeting in Yuma, at which many hundreds of people attended. In general, customers were shocked and angered about the size of the requested increase, expressed service-related concerns and were very suspicious, and sought investigation of the Company's transactions with its shareholders and companies affiliated with its shareholders.

12. On March 19, 2009, RUCO filed the Direct Testimony of William Rigsby, and on March 24, 2009, Staff filed the Staff Report of Gerald Becker.

13. On March 31, 2009, Far West filed the Rebuttal Testimony of Andrew Capestro and Thomas Bourassa.

14. The hearing commenced on April 6, 2009, and continued on April 7, 2009, May 12 - 14, 2009, and May 21, 2009.

15. On June 22, 2009, Far West, Staff and RUCO filed their Initial Briefs. Staff filed its Reply Brief on July 2, 2009, and RUCO and Far West filed their Reply Briefs on July 9, 2009.

16. Far West is located in Yuma County and provides water utility service to approximately 15,000 customers and sewer utility service to approximately 7,300 of those customers.

17. The Company is seeking an emergency rate increase designed to produce additional revenue of $2,161,788 on an annual basis. The Company claims its request would result in a zero Operating Income. The requested increase would be a 101.95 percent increase over current sewer division revenues.

18. On March 10, 2006, ADEQ entered into a Consent Order with Far West with respect to the Del Oro treatment facility. In that Consent Order, Far West was required to make short, medium and long-term measures to address operational, maintenance, capacity and permitting deficiencies associated with the Del Oro plant.

19. In April 2006, after the Del Oro Consent Order, Far West hired Coriolis, an engineering firm, to perform a "comprehensive review of the entire utility, water and sewer" including addressing the issues of the wastewater plants. With the assistance of Coriolis, Far West found a temporary solution to the operational deficiencies of the Del Oro plant and addressed odor issues plaguing the Company, and later developed a comprehensive sewer renovation project as discussed herein.

20. In July 2006, the Company obtained the first of two BANs. The first BAN was in the amount of $11.1 million, and was secured by the pledge of the shareholders' stock in Far West. The purpose of the first BAN was to allow Far West to begin funding the costs of the system-wide improvements, including design and engineering costs.

21. On October 25, 2006, Far West entered into a second Consent Order with ADEQ, which order superseded the first. The new Consent Order required Far West to apply for new or amended APPs for the Del Oro, Seasons and Section 14 plants, as well as closure permits for the Villa Royale, Villa Del Rey and Palm Shadows plants.

22. In the Second Consent Order, ADEQ directed Far West to cease all construction-related activities, including procuring equipment, until the APPs were issued. Far West could not convince ADEQ to allow it to proceed at its own risk with construction activities. Far West states that all construction on the Consent Order projects and most procurement activities stopped until ADEQ issued the APPs.

23. On December 31, 2006, Far West closed on a second BAN for $17.7 million, which was secured by a pledge of the shareholders' stock. The purpose of the second BAN was to pay off the first BAN and provide additional funds to cover the costs of the ongoing water and sewer system renovation. Far West's shareholders used the BANs to continue the procurement process and begin construction. Far West determined that it would order plant prior to receiving ADEQ approval of the APPs. The Company believed that it could start ordering equipment as long as it did not hook it up until after it received the APP approvals from ADEQ.

24. During the period ADEQ had the APPs under review, Far West sought permanent financing for the system improvements. The Company obtained a commitment for the issuance of IDA bonds through the Yuma County IDA.

25. On July 26, 2007, Far West filed a Financing Application with the Commission for authority to issue evidence of indebtedness in an amount not to exceed $25,215,000 for the purpose of constructing sewer system infrastructure improvements needed to ensure safe and reliable utility service and comply with the two Consent Orders and for the repayment and consolidation of the BANs. On October 30, 2007, in Decision No. 69950, the Commission authorized Far West to obtain

the IDA financing.

26. The Company used the IDA bond funds to pay off the BANs and an existing WIFA loan and to construct portions of the sewer renovation project that did not require ADEQ approval.

27. ADEQ issued the final permits in August, 2008.

28. After ADEQ approved the final APPs, Far West began seeking bids for the project, and discovered that from the time it first obtained the bonds and the time when it was able to bid the project, prices had increased dramatically due to price increases for materials and the devaluation of the U.S. dollar against the Canadian dollar.

29. The Company discovered that the IDA loan proceeds would not be sufficient to complete the project and tried to secure additional financing. The Company claims that despite its efforts, neither the Company, nor its shareholders have been unable to secure additional equity or debt capital that would allow it to complete the projects required under the second ADEQ Consent Order.

30. Far West provided evidence that it owes contractors on the project $3,350,933 and that an additional $1,272,663 is required to complete the project.

31. Far West states that its contractors will not agree to complete their work on the project without a substantial down payment on past due invoices.

32. In addition, the Company owes Yuma County $318,281 and the YMID $100,000 for Colorado River water.

33. In 2008, on a Company-wide basis, Far West experienced operating income of $1,441,403, and a net loss of $809,863 on total income of $7,857,117. The water division had net income of $1,766,803 and the sewer division had a net loss of $2,576,667. With non-cash expenses of $1,423,338, the Company had a positive cash flow of $613,475 in 2008.

34. Based on the Company-wide financial statements for 2007 and 2008, which indicate a positive cash flow, neither Staff nor RUCO believe that Far West is facing an emergency that casts doubt on its ability to continue providing service pending a permanent rate case.

35. The Company's revenues from operations are sufficient to meet its operating expenses and its debt service.

36. The Company has depleted its IDA loan proceeds prior to completing the sewer renovation project and cash from operations is not sufficient to complete the project.

37. While cash flow from operations is sufficient for this Company to continue operations, the continued operation of wastewater treatment plants that do not comply with ADEQ regulations creates a serious issue of public health and safety.

38. As discussed herein, the Company has not demonstrated that it cannot raise additional capital from its shareholders or affiliated companies, and has not offered a reasonable plan for how the sewer renovation project will be completed even with the assistance of an interim rate increase.

39. Without additional information, we cannot find that interim relief is in the public interest.

40. This proceeding has raised issues concerning the ability of the current management to manage the completion of the project, and it is reasonable to direct Staff to conduct an investigation and formulate a recommendation to the Commission, in the permanent rate case or sooner, whether it is in the public interest to have an interim operator appointed for the Company.

CONCLUSIONS OF LAW

1. Far West is a public service corporation pursuant to Article XV of the Arizona Constitution and A.R.S. §§ 40-250 and 40-251.

2. The Commission has jurisdiction over Far West and the subject matter of the application.

3. Notice of the proceeding was provided in conformance with law.

4. The interim rates proposed by the Company are not just and reasonable and are not in the public interest.

ORDER

IT IS THEREFORE ORDERED that the application of Far West Water and Sewer Company for an interim rate increase of $2,161,788 is denied.

IT IS FURTHER ORDERED that within 30 days of the Effective Date of this Decision, Far West Water and Sewer Company shall supplement the record with additional evidence of the ability of its shareholders and/or affiliates to provide capital to Far West Water and Sewer Company and a more detailed and comprehensive plan on how the sewer improvements will be completed.

IT IS FURTHER ORDERED that Staff shall investigate and formulate a recommendation to the Commission, in the permanent rate case or sooner, about whether it is in the public interest to appoint an interim manager for this Company, and any other appropriate recommendations.

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

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN

COMMISSIONER

COMMISSIONER

COMMISSIONER

COMMISSIONER

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

ERNEST G. JOHNSON
EXECUTIVE DIRECTOR

DISSENT ____________________

DISSENT ____________________

DECISION NO. 71447

SERVICE LIST FOR: FAR WEST WATER AND SEWER COMPANY

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