

ORIGINAL



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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

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

IN THE MATTER OF THE APPLICATION OF SOUTHLAND UTILITIES COMPANY, INC. FOR AUTHORITY TO INCUR LONG-TERM DEBT.

DOCKET NO. W-02062A-09-0466

IN THE MATTER OF THE APPLICATION OF SOUTHLAND UTILITIES COMPANY, INC. FOR A RATE INCREASE.

DOCKET NO. W-02062A-09-0515

STAFF'S NOTICE OF FILING DIRECT TESTIMONY

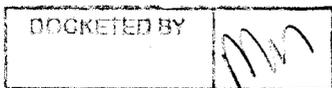
The Utilities Division of the Arizona Corporation Commission ("Staff") hereby files the Direct Testimony of Staff Witnesses Juan C. Manrique, Gerald W. Becker, and Katrin Stukov in the above-mentioned matter.

RESPECTFULLY SUBMITTED this 19th day of July, 2010.

Arizona Corporation Commission

DOCKETED

JUL 19 2010



Robin R. Mitchell
Attorney, Legal Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007
(602) 542-3402

Original and thirteen (13) copies of the foregoing filed this 19th day of July, 2010, with:

Docket Control
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

AZ CORP COMMISSION
DOCKET CONTROL

2010 JUL 19 P 4: 54

RECEIVED

1 Copy of the foregoing mailed this
2 19th day of July, 2010, to:

3 Steve Wene, Esq.
4 MOYES SELLERS & SIMS
5 1850 North Central Avenue, Suite 1100
6 Phoenix, Arizona 85004

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Southland Utilities Company, Inc. Staff Report	Exhibit 1
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**EXECUTIVE SUMMARY
SOUTHLAND UTILITIES COMPANY, INC.
DOCKET NOS. W-02062A-09-0466 AND W-02062A-09-0515**

The Testimony of Staff witness Juan C. Manrique addresses the following issues:

Financing – Staff recommends that the Commission authorize Southland Utilities Company, Inc. to incur long-term debt with the Water Infrastructure Finance Authority in the amount of \$1,825,941 and to encumber utility assets in conjunction with the loan.

1 **I. INTRODUCTION**

2 **Q. Please state your name, occupation, and business address.**

3 A. My name is Juan C. Manrique. I am a Public Utilities Analyst employed by the Arizona
4 Corporation Commission (“ACC” or “Commission”) in the Utilities Division (“Staff”).
5 My business address is 1200 West Washington Street, Phoenix, Arizona 85007.

6
7 **Q. Briefly describe your responsibilities as a Public Utilities Analyst.**

8 A. In my position as a Public Utilities Analyst, I perform studies to estimate the cost of
9 capital component in rate filings to determine the overall revenue requirement and analyze
10 requests for financing authorizations.

11
12 **Q. Please describe your educational background and professional experience.**

13 A. I graduated from Arizona State University and received a Bachelor of Science degree in
14 Finance. My course of studies included courses in corporate and international finance,
15 investments, accounting, statistics, and economics. I began employment as a Staff Public
16 Utilities Analyst in October 2008. My professional experience includes two years as a
17 Loan Officer with a homebuilder and as an Associate for an Investor Relations firm.

18
19 **Q. What is the scope of your testimony in this case?**

20 A. My testimony provides Staff’s recommended long-term debt authorization and
21 encumbrance of assets for Southland Utilities Company, Inc. (“Southland”).

22
23 **Q. Have you prepared any exhibits to accompany your testimony?**

24 A. I have prepared and attached a Staff Report and Schedule detailing these
25 recommendations.

1 **Q. Does this conclude your testimony?**

2 **A. Yes, it does.**

MEMORANDUM

TO: Gerald W. Becker

FROM: Juan C. Manrique *no for*
Public Utilities Analyst I
Utilities Division

DATE: July 19, 2010

RE: STAFF REPORT FOR THE APPLICATION OF SOUTHLAND UTILITIES
COMPANY, INC. FOR AUTHORITY TO INCUR LONG-TERM DEBT (DOCKET
NOS. W-02062A-09-0466 AND W-02062A-09-0515)

Attached is the Staff Report for the Southland Utilities Company, Inc.'s application for authority to borrow funds from the Water Infrastructure Finance Authority of Arizona. Staff recommends conditional approval.

Any party who wishes may file comments to the Staff Report with the Commission's Docket Control by 4:00 p.m. on or before July 27, 2010.

SO:JCM:kdh

Originator: Juan C. Manrique

Service List for: Southland Utilities Company, Inc.
Docket Nos. W-02062A-09-0466 and W-02062A-09-0515

Mr. Steven Wene
Moyes Sellers & Sims
1850 North Central Avenue, Suite 1100
Phoenix, Arizona 85004

**STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION**

SOUTHLAND UTILITIES COMPANY, INC.

**DOCKET NOS. W-02062A-09-0466
W-02062A-09-0515**

**APPLICATION FOR AUTHORITY
TO
INCUR LONG-TERM INDEBTEDNESS**

JULY 19, 2010

STAFF ACKNOWLEDGMENT

The Staff Report for Southland Utilities Company, Inc., Docket Nos. W-02062A-09-0466 and W-02062A-09-0515, is the responsibility of the Staff members listed below. Juan C. Manrique is responsible for the financial analysis.

Nancy Scott for

JUAN C. MANRIQUE
PUBLIC UTILITIES ANALYST I

EXECUTIVE SUMMARY
SOUTHLAND UTILITIES COMPANY, INC.
DOCKET NOS. W-02062A-09-0466 AND W-02062A-09-0515

On September 30, 2009, Southland Utilities Company, Inc. ("Southland" or "Company"), filed an application with the Arizona Corporation Commission ("Commission") requesting authorization to execute a loan agreement with the Water Infrastructure Finance Authority of Arizona ("WIFA") for \$2,233,796. On April 12, 2010 Southland filed an amended application requesting the amount of indebtedness changed to \$1,825,941.

The Company is a for-profit Class "C" Arizona public service corporation that owns and operates a public water utility in the area of Sierra Vista, Arizona. The Company seeks a \$1,825,941 WIFA loan. A 20-year amortizing loan at approximately 5.25 percent per annum is anticipated. The purpose of the loan is to fund system improvements and repay a previous loan used to replace a failing and inadequate storage tank. The system improvements include the acquisition of an onsite generator, connecting an additional storage tank to the system and replacing 40-year old, failing asbestos-cement pipelines.

Staff calculated pro forma debt service coverage ("DSC") ratio of negative 0.02 under the Company's current rates and repayment of its current outstanding loan. This DSC pro forma is below the WIFA requirement of 1.2, and it shows that cash flow from operations is not sufficient to cover all obligations, including WIFA's requirement to fund a "Debt Service Reserve Fund" equal to 20 percent of debt service. However, Southland has a pending rate case with the Commission (Docket No. W-02062A-09-0515).

Using Staff's recommended operating income of \$41,798 in the pending rate case; Staff calculated the maximum amount the Company can borrow and maintain a 1.2 Debt Service Reserve Fund is \$780,000. Under this scenario, Staff calculated a pro forma capital structure of 2.4 percent short-term debt, 79.4 percent long-term debt and 18.2 percent equity; and a pro forma 1.25 DSC. Under this scenario, the DSC results show that cash flow from operations would be sufficient to cover all obligations including a maximum loan amount of \$810,000.

Since the Company is requesting a loan in the amount of \$1,825,941, a separate funding source is required to make up the difference. In the pending rate case, Staff is recommending a surcharge to cover the remaining part of the loan that cannot be paid through Staff's recommended operating income.

Staff concludes that the Company's proposed capital projects are appropriate and that the related cost estimates are reasonable.

Staff further concludes that issuance of the proposed debt financing for the purposes stated in the application is within Southland's corporate powers, is compatible with the public interest, will not impair its ability to provide services and is consistent with sound financial practices provided Staff's recommended operating income and surcharge amounts are adopted in the current rate case.

Staff recommends authorization to incur an 18-to-22 year amortizing loan in an amount not to exceed \$1,825,941 and at an interest rate not to exceed that which is available from WIFA.

Staff further recommends that the Commission authorize Southland to pledge its assets in the State of Arizona pursuant to A.R.S. § 40-285 and R18-15-104 in connection with the WIFA loan.

Staff further recommends that any authorization to incur debt granted in this proceeding terminate on June 30, 2013.

Staff further recommends authorizing Southland to engage in any transaction and to execute any documents necessary to effectuate the authorizations granted.

Staff further recommends that Southland file with Docket Control, as a compliance item in this matter, copies of the loan documents within 60 days of the execution of any financing transaction authorized herein.

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INTRODUCTION

On September 30, 2009, Southland Utilities Company, Inc. ("Southland" or "Company"), filed an application with the Arizona Corporation Commission ("Commission") requesting authorization to execute a loan agreement with the Water Infrastructure Finance Authority of Arizona ("WIFA") for \$2,233,796. On April 12, 2010 Southland filed an amended application requesting the amount of indebtedness changed to \$1,825,941.

PUBLIC NOTICE

On May 19, 2010, the Company filed an affidavit of publication verifying public notice of its financing application. The Company published notice of its financing and rate applications in the *Sierra Vista Herald* and *Bisbee Daily Review* on May 5, 2010. Both are newspapers of general circulation and are published six days a week in the Cities of Sierra Vista and Bisbee, County of Cochise, Arizona. The affidavit of publication is attached along with a copy of the Notice.

BACKGROUND

The Company is a for-profit Class "C" Arizona public service corporation that owns and operates a public water utility in the area of Sierra Vista, Arizona.

COMPLIANCE

A check of the Compliance Database indicates that there are currently no delinquencies for Southland Utilities Company, Inc.

PURPOSE AND DESCRIPTION OF THE REQUESTED FINANCING

The purpose of the loan is to fund system improvements and repay a previous loan used to replace a failing and inadequate storage tank. The system improvements include the acquisition of an onsite generator, connecting an additional storage tank to the system and replacing 40-year old, failing asbestos pipelines.

The Company requests that the Commission authorize it to secure financing in an amount not to exceed \$1,825,941 from WIFA. The Company expects a 20-year amortizing loan at 5.25 percent per annum. The current base interest rate on a WIFA loan is 5.25 percent. The base interest rate is calculated by using the current prime rate of 3.25 percent plus 2.00 percent.

ENGINEERING ANALYSIS

Staff reviewed the Company's proposed capital improvements and found the project appropriate and the related cost estimates reasonable. Staff makes no "used and useful" determination of the proposed improvements nor any conclusions for rate base or ratemaking purposes. (see Staff's Engineering Report)

FINANCIAL ANALYSIS

Staff's analysis is illustrated on Schedules JCM-1. Column [A] of the schedule reflects the Company's historical financial information for the year ended December 31, 2008, and Column [B] presents pro forma financial information that modifies Column [A] to reflect Staff's recommendation in the pending rate case (W-02062A-09-0515) of \$41,798 and a 20-year, \$780,000 amortizing loan at 5.25 percent. This is the maximum loan amount the Company can support with Staff's operating income recommendation and still maintain WIFA's 1.2 "Debt Service Reserve Fund". Therefore, a separate funding source is required to make up the difference between the \$780,000 the Company can borrow under Staff's operating income recommendation in the current rate case and the \$1,825,941 the Company is requesting. This difference is to be made up by a surcharge that Staff is recommending in the current rate case.

DSC

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

Schedule JCM-1, Column [A] shows that for the year ended December 31, 2008, the Company's DSC was -0.02. The pro forma DSC for the Company under the scenario described above for Column [B] is 1.25.

Capital Structure

As of December 31, 2008, the Company's capital structure consisted of 74.0 percent short-term debt, 0.0 percent long-term debt, and 26.0 percent equity (Schedule JCM-1, Column [A], lines 19-25). Staff calculated a pro forma capital structure reflecting issuance of a \$810,000, 20-year amortizing loan at 5.25 percent per annum, and it is composed of 2.4 percent short-term debt, 79.4 percent long-term debt and 18.2 percent equity (Schedule JCM-1, Column [C], lines 19-25).

Capital Structure inclusive of AIAC and CIAC

As of December 31, 2008, the Company's capital structure, inclusive of Advances-In-Aid-of-Construction ("AIAC") and Net Contributions-In-Aid-of-Construction ("CIAC")¹ consisted of 73.0 percent short-term debt, 0.0 percent long-term debt, 25.6 percent equity, 0.5 percent AIAC and 0.9 percent CIAC (Schedule JCM-1, Column [A], lines 30-40).

Encumbrance

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

CONCLUSION AND RECOMMENDATIONS

Staff concludes that the Company's proposed capital projects are appropriate and that the related cost estimates are reasonable.

Staff further concludes that issuance of the proposed debt financing for the purposes stated in the application is within Southland's corporate powers, is compatible with the public interest, will not impair its ability to provide services and is consistent with sound financial practices provided Staff's recommended operating income and surcharge amounts are adopted in the current rate case.

Staff recommends authorization to incur an 18-to-22 year amortizing loan in an amount not to exceed \$1,825,941 and at an interest rate not to exceed that which is available from WIFA.

Staff further recommends that the Commission authorize Southland to pledge its assets in the State of Arizona pursuant to A.R.S. § 40-285 and R18-15-104 in connection with the WIFA loan.

Staff further recommends that any authorization to incur debt granted in this proceeding terminate on June 30, 2013.

Staff further recommends authorizing Southland to engage in any transaction and to execute any documents necessary to effectuate the authorizations granted.

¹ Contributions in Aid of Construction less Accumulated Amortization of Contributions in Aid of Construction.

Southland Utilities Company, Inc.

Docket No. W-02062A-09-0466

Page 4

Staff further recommends that Southland file with Docket Control, as a compliance item in this matter, copies of the loan documents within 60 days of the execution of any financing transaction authorized herein.

FINANCIAL ANALYSIS

Southland Utilities Company, Inc.
Selected Financial Information

	[A] ¹ <u>12/31/2008</u>		[B] ² <u>Pro Forma</u>	
1	Operating Income	-\$26,864		\$41,798
2	Depreciation & Amort.	\$15,153		\$30,612
3	Income Tax Expense	\$0		\$6,304
4				
5	Interest Expense	\$0		\$40,410
6	Repayment of Principal	\$494,622		\$22,662
7				
8				
9				
10				
11	DSC			
12	[1+2+3] ÷ [5+6]	-0.02		1.25
13				
14				
15				
16				
17	Capital Structure			
18				
19	Short-term Debt	\$494,622	74.0%	\$22,662 2.4%
20				
21	Long-term Debt	\$0	0.0%	\$757,338 79.4%
22				
23	Common Equity	\$173,443	26.0%	\$173,443 18.2%
24				
25	Total Capital	\$668,065	100.0%	\$953,443 100.0%
26				
27				
28	Capital Structure (inclusive of AIAC and Net CIAC)			
29				
30	Short-term Debt	\$494,622	73.0%	\$22,657 2.4%
31				
32	Long-term Debt	\$0	0.0%	\$757,338 78.7%
33				
34	Common Equity	\$173,443	25.6%	\$173,443 18.0%
35				
36	Advances in Aid of Construction ("AIAC")	\$3,182	0.5%	\$3,182 0.3%
37				
38	Contributions in Aid of Construction ("CIAC") ³	\$6,196	0.9%	\$6,196 0.6%
39				
40	Total Capital (Inclusive of AIAC and CIAC)	\$677,443	100.0%	\$962,816 100.0%
41				
42				
43	AIAC and CIAC Funding Ratio⁴	1.4%		1.0%
44	(36+38)/(40)			
45				
46				

47 ¹ Column [A] is based on audited 2008 financial information for the year ended December 31, 2008.

48 ² Column [B] reflects the issuance of \$810 Thousand Loan at 5.25 percent.

49 ³ Net CIAC balance (i.e. less: amortization of contributions).

50 ⁴ Staff typically recommends that combined AIAC and Net CIAC funding not exceed 30 percent of total capital,
51 inclusive of AIAC and Net CIAC, for private and investor owned utilities.

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1 Steve Wene, No. 019630
2 MOYES SELLERS & SIMS LTD.
3 1850 N. Central Avenue, Suite 1100
4 Phoenix, Arizona 85004
5 (602)-604-2189
6 swene@lawms.com
7 Attorney for Southland Utilities Company, Inc.

RECEIVED

2010 MAY 19 A 9:41

AZ CORP COMMISSION
DOCKET CONTROL

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

9 KRISTIN K. MAYES, CHAIRMAN
10 GARY PIERCE
11 PAUL NEWMAN
12 SANDRA D. KENNEDY
13 BOB STUMP

Arizona Corporation Commission

DOCKETED

MAY 19 2010

DOCKETED BY

14 IN THE MATTER OF THE APPLICATION OF
15 SOUTHLAND UTILITIES COMPANY, INC.
16 FOR AUTHORITY TO INCUR LONG-TERM
17 DEBT.

DOCKET NO. W-02062A-09-0466

18 IN THE MATTER OF THE APPLICATION OF
19 SOUTHLAND UTILITIES COMPANY, INC.
20 FOR A RATE INCREASE.

DOCKET NO. W-02062A-09-0515

**NOTICE OF FILING OF
AFFIDAVIT OF MAILING AND
AFFIDAVIT OF PUBLICATION**

21 Pursuant to procedural order dated March 24, 2010, the Southland Utilities
22 Company, Inc. ("Company"), hereby files the affidavit of mailing and the affidavit of
23 publication, set forth in Exhibits 1 and 2, respectively, verifying that the Company has
24 mailed to each known customer the customer notification and published the public notice
25 in the Sierra Vista Herald and Bisbee Daily Review.
26
27
28

1 RESPECTFULLY SUBMITTED this 19th day of May, 2010.

2 **MOYES SELLERS & SIMS Ltd.**

3
4 

5 Steve Wene
6 1850 North Central Avenue
7 Suite 1100
8 Phoenix, Arizona 85004
9 swene@lawms.com
10 Attorney for Southland Utilities Company, Inc.

11 Original and 15 copies of the foregoing
12 filed this 19th day of May, 2010, with:

13 Docket Control
14 Arizona Corporation Commission
15 1200 West Washington
16 Phoenix, Arizona 85007

17 Copy of the foregoing mailed this
18 19th day of May, 2010, to:

19 Janice Alward, Chief Counsel
20 Legal Division
21 Arizona Corporation Commission
22 1200 W. Washington Street
23 Phoenix, Arizona 85007

24 Steven M. Olea, Director
25 Utilities Division
26 Arizona Corporation Commission
27 1200 West Washington Street
28 Phoenix, Arizona 85007



AFFIDAVIT OF PUBLICATION

STATE OF ARIZONA)
COUNTY OF COCHISE)

PAMELA M. MCELROY

[Signature]

being first

ly sworn, deposes and says: That (he) (she) is the Agent to the Publisher of the

PUBLIC NOTICE

PUBLIC NOTICE OF HEARING ON THE RATE APPLICATION AND FINANCING APPLICATION OF

SOUTHLAND UTILITIES COMPANY, INC., DOCKET NOS. W-02062A-09-0466 AND W-02062A-09-0515 On September 29, 2009, Southland Utilities Company, Inc. ("Company") filed an application with the Arizona Corporation Commission ("Commission") for authority to incur long-term debt in the amount of \$2,233,796 to finance water system improvements.

On November 5, 2009, the Company filed an application with the Commission for a rate increase and on November 23, 2009, the Company filed an amended rate application. On April 12, 2010, the Company filed a second amended rate application. In the second amended rate application, the Company requests an approximate 255.02 percent increase in revenue (\$358,072). Under the Company's proposal, the typical residential customer on a 5/8 x 3/4-inch meter, using an average of 6,412 gallons per month, would experience a monthly increase of \$45.65, or 246.38 percent, from \$18.53 to \$64.18, and the typical residential customer on a 5/8 x 3/4-inch meter, using a median of 4,256 gallons per month, would experience a monthly increase of \$40.00, or 255.42 percent, from \$15.68 to \$55.66.

If you have any questions concerning how the Company's financing and/or rate proposals will affect your bill or have other substantive questions about this application, you may contact the Company at: P.O. Box 85160, Tucson, Arizona 85754, 520-523-5172, playere@southwesternutility.com

The Commission's Utilities Division Staff has not yet made recommendations regarding the Company's financing and rate increase proposals, and the Commission will determine the appropriate relief to be granted based on the evidence of record in this proceeding. The Commission is not bound

by the proposals made by the Company, Staff, or any intervenors and, therefore, the final rates approved in this docket may be lower or higher than the rates described above.

How You Can View or Obtain a Copy of the Financing and/or Rate Proposals: Copies of the application and proposed tariffs are available at the Company's offices at 2102 N. Forbes Blvd., Ste. 107, Tucson, Arizona 85745 and at the Commission's Docket Control Center at 1200 West Washington Street, Phoenix, Arizona and its Tucson offices, 400 West Congress, Suite 218, Tucson, Arizona and on the Internet via the Commission website (www.szc.gov) using the e-docket function.

Public Hearing Information: The Commission will hold a hearing on this matter beginning August 31, 2010, at 10:00 a.m., at the Commission's offices, Room 222, 400 West Congress, Tucson, Arizona. Public comments will be taken at the beginning of the first day of the hearing. Written public comments may be submitted by mailing a letter referencing Docket Nos. W-02062A-09-0466 and W-02062A-09-0515 to Arizona Corporation Commission, Consumer Services Section, 1200 West Washington Street, Phoenix, Arizona 85007, or by e-mail. For a form to use and instructions on how to e-mail comments to the Commission, go to http://www.szc.gov/divisions/utilities/forms/public_comment.pdf. If you require assistance, you may contact the Consumer Services Section at 1-800-222-7000 or (520) 628-8550.

About Intervention: The law provides for an open public hearing at which, under appropriate circumstances, interested parties may intervene. Any person or entity entitled by law to intervene and having a direct and substantial interest in the matter will be permitted to intervene. If you wish to intervene, you must file an original and 13 copies of a written motion to intervene with the Commission no later than July 2, 2010, and a copy of the motion to CWCGV of its counsel and to all parties of record.

Your motion must contain the following:

- 1. Your name, address, and telephone number and the name, address and telephone number of any party upon whom service of documents is to be made, if not yourself.
2. A short statement of your interest in the proceeding (e.g., a customer of the Company, a shareholder of the Company, etc.).
3. A statement certifying that you have mailed a copy of the motion to intervene to the Company or its counsel and to all parties of record in the case.

The granting of motions to intervene shall be governed by A.A.C. R14-3-105, except that all motions to intervene must be filed on or before July 2, 2010. If representation by counsel is required by Rule 31 of the Rules of the Arizona Supreme Court, intervention will be conditioned upon the intervenor obtaining counsel to represent the intervenor. For information about requesting intervention, visit the Commission's website at http://www.szc.gov/divisions/utilities/forms/intervene.n.pdf.

The granting of intervention, among other things, entitles a party to present sworn evidence at the hearing and to cross-examine other witnesses. However, failure to intervene will not preclude any interested person or entity from appearing at the hearing and providing public comment on the application or from filing written comments in the record of the case.

ADA/Equal Access Information: The Commission does not discriminate on the basis of disability in admission to its public meetings. Persons with a disability may request a reasonable accommodation such as a sign language interpreter, as well as request this document in alternative format, by contacting the ADA Coordinator Shyrin Bemal, email Sbermal@azcc.gov, voice phone number 602-542-3931. Requests should be made as early as possible to allow time to arrange the accommodation. PUBLISH: May 5, 6, 7, 2010

ERRA VISTA HERALD and the BISBEE DAILY REVIEW newspapers printed and published six days a week in the County of Cochise, State of Arizona, and of general circulation in the cities of Sierra Vista and Bisbee, County of Cochise, State of Arizona and elsewhere, and hereto attached

PUBLIC NOTICE OF SOUTHLAND UTILITIES COMPANY, INC DOCKET NOS.

W-02062A-09-0466 s printed and published correctly in the regular and entire issue of said SIERRA VISTA

RALD and BISBEE DAILY REVIEW for 3 issues, that the first was

ide on the 5th day of MAY 20 10

the last publication thereof was made on the 7th day of

MAY 20 10 that said publication

s made on each of the following dates, to wit:

- 05/05/10
05/06/10
05/07/10

quest of

Sierra Vista Herald Bisbee Daily Review

[Signature]

scribed sworn to before me this 7th day of MAY

10



Notary Public in and for the County of Cochise, State of Arizona

My Commission Expires:

5/21/12

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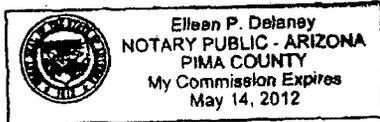
AFFIDAVIT

STATE OF ARIZONA)
)
County of Pima) ss.

I, the undersigned, after being first duly sworn upon my oath, hereby affirm as follow:

- 1) I am over the age of eighteen.
- 2) I have personal knowledge of the statements set forth herein and I am competent to testify at a hearing or trial with respect to the same.
- 3) I certify that on behalf of Southland Utilities Company, Inc., on APRIL 22, 2010, I mailed, or caused to be mailed, to each Company customer a copy of the Customer Notification attached hereto.

DATED this 18 day of MAY, 2010.



Bonnie O'Connor
Bonnie O'Connor, President
Southwestern Utility Management, Inc.

SUBSCRIBED AND SWORN TO before me, a Notary Public, this 18 day of MAY, 2010.

Eileen P. Delaney
Notary Public

My Commission Expires:
May 14, 2012

BEFORE THE ARIZONA CORPORATION COMMISSION

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

IN THE MATTER OF THE APPLICATION OF)
SOUTHLAND UTILITIES COMPANY, INC.)
FOR AUTHORITY TO INCUR LONG-TERM)
DEBT.)

DOCKET NO. W-02062A-09-0466

IN THE MATTER OF THE APPLICATION OF)
SOUTHLAND UTILITIES COMPANY, INC.)
FOR A RATE INCREASE)

DOCKET NO. W-02062A-09-0515

DIRECT
TESTIMONY
OF
GERALD W. BECKER
PUBLIC UTILITIES ANALYST V
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION

JULY 19, 2010

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EXECUTIVE SUMMARY
SOUTHLAND UTILITIES COMPANY, INC.
DOCKET NOS. W-02062A-09-0515 AND W-02062A-09-0466

Southland Utilities Company, Inc. ("Southland" or "Company") is an Arizona public service corporation that provides water utility service to an average of 612 customers in an area located approximately five miles south of Sierra Vista, Arizona.

On September 29, 2009, Southland filed with the Arizona Corporation Commission ("Commission") an application for authority to incur long-term debt ("Financing Application").

On November 5, 2009, Southland filed with the Commission an application for a rate increase, and on November 23, 2009, Southland filed an amended rate application (together with the original rate application, the "Rate Application").

On December 18, 2009, the Commission's Utilities Division Staff ("Staff") filed its Sufficiency Letter indicating that Southland's Rate Application was sufficient under the Arizona Administrative Code ("A.A.C."), and classified the Company as a Class C utility.

On December 28, 2009, a Procedural Order was issued directing consolidation of the two dockets.

On December 30, 2009, a Procedural Order was filed setting a hearing for this matter for June 15, 2010, and setting other procedural deadlines.

On March 17, 2010, the Company filed a Motion to Extend Deadlines ("Motion"), requesting that all deadlines in this matter be extended for 60 to 90 days, and on March 25, 2010, a Procedural Order was issued re-setting the hearing for August 31, 2010, and scheduling other procedural deadlines.

On April 12, 2010, the Company filed an Amended Finance Application and a Second Amended Rate Application.

In its original application, the Company proposes a revenue increase of \$512,124 or 364.73 percent, from \$140,411 to \$652,535. In its Second Amended Application, the Company proposes a revenue increase of \$358,072, or 255.02 percent, from \$140,411 to \$498,483. The Company's proposed revenues include amounts needed to pay the debt service on an anticipated WIFA loan it requested authorization to obtain in the consolidated Docket No. W-02062A-09-0466. Staff witness Juan Manrique is presenting testimony on that financing request. The Company's proposed revenue increase would produce an operating income of \$180,760 for an 8.91 percent rate of return on an original cost rate base ("OCRB") of \$2,029,253.

Staff's revenue requirement is comprised of a permanent requirement and a surcharge requirement to service the WIFA loan of \$1,825,941. Staff recommends a permanent revenue component of \$284,608 which represents an increase of \$144,197, or 102.7 percent, for a 10.00

percent rate of return on a Staff-adjusted OCRB of \$417,978. The Company proposes to use OCRB as its Fair Value Rate Base.

(Info on typical bills to be added or filed separately with Rate Design.)

1 **INTRODUCTION**

2 **Q. Please state your name, occupation, and business address.**

3 A. My name is Gerald Becker. I am a Public Utilities Analyst V employed by the Arizona
4 Corporation Commission ("ACC" or "Commission") in the Utilities Division ("Staff").
5 My business address is 1200 West Washington Street, Phoenix, Arizona 85007.

6
7 **Q. Briefly describe your responsibilities as a Public Utilities Analyst V.**

8 A. I am responsible for the examination and verification of financial and statistical
9 information included in utility rate applications. In addition, I develop revenue
10 requirements, and prepare written reports, testimonies, and schedules that include Staff
11 recommendations to the Commission. I am also responsible for testifying at formal
12 hearings on these matters.

13
14 **Q. Please describe your educational background and professional experience.**

15 A. I received a Masters of Business Administration with an emphasis in Accounting from
16 Pace University. I am a Certified Public Accountant and a Certified Internal Auditor.

17
18 I have participated in multiple rate, financing and other regulatory proceedings. I attended
19 the National Association of Regulatory Utility Commissioners ("NARUC") Utilities Rate
20 School.

21
22 I began employment with the Commission as a utilities regulatory analyst in April 2006.
23 Prior to joining the Commission, I worked as an Auditor at the Department of Economic
24 Security and Department of Revenue in the Taxpayer Assistance Section. Prior to those
25 jobs, I worked for 15 years as an Auditor, Analyst, Financial Analyst, and Budget
26 Manager at United Illuminating, an investor-owned electric company in New Haven, CT.

1 **Q. What is the scope of your testimony in this case?**

2 A. I am presenting Staff's analysis and recommendations in the areas of rate base, operating
3 revenues and expenses, the permanent component of the recommended revenue
4 requirement, rate design and a surcharge to recover the debt service on the proposed
5 WIFA loan, regarding the application of Southland Utilities Company, Inc ("Southland"
6 or "Company"). This application was consolidated with an application to incur long-term
7 debt (Docket No. W-02062A-09-0466). Staff witness Juan Manrique is presenting Staff's
8 analysis and recommendations regarding the Company's application to incur long term
9 debt. Staff witness Katrin Stukov is presenting Staff's engineering analysis and
10 recommendations.

11

12 **Q. What is the basis of your recommendations?**

13 A. I performed a regulatory audit of Southland's application to determine whether sufficient,
14 relevant, and reliable evidence exists to support the Company's requested rate increases.
15 The regulatory audit consisted of examining and testing the financial information,
16 accounting records, and other supporting documentation and verifying that the accounting
17 principles applied were in accordance with the Commission-adopted NARUC Uniform
18 System of Accounts ("USOA").

19

20 **BACKGROUND**

21 **Q. Please describe the Company's operations.**

22 A. Southland is an Arizona public service corporation that provides water utility service to an
23 average of 612 customers in an area located approximately five miles south of Sierra
24 Vista, Arizona.

1 **Q. What are the primary reasons for the Company's requested permanent rate**
2 **increase?**

3 A. The Company's application states it is seeking a rate increase to pay for needed system
4 upgrades and improvements. The Company states that it had previously borrowed
5 \$494,922 to pay for the cost of a failing and inadequate storage tank and to purchase
6 another storage tank to alleviate concerns caused by high demand in the summer months.
7 The Company wants to repay this short-term loan with a WIFA loan. In addition to the
8 \$494,922, the Company seeks to borrow an additional \$1,331,320 which would be used to
9 acquire an on-site generator, to replace failing asbestos-cement pipelines, and to connect
10 the additional storage tank that has already been purchased. The Company's application
11 does not separate the requested increase into permanent and surcharge components, in the
12 way that Staff suggests. Instead, the Company seeks an increase to cover both
13 components.
14

15 **CONSUMER SERVICE**

16 **Q. Please provide a brief history of customer complaints received by the Commission**
17 **regarding Southland.**

18 A. Staff reviewed the Commission's records for the period January 1, 2007, through July 15,
19 2010 and found:

20 2007 – Zero Complaints, Inquiries or Opinions;

21 2008 – One Complaint (quality of service), 2 Inquiries (rates) and zero Opinions;

22 2009 – One Complaint (billing), Zero Inquiries or Opinions;

23 2010 – One Complaint (billing), Seven Inquiries (Five ACC questions, One rate
24 case item, One quality of service), Nine Opinions opposed to this
25 application;
26

1 All complaints have been resolved and closed.

2

3 **SUMMARY OF PROPOSED REVENUES**

4 **Q. Please summarize the Company's filing.**

5 A. The Company proposes to include the anticipated improvements in its rate base of
6 \$2,029,252 earning a rate of return of 5.43 percent. The Company proposes a rate
7 increase of \$253,313, or 180.41 percent over test year revenues of \$140,411.

8

9 **Q. Please summarize Staff's recommended revenue.**

10 A. Staff recommends that the increase be segregated into a permanent component and a
11 surcharge component to provide supplementary debt service on the proposed \$1,825,941
12 WIFA loan. The permanent component represents an increase of \$144,197, or 102.7
13 percent over test year revenues of \$140,411, and would provide a 10.0 percent rate of
14 return on the \$444,587 rate base.

15

16 **Q. What Test Year did the Company utilize for this filing?**

17 A. Southland's rate filing is based on the twelve months ended December 31, 2008 ("test
18 year").

19

20 **Q. Please summarize the rate base and operating income recommendations and
21 adjustments addressed in your testimony for Southland.**

22 A. A summary of my testimony on rate base and operating income is represented below:

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Staff-Recommended Rate Base Adjustments:

Plant in Service – Adjustment no. 1 adds \$45,222 to restate the cost of the storage tank at site no. 2, based on the engineering analysis.

Plant in Service, Accumulated Depreciation, Contributions in Aid of Construction and Accumulated Amortization-CIAC – Adjustment no. 2 records the retirement of a \$21,024 (restated amount resulting from rate base adjustment no. 1) storage tank that was fully depreciated and originally funded by CIAC. The adjustment reduces plant, accumulated depreciation, CIAC and accumulated amortization of CIAC by \$21,024, and it has no impact to rate base.

Plant in Service – Adjustment no. 3 transfers \$27,782 from Account 330000, Distribution Reservoirs and Standpipes to Account 330100, Storage Tanks.

WIFA Construction and Property Held for Future Use – Adjustment no. 4 removes \$1,634,244 of anticipated future plant that is not currently used and useful for the provision of service.

Plant in Service and Accumulated Depreciation – Adjustment no. 5 increases plant and accumulated depreciation by \$2,663 to correct the overstated value of retirements to Account 304000, Structures and Improvements.

Working Capital – Adjustment no. 5 removes the \$22,252 portion of the proposed Working Capital that was calculated using the formula method.

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Staff-Recommended Operating Income Adjustments:

Water Testing Expense – Adjustment no. 1 decreases Chemicals/Water Testing Expense by \$3,129 to reflect the on-going expense recommended by Staff.

Fuel and Power Expense – Adjustment no. 2 increases Fuel and Power Expense by \$1,521 to reflect correction of an error in the Company’s filing identified in the Company’s response to Staff data request GWB 4.4.a.

Outside Services and General Office Expense – Adjustment no. 3 has no net impact on test year expenses, as it reclassifies \$2,800 from General Office Expense to Outside Services.

Depreciation Expense – Adjustment no. 4 decreases Depreciation Expense by \$42,587 to reflect application of Staff’s recommended depreciation rates to Staff’s recommended plant balances in this proceeding.

Income Tax Expense – Adjustment no. 5 increases income taxes by \$45,760 to reflect the application of statutory State and Federal income tax rates to Staff’s test year taxable income.

RATE BASE

Q. Did the Company prepare a schedule showing the elements of Reconstruction Cost New Rate Base?

A. No, the Company did not. The Company requested that its OCRB be treated as its fair value rate base.

1 **RATE BASE ADJUSTMENTS**

2 **Q. Is Staff proposing any adjustments to rate base in this system?**

3 A. Yes.

4
5 **Q. Please summarize Staff's adjustments to Southland's rate base shown in Schedules**
6 **GWB-3, GWB-4, GWB-5, GWB-6, GWB-7, GWB-8, GWB-9 and GWB-9A.**

7 A. Staff's adjustments to the Company's rate base result in a net decrease of \$1,566,296,
8 from \$2,029,252 to \$444,595. This decrease was due to recalculating the value of the
9 storage tank at Site #2, removing plant that is expected to be built in the future, correcting
10 the recorded value of certain plant retirements, and recalculating cash working capital.

11
12 **Rate Base Adjustment No. 1 – Plant in Service**

13 **Q. What did the Company propose for Plant in Service for Account 330100 Storage**
14 **Tanks?**

15 A. The Company proposed a balance of \$302,926 for account 330100.

16
17 **Q. What is the nature of Staff's adjustments to this plant account?**

18 A. During its engineering review, Staff determined that the value of the new storage tank
19 should be \$348,148. Rate Base Adjustment no. 1 increases the balance of this account
20 from \$302,926 to \$348,148.

21
22 **Q. What does Staff recommend?**

23 A. Staff recommends increasing the balance of this account from \$302,926 to \$348,148, as
24 shown in Schedules GWB-4 and GWB-5.¹

25

¹ Storage Tanks is further decreased by \$348,148 to \$0 by Staff rate base adjustment no. 3.

1 **Rate Base Adjustment No. 2 – Plant in Service, Accumulated Depreciation, CIAC, and**
2 **Accumulated Amortization-CIAC.**

3 **Q. Does the Company's application accurately reflect the amount for Plant in Service**
4 **for Account 330000, Distribution Reservoirs and Standpipes currently providing**
5 **service?**

6 A. No. The Company proposes a balance of \$48,806 for account 330000. Staff's
7 engineering review revealed that this account includes the value of the old storage tank
8 that was removed from Site #2 when the new storage tank at Site #2 was installed. (See
9 also Adjustment no. 1 and the testimony of Staff's Engineering witness.) The value of the
10 unrecorded retirement is \$21,024. Further, the tank had originally been funded by CIAC
11 and, at the time of the retirement, the tank was fully depreciated and the associated CIAC
12 was fully amortized. Rate Base Adjustment no. 2 removes \$21,024 from each associated
13 account including: plant account 330000 Distribution Reservoirs and Standpipes;
14 Accumulated Depreciation; CIAC; and Accumulated Amortization-CIAC, as shown in
15 Schedules GWB-4 and GWB-6.

16
17 **Q. What does Staff recommend?**

18 A. Staff recommends decreasing the balances of these account by \$21,024, as shown in
19 Schedules GWB-4 and GWB-6. This adjustment reduces the balance of account 330000,
20 Distribution Reservoirs and Standpipes by \$21,024 from \$48,806 to \$27,782,²
21 Accumulated Depreciation by \$21,204 from 398,206 to \$377,182,³ CIAC by \$21,024
22 from \$105,798 to \$84,774, and Accumulated Amortization-CIAC by \$21,024 from
23 \$99,602 to \$78,578.

24

² Distribution Reservoirs and Standpipes is further adjusted downward by \$27,782 to \$0 by Staff rate base adjustment no. 3.

³ Accumulated Depreciation is further adjusted upward by \$2,663 to \$379,845 by Staff rate base adjustment no. 5.

1 **Rate Base Adjustment No. 3 – Plant in Service**

2 **Q. Is there an additional adjustment to Account 330000, Distribution Reservoirs and**
3 **Standpipes?**

4 A. Yes.

5
6 **Q. Please explain.**

7 A. Yes. Account 330000, Distribution Reservoirs and Standpipes, is a capstone account for
8 two types of storage tanks (storage tanks in Account 330100 and pressure tanks in
9 Account 330200). Subsequent to Staff rate base adjustment no. 2, the balance in Account
10 330000, Distribution Reservoirs and Standpipes is \$27,782. Staff determined that this
11 remaining \$27,782 in the account pertains to the storage tank at Site #1 and reclassified
12 the balance to Account 330100, Storage Tanks, as reflected in Rate Base Adjustment no. 3
13 and in Schedule GWB-7.

14
15 **Rate Base Adjustment No. 4 – WIFA Construction and Plant Held for Future Use**

16 **Q. What did the Company propose for WIFA Construction and Plant Held for Future**
17 **Use Plant in Service?**

18 A. The Company proposed a total of \$1,634,244 for these items.

19
20 **Q. Is it normal ratemaking practice to include in rate base contemplated future plant**
21 **that is not providing service to customers?**

22 A. No. Only plant that is providing service to customers should be included in rate base.

23
24 **Q. What does Staff recommend?**

25 A. Staff recommends removing all of the Company's proposed \$1,634,244 pro forma
26 increase to rate base related to these items, as shown in Schedules GWB-4 and GWB-8.

1 **Rate Base Adjustment No. 5 – Plant in Service and Accumulated Depreciation**

2 **Q. What did the Company propose for Plant in Service for Account 304000 Structures**
3 **and Improvements?**

4 A. The Company proposed a balance of \$1,725 for accounts 304000, Structures and
5 Improvements.

6
7 **Q. Did Staff identify any errors in the Company's proposed amount for this account?**

8 A. Yes. In response to Staff Data Request GWB4.6, the Company indicated that it overstated
9 the value of a retirement to this account— \$19,824 as compared with the correct amount
10 of \$17,161—a difference of \$2,663. Adjustment no. 5, shown in Schedule GWB-9,
11 corrects the excessive amount recorded by the Company to both the plant and accumulated
12 depreciation accounts.

13
14 **Q. What does Staff recommend?**

15 A. Staff recommends increasing the balances of Structures and Improvements and
16 Accumulated Depreciation by \$2,663, as shown in Schedules GWB-4 and GWB-9.

17
18 **Rate Base Adjustment No. 6 – Working Capital**

19 **Q. Please describe the working capital component of rate base.**

20 A. Working capital is a collective term that typically includes amounts for prepaid expenses,
21 materials and supplies inventory, and cash working capital.

22
23 **Q. How did Southland calculate the cash working capital it proposes to include in rate**
24 **base?**

25 A. In this case, the Company uses the so-called formula method to calculate its working
26 capital requirement. This method calculates cash working capital by using 1/24 of

1 Purchased Power, 1/24 of Purchased Water 1/8 of Operation and Maintenance Expense,
2 and to this subtotal, adds the value of Material and Supplies Inventories and Prepayments.
3

4 **Q. Is the formula method proposed by the Company a preferred method for calculating**
5 **a cash working capital allowance for a Class C utility?**

6 A. No, although the formula method is typically used for Class D and E utilities, it is not a
7 method typically used for Class A, B and C size companies. The formula method always
8 results in a positive outcome. There is no basis for presuming that there is a need for
9 ratepayers to provide a cash working capital allowance for large utilities. In fact, since
10 several relatively large expenses (e.g., property and income taxes) are usually paid long
11 after cash is received from ratepayers, a negative cash working capital requirement is
12 reasonably expected. Cash working capital requirements are best determined by a lead-lag
13 study. In the absence of a lead-lag study demonstrating otherwise, there is no reason to
14 expect a positive cash working capital requirement consistent with the outcome of the
15 Company's proposed formula method.
16

17 **Q. Can Staff cite any instance when the Commission has adopted Staff's**
18 **recommendation to remove the cash working capital allowance from a Class C water**
19 **company's rate base because it had not performed a lead-lag study?**

20 A. Yes, the Commission in Decision No. 69404 dated April 16, 2007, (page 7, beginning at
21 line 15), adopted Staff's recommendation to remove Goodman Water Company's cash
22 working capital allowance because it had not performed a lead-lag study.
23

24 **Q. Does Staff have any objection to the Materials and Supplies Inventories and**
25 **Prepayment portions of the Companies proposed working capital allowance?**

26 A. No.

1 **Q. What does Staff recommend?**

2 A. Staff recommends decreasing the Company's proposed \$22,501 working capital
3 allowance by \$22,252 to \$249 to remove the portion related to use of the formula method,
4 as shown in Schedules GWB-4 and GWB-9A.

5

6 **OPERATING INCOME ADJUSTMENTS**

7 **Q. Please summarize the results of Staff's examination of test year operating income.**

8 A. Staff determined a test year operating loss of \$62,041, a \$1,565 greater loss than the
9 Company's proposed \$60,476 operating loss. Staff's recommendation results from the
10 five operating income adjustments described below.

11

12 **Operating Income Adjustment No. 1 – Water Testing Expense**

13 **Q. What is the Company proposing for Water Testing Expense?**

14 A. Southland is proposing water testing expenses of \$6,087 in the test year.

15

16 **Q. Does Staff agree with the Company's proposed amount?**

17 A. No. Staff has recalculated a reasonable on-going Water Testing Expense of \$2,958, or
18 \$3,129 less than the Company's proposed amounts.

19

20 **Q. What is Staff recommendation for Water Testing Expense?**

21 A. Staff recommends a decrease to Chemical/Water Testing Expense of \$3,129, from \$6,087
22 to \$2,958, as shown in Schedule GWB-12.

23

24 **Operating Income Adjustment No. 2 – Fuel and Power Expense**

25 **Q. What is the Company proposing for Fuel and Power Expense?**

26 A. For the test year, the Company proposes \$28,895 for Fuel and Power Expense.

1 **Q. Does Staff agree with the Company's proposed amount?**

2 A. No. In response to Staff data request GWB 4.4.a, the Company indicated that it had
3 overlooked an invoice and that Fuel and Power Expense should be increased by \$1,521,
4 from \$28,895 to \$30,416.

5
6 **Q. What is Staff's recommendation for Fuel and Power Expense?**

7 A. Staff recommends an increase to Fuel and Power Expense of \$1,521, from \$28,895 to
8 \$30,416, as shown in Schedule GWB-13.

9
10 **Operating Income Adjustment No. 3 – Expense Reclassification**

11 **Q. What is the Company proposing for Outside Services and General Office Expense?**

12 A. Southland is proposing the test year amounts of \$108,755 and \$13,079 for Outside
13 Services and General Office Expense accounts, respectively.

14
15 **Q. Does Staff agree with the Company's proposed amount?**

16 A. No. In its response to Staff Data Requests GWB 4.5.b. and GWB 4.5.c, the Company
17 indicates that \$2,800 of Outside Services Expense was recorded in the General Office
18 Expense account, and that this amount should be reclassified.

19
20 **Q. What is Staff recommending for these expense accounts?**

21 A. As indicated in Operating Income Adjustment No. 3 in Schedule GWB-14, Staff
22 recommends reclassification of \$2,800 from General Office Expense to Outside Services,
23 resulting in test year balances of \$111,755 and \$10,279 for Outside Services and General
24 Office Expense, respectively.

1 **Operating Income Adjustment No. 4 – Depreciation Expense**

2 **Q. What amount of depreciation expense is the Company proposing?**

3 A. Southland is proposing depreciation expense of \$73,199.

4
5 **Q. What are the components of the Company's proposed depreciation expense?**

6 A. The Company-proposed depreciation expense consists of test year depreciation expense
7 plus pro forma adjustments to recognize depreciation on future plant additions and the
8 amortization of CIAC.

9
10 **Q. How did Southland calculate each component of its proposed depreciation expense**
11 **for each of the five systems?**

12 A. The Company calculated test year depreciation expense by multiplying the original cost of
13 its depreciable test year plant in service, plus its expected future construction, by the
14 "Staff's standard recommended (depreciation) rates"⁴ approved in other proceedings.

15
16 **Q. Did Staff recompute the Company's depreciation expense?**

17 A. Yes. Staff recomputed depreciation expense based on Staff's recommended total plant in
18 service and the depreciation rates recommended in this proceeding. Staff's calculation
19 differs from the Company's due primarily to Staff's removal of the plant that the
20 Company expects to construct in the future. Staff used its recommended depreciation
21 rates for this proceeding. Both Staff and the Company reduced depreciation expense for
22 the amortization of CIAC in accordance with the NARUC USOA.

⁴ Company application of November 5, 2009, Testimony of Sonn S Rowell, page 4, line 10.

1 **Q. What is Staff's recommendation?**

2 A. Staff recommends a decrease in depreciation expense of \$42,587, from \$73,199 to
3 \$30,612, as shown in Schedule GWB-15.

4

5 **Operating Income Adjustment No. 5 – Income Taxes**

6 **Q. What is the Company proposing for test year Income Tax Expense?**

7 A. The Company is proposing a negative \$77,225 for test year Income Tax Expense.

8

9 **Q. How did Staff calculate test year income tax expense?**

10 A. Staff calculated test year income tax expense by applying the statutory State and Federal
11 income tax rates to Staff's adjusted test year taxable income, as shown in Schedule GWB-
12 2.

13

14 **Q. Did Staff prepare a schedule showing the computation of test year income taxes?**

15 A. Yes. Staff's computation of income taxes is shown in Schedule GWB-2.

16

17 **Q. Did Staff make any adjustments to test year Income Tax Expense?**

18 A. Yes. Staff's adjustment reflects Staff's calculation of the income tax expense based upon
19 Staff's adjusted test year taxable income, as shown in Schedule GWB-2.

20

21 **Q. What is Staff's recommendation?**

22 A. Staff recommends increasing test year Income Tax Expense by \$45,760, from negative
23 \$77,225 to negative \$31,465, as shown in Schedules GWB-2 and GWB-16.

1 **DEBT SERVICE SURCHARGE**

2 **Q. How does Staff recommend incorporating the proposed debt service into rates?**

3 A. Staff recommends total revenue of \$369,024, comprised of a permanent component
4 increasing base rates and a surcharge component. The permanent component of \$284,608
5 is intended to support ordinary operations and a portion of the proposed WIFA loan.
6 Staff's permanent revenue component is sufficient to cover all operating expenses, but
7 only \$780,000 of the proposed WIFA loan amount of \$1,825,941. The WIFA surcharge
8 component of \$84,596 is necessary to provide additional funds for Southland to comply
9 with WIFA's Debt Service Coverage ("DSC") requirement on the indebtedness over
10 \$780,000. In order to provide adequate DSC for the entire loan amount, the Company
11 needs an annual surcharge of approximately \$84,596.

12
13 **Q. Does this conclude your Direct Testimony on Revenue Requirements?**

14 A. Yes, it does.

REVENUE REQUIREMENT

LINE NO.	DESCRIPTION	(A) COMPANY ORIGINAL COST	(B) COMPANY FAIR VALUE	(C) STAFF ORIGINAL COST	(D) STAFF FAIR VALUE
1	Adjusted Rate Base	\$ 2,029,252	\$ 2,029,252	\$ 417,978	\$ 417,978
2	Adjusted Operating Income (Loss)	\$ (60,476)	\$ (60,476)	\$ (62,041)	\$ (62,041)
3	Current Rate of Return (L2 / L1)	-2.98%	-2.98%	-14.84%	-14.84%
4	Required Rate of Return	8.91% *	8.91%	10.00%	10.00%
5	Required Operating Income (L4 * L1)	\$ 180,764	\$ 180,764	\$ 41,798	\$ 41,798
6	Operating Income Deficiency (L5 - L2)	\$ 241,240	\$ 241,240	\$ 103,838	\$ 103,838
7	Gross Revenue Conversion Factor	1.4843	1.4843	1.3887	1.3887
8	Required Revenue Increase (L7 * L6)	\$ 358,072	\$ 358,072	\$ 144,197	\$ 144,197
9	Adjusted Test Year Revenue	\$ 140,411	\$ 140,411	\$ 140,411	\$ 140,411
10	Proposed Annual Revenue (L8 + L9)	\$ 498,483	\$ 498,483	\$ 284,608	\$ 284,608
11	Required Increase in Revenue (%)	255.02%	255.02%	102.70%	102.70%
12	Rate of Return on Common Equity (%)	10.00%	10.00%	10.00%	10.00%

* Staff notes that, while the Company's application suggests that it is proposing a rate of return of 5.43%, the Company's proposed revenue corresponds to a return of 8.91% and appears to actually be calculated based on an operating margin of 36.26%.

References:

Column (A): Company Schedule A-1
Column (B): Company Schedule A-1
Column (C): Staff Schedules GWB-2, GWB-3, and GWB-10

GROSS REVENUE CONVERSION FACTOR

LINE NO.	DESCRIPTION	(A)	(B)	(C)
<u>Calculation of Gross Revenue Conversion Factor:</u>				
1	Revenue	100.0000%		
2	Uncollectible Factor (Line 11)	0.0000%		
3	Revenues (L1 - L2)	100.0000%		
4	Combined Federal and State Income Tax and Property Tax Rate (Line 23)	27.9885%		
5	Subtotal (L3 - L4)	72.0115%		
6	Revenue Conversion Factor (L1 / L5)	1.388667		
<u>Calculation of Uncollectible Factor:</u>				
7	Unity	100.0000%		
8	Combined Federal and State Tax Rate (Line 17)	26.6716%		
9	One Minus Combined Income Tax Rate (L7 - L8)	73.3284%		
10	Uncollectible Rate	0.0000%		
11	Uncollectible Factor (L9 * L10)		0.0000%	
<u>Calculation of Effective Tax Rate:</u>				
12	Operating Income Before Taxes (Arizona Taxable Income)	100.0000%		
13	Arizona State Income Tax Rate	6.9680%		
14	Federal Taxable Income (L12 - L13)	93.0320%		
15	Applicable Federal Income Tax Rate (Line 44)	21.1793%		
16	Effective Federal Income Tax Rate (L14 x L15)	19.7036%		
17	Combined Federal and State Income Tax Rate (L13 + L16)		26.6716%	
<u>Calculation of Effective Property Tax Factor</u>				
18	Unity	100.0000%		
19	Combined Federal and State Income Tax Rate (L17)	26.6716%		
20	One Minus Combined Income Tax Rate (L18-L19)	73.3284%		
21	Property Tax Factor (GWB-18, L25)	1.7959%		
22	Effective Property Tax Factor (L20*L21)		1.3169%	
23	Combined Federal and State Income Tax and Property Tax Rate (L17+L22)			27.9885%

24	Required Operating Income (Schedule GWB-1, Line 5)	\$ 41,798		
25	Adjusted Test Year Operating Income (Loss) (Schedule GWB-10, Line 42)	\$ (82,041)		
26	Required Increase in Operating Income (L24 - L25)		\$ 103,838	
27	Income Taxes on Recommended Revenue (Col. (F), L52)	\$ 6,304		
28	Income Taxes on Test Year Revenue (Col. (C), L52)	\$ (31,465)		
29	Required Increase in Revenue to Provide for Income Taxes (L27 - L28)		\$ 37,769	
30	Required Revenue Increase (Schedule GWB-1, Line 8)	\$ 144,197		
31	Uncollectible Rate (Line 10)	0.0000%		
32	Uncollectible Expense on Recommended Revenue (L30 * L31)	\$ -		
33	Adjusted Test Year Uncollectible Expense	\$ -		
34	Required Increase in Revenue to Provide for Uncollectible Exp.		\$ -	
35	Property Tax with Recommended Revenue (GWB-17, Line 19)	\$ 10,155		
36	Property Tax on Test Year Revenue (GWB-17, Col A, L16)	\$ 7,565		
37	Increase in Property Tax Due to Increase in Revenue (L35-L36)		\$ 2,590	
38	Total Required Increase in Revenue (L26 + L29 + L34+ L37)		\$ 144,197	

	(A)	(B)	(C)
Test Year			Staff Recommended
<u>Calculation of Income Tax:</u>			
39	Revenue (Sch GWB-9, Col.(C) L5, GWB-1, Col. (D), L9)	\$ 140,411	\$ 284,608
40	Operating Expenses Excluding Income Taxes	\$ 233,917	\$ 236,507
41	Synchronized Interest (L56)	\$ 17,973	\$ 17,973
42	Arizona Taxable Income (L39 - L40 - L41)	\$ (111,479)	\$ 30,128
43	Arizona State Income Tax Rate	6.9680%	6.9680%
44	Arizona Income Tax (L42 x L43)	\$ (7,768)	\$ 2,099
45	Federal Taxable Income (L33 - L35)	\$ (103,711)	\$ 28,029
46	Federal Tax on First Income Bracket (\$1 - \$50,000) @ 15%	\$ (7,500)	\$ 4,204
47	Federal Tax on Second Income Bracket (\$50,001 - \$75,000) @ 25%	\$ (6,250)	\$ -
48	Federal Tax on Third Income Bracket (\$75,001 - \$100,000) @ 34%	\$ (8,500)	\$ -
49	Federal Tax on Fourth Income Bracket (\$100,001 - \$335,000) @ 39%	\$ (1,447)	\$ -
50	Federal Tax on Fifth Income Bracket (\$335,001 - \$10,000,000) @ 34%	\$ -	\$ -
51	Total Federal Income Tax	\$ (23,697)	\$ 4,204
52	Combined Federal and State Income Tax (L44 + L51)	\$ (31,465)	\$ 6,304

53 Effective Tax Rate 21.1793%

Calculation of Interest Synchronization:

54	Rate Base (Schedule GWB-3, Col. (C), Line 18)	\$ 417,978
55	Weighted Average Cost of Debt	4.30%
56	Synchronized Interest (L54 X L55) Based on WIFA Loan	\$ 17,973

RATE BASE - ORIGINAL COST

LINE NO.	(A) COMPANY AS FILED	(B) STAFF ADJUSTMENTS	(C) STAFF AS ADJUSTED
1	\$ 780,091	\$ 45,222	\$ 806,952
2	398,206	(18,361)	379,845
3	<u>\$ 381,885</u>	<u>\$ 63,583</u>	<u>\$ 427,107</u>
<u>LESS:</u>			
4	\$ 105,798	\$ (21,024)	\$ 84,774
5	99,602	(21,024)	78,578
6	<u>6,196</u>	-	<u>6,196</u>
7	3,182	-	3,182
8	-	-	-
9	-	-	-
<u>ADD:</u>			
10	-	-	-
11	22,501	(22,252)	249
12	1,331,319	(1,331,319)	-
13	302,925	(302,925)	-
14	-	-	-
15	-	-	-
16	-	-	-
17	<u>\$ 2,029,252</u>	<u>\$ (1,592,913)</u>	<u>\$ 417,978</u>

References:

Column (A), Company Schedule B-2
Column (B): Schedule GWB-4
Column (C): Column (A) + Column (B)

SUMMARY OF ORIGINAL COST RATE BASE ADJUSTMENTS

LINE NO.	ACCT. NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] Storage Tank ADJ #1 GWB-5	[C] Retirements ADJ #2 GWB-6	[D] Reclassification ADJ #3 GWB-7	[E] Plant Not Yet Built ADJ #4 GWB-8	[E] Structures & Imp ADJ #5 GWB-9	[F] Working Capital ADJ #6 GWB-9A	[F] STAFF ADJUSTED
<i>PLANT IN SERVICE:</i>										
1	303000	Land & Land Rights SS	1,070							1,070
2	304000	Struct & Imp SS	1,725							4,388
3	307000	Wells & Springs	30,144					2,663		30,144
4	311000	Pump Equipment	75,674							75,674
5	320200	Solution Chemical Feeders	4,732							4,732
6	330000	Dist Reservoirs & Standpipe	48,806		(21,024)	(27,782)				-
7	330100	Storage Tanks	302,926	45,222		27,782				375,930
8	331000	TD Mains	209,091							209,091
9	333000	Services	41,070							41,070
10	334000	Meters & Meter Installations	64,853							64,853
11										
12		Total Plant in Service	<u>780,091</u>	<u>45,222</u>	<u>(21,024)</u>	<u>-</u>	<u>-</u>	<u>2,663</u>	<u>-</u>	<u>806,952</u>
13										
14		Accumulated Depreciation	<u>398,206</u>							<u>379,845</u>
15		Net Plant in Service	<u>\$ 381,885</u>	<u>\$ 45,222</u>	<u>\$ (21,024)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,663</u>	<u>\$ -</u>	<u>\$ 427,107</u>
16										
17		LESS:								
18		Contributions in Aid of Construction (CIAC)	\$ 105,798		(21,024)					84,774
19		Less: Accumulated Amortization	<u>99,602</u>		<u>(21,024)</u>					<u>78,578</u>
20		Net CIAC (L63 - L64)	<u>6,196</u>							<u>6,196</u>
21		Advances in Aid of Construction (AIAC)	3,182							3,182
22		Accumulated Deferred Income Tax Credits								
23		Customer Meter Deposits								
24		ADD:								
25		Accumulated Deferred Income Tax Debits								
26		Working Capital Allowance	22,501							
27		WIFA Construction per OPC	1,331,319				(1,331,319)		(22,252)	
28		Property Held in Service	302,925				(302,925)			
29		Material and Supplies Inventory								
30		Prepayments								
31		Projected Capital Expenditures								
32		Deferred Debits								
33		Original Cost Rate Base	<u>\$ 2,029,252</u>	<u>\$ 45,222</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (1,634,244)</u>	<u>\$ -</u>	<u>\$ (22,252)</u>	<u>\$ 417,978</u>

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Schedule GWB-5

RATE BASE ADJUSTMENT #1 - PLANT (STORAGE TANK, SITE #2)

<u>LINE</u> <u>NO.</u>	<u>ACCT</u> <u>NO.</u>	<u>Description</u>	<u>[A]</u> <u>COMPANY</u> <u>AS</u> <u>FILED</u>	<u>[B]</u> <u>STAFF</u> <u>ADJUSTMENTS</u>	<u>[C]</u> <u>STAFF</u> <u>AS</u> <u>ADJUSTED</u>
1	330.10	Storage Tanks *	302,926	45,222	348,148

References:

Column [A]: Amounts included in plant balances

Column [B]: Column [C] less Column [A]

Column [C]: Amount per Staff Engineering Report

* Plant Account #330100, Storage Tanks is further increased
by Rate Base Adjustment #3 in Schedule GWB-7

RATE BASE ADJUSTMENT #2 - UNRECORDED PLANT RETIREMENTS SITE #2

<u>LINE</u> <u>NO.</u>	<u>DESCRIPTION</u>	<u>[A]</u> <u>COMPANY</u> <u>AS</u> <u>FILED</u>	<u>[B]</u> <u>STAFF</u> <u>ADJUSTMENTS</u>	<u>[C]</u> <u>STAFF</u> <u>AS</u> <u>ADJUSTED</u>
1	Plant Account #330000, Distribution Reservoirs & Standpipes*	\$ 48,806	\$ (21,024)	\$ 27,782
2	Accumulated Depreciation**	\$ 398,206	\$ (21,024)	\$ 377,182
3	CIAC	\$ 105,798	\$ (21,024)	\$ 84,774
4	Accumulted Amortization-CIAC	\$ 99,602	\$ (21,024)	\$ 78,578

References:

Column [A]: Amounts included in plant balances

Column [B]: Staff adjustments, See Testimony GWB

Column (C): Column [A] plus Column [B]

* Plant Account #330000, Distribution Reservoirs & Standpipes is further reduced by Rate Base Adjustment #2 in Schedule GWB-7.

Accumulated Depreciation is further adjusted by Staff Rate Base Adjustment #9.

SOUTHLAND UTILITIES COMPANY, INC.
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Schedule GWB- 7

RATE BASE ADJUSTMENT #3 - RECLASSIFICATION TO CORRECT PLANT ACCOUNT

LINE NO.	DESCRIPTION	[A]	[B]	[C]
		COMPANY AS FILED	STAFF ADJUSTMENTS	STAFF AS ADJUSTED
1	Plant Account #330000, Distribution Reservoirs & Standpipes*	\$ 27,782	\$ (27,782)	\$ -
2	Plant Account #330100, Storage Tanks **	\$ 348,148	\$ 27,782	\$ 375,930

References:

Column [A]: Amounts included in plant balances
 Column [B]: Staff adjustments, See Testimony GWB
 Column (C): Column [A] plus Column [B]

* Adjusted Balance, per Schedule GWB-6

** Adjusted Balance, per Schedule GWB-5

RATE BASE ADJUSTMENT #2 - UNRECORDED PLANT RETIREMENTS SITE #2

LINE NO.	DESCRIPTION	[A]	[B]	[C]
		COMPANY AS FILED	STAFF ADJUSTMENTS	STAFF AS ADJUSTED
1	Plant Account #330000, Distribution Reservoirs & Standpipes*	\$ 48,806	\$ (21,024)	\$ 27,782
2	Accumulated Depreciation	\$ 398,206	\$ (21,024)	\$ 377,182
3	CIAC	\$ 105,798	\$ (21,024)	\$ 84,774
4	Accumulted Amortization-CIAC	\$ 99,602	\$ (21,024)	\$ 78,578

References:

Column [A]: Amounts included in plant balances
Column [B]: Staff adjustments, See Testimony GWB
Column [C]: Column [A] plus Column [B]

* Plant Account #330000, Distribution Reservoirs & Standpipes
is further reduced by Rate Base Adjustment #2 in Schedule
GWB-7

RATE BASE ADJUSTMENT #4 - REMOVAL OF PLANT NOT YET BUILT

<u>LINE NO.</u>	<u>DESCRIPTION</u>	[A] COMPANY AS FILED	[B] STAFF ADJUSTMENTS	[C] STAFF AS ADJUSTED
1	WIFA Construction per OPC	\$ 1,331,319	\$ (1,331,319)	\$ -
2	Property Held place in Service	\$ 302,925	\$ (302,925)	\$ -
	Total	\$ 1,634,244	\$ (1,634,244)	\$ -

References:

Column [A]: Amounts included in plant balances
Column [B]: Staff adjustments, See Testimony GWB
Column (C): Column [A] plus Column [B]

RATE BASE ADJUSTMENT #5 - CORRECTION OF OVERSTATED RETIREMENTS

LINE NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] STAFF ADJUSTMENTS	[C] STAFF AS ADJUSTED
1	Struct & Imp SS Accumulated Depreciation*	1,725 377,182	2,663 2,663	4,388 379,845

REFERENCES:

Columns [A]: Company schedules
 Column [B]: Column [C] less Column [A]
 Column [C]: See testimony GWB

*Company amount reflects Staff Rate Base Adjustment #2.

RATE BASE ADJUSTMENT #6 - WORKING CAPITAL

LINE NO.	DESCRIPTION	[A] COMPANY TEST YEAR AS FILED	[B] STAFF ADJUSTMENTS	[C] STAFF AS ADJUSTED
1	1/24 Purchased Power	\$ 1,204	\$ (1,204)	\$ -
2	1/24 Purchased Water	-	-	-
3	1/8 Operation & Maintenance Expense	21,048	(21,048)	-
4	Material & Supplies Inventories	-	-	-
5	Prepayments	249		249
6	Total working Capital allowance	<u>22,501</u>	<u>(22,252)</u>	<u>249</u>

- 7 References:
8 Column [A]: Company Workpapers
9 Column [B]: Staff adjustments to expenses, See Testimony GWB
10 Column [C]: Column [A] + Column [B]

OPERATING INCOME STATEMENT - TEST YEAR AND STAFF RECOMMENDED

LINE NO.	DESCRIPTION	[A] COMPANY TEST YEAR AS FILED	[B] STAFF TEST YEAR ADJUSTMENTS	[C] STAFF TEST YEAR AS ADJUSTED	[D] STAFF RECOMMENDED CHANGES	[E] STAFF RECOMMENDED
1	Water Revenues	\$ 135,713	-	\$ 135,713	\$ 144,197	\$ 279,910
2	Other Revenues	4,698	-	4,698	-	4,698
3	Other	-	-	-	-	-
4	Total Operating Revenues	\$ 140,411	\$ -	\$ 140,411	\$ 144,197	\$ 284,608
5	Outside Services	\$ 108,755	\$ 2,800	\$ 111,555	\$ -	\$ 111,555
6	Purchased Water	-	-	-	-	-
7	Fuel & Power	28,895	1,521	30,416	-	30,416
8	Chemicals/Water Testing	6,087	(3,129)	2,958	-	2,958
9	Transportation	2,308	-	2,308	-	2,308
10	Management Fees	-	-	-	-	-
11	Group Insurance	-	-	-	-	-
12	Pensions	-	-	-	-	-
13	Rate Case Expense	8,333	-	8,333	-	8,333
14	Insurance Other Than Group	1,204	-	1,204	-	1,204
15	Customer Accounting	-	-	-	-	-
16	Rents	-	-	-	-	-
17	General Office Expense	13,079	(2,800)	10,279	-	10,279
18	Miscellaneous	2,717	-	2,717	-	2,717
19	Maintenance Expense	25,903	-	25,903	-	25,903
20	Depreciation & Amortization	73,199	(42,587)	30,612	-	30,612
21	General Taxes-Property	7,632	-	7,632	2,590	10,222
22	General Taxes-Other	-	-	-	-	-
23	Income Taxes	(77,225)	45,760	(31,465)	37,769	6,304
24						
25	Total Operating Expenses	200,887	1,565	202,452	40,359	242,810
26	Operating Income (Loss)	\$ (60,476)	\$ (1,565)	\$ (62,041)	\$ 103,838	\$ 41,798

References:
Column (A): Company Schedule C-1
Column (B): Schedule GWB 11
Column (C): Column (A) + Column (B)
Column (D): Schedules GWB 2, Lines 29, 34 and 37
Column (E): Column (C) + Column (D)

SUMMARY OF OPERATING INCOME ADJUSTMENTS - TEST YEAR

LINE NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] Water Testing ADJ #1 GWB-12	[C] Power Correction ADJ #2 GWB-13	[D] Exp Reclass ADJ #3 GWB-14	[E] Depreciation Exp. ADJ #4 GWB-15	[F] Income Taxes ADJ #5 GWB-16	[H] STAFF ADJUSTED
1	Water Revenues	\$ 135,713	-	-	-	\$ -	\$ -	\$ 135,713
2	Other Revenues	4,698	-	-	-	-	-	4,698
3	Other	-	-	-	-	-	-	-
4	Total Operating Revenues	\$ 140,411	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 140,411
5	Outside Services	\$ 108,755	-	-	2,800	\$ -	\$ -	\$ 111,555
6	Purchased Water	-	-	-	-	-	-	-
7	Fuel & Power	28,895	(3,129)	1,521	-	-	-	30,416
8	Chemicals/Water Testing	6,087	-	-	-	-	-	2,958
9	Transportation	2,308	-	-	-	-	-	2,308
10	Management Fees	-	-	-	-	-	-	-
11	Group Insurance	-	-	-	-	-	-	-
12	Pensions	-	-	-	-	-	-	-
13	Rate Case Expense	8,333	-	-	-	-	-	8,333
14	Insurance Other Than Group	1,204	-	-	-	-	-	1,204
15	Customer Accounting	-	-	-	-	-	-	-
16	Rents	-	-	-	-	-	-	-
17	General Office Expense	13,079	-	-	(2,800)	-	-	10,279
18	Miscellaneous	2,717	-	-	-	-	-	2,717
19	Maintenance Expense	25,903	-	-	-	-	-	25,903
20	Depreciation & Amortization	73,199	-	-	-	(42,587)	-	30,612
21	General Taxes-Property	7,632	-	-	-	-	-	7,632
22	General Taxes-Other	-	-	-	-	-	45,760	-
23	Income Taxes	(77,225)	-	-	-	-	-	(31,465)
24								
25								
26	Total Operating Expenses	\$ 200,887	\$ (3,129)	\$ 1,521	\$ -	\$ (42,587)	\$ 45,760	\$ 202,452
27	Operating Income (Loss)	\$ (60,476)	\$ 3,129	\$ (1,521)	\$ -	\$ 42,587	\$ (45,760)	\$ (62,041)

References:
Column (A): Company Schedule C-1

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Schedule GWB-12

OPERATING INCOME ADJUSTMENT #1 - WATER TESTING EXPENSE

<u>LINE NO.</u>	<u>DESCRIPTION</u>	<u>[A] COMPANY PROPOSED</u>	<u>[B] STAFF ADJUSTMENTS</u>	<u>[C] STAFF RECOMMENDED</u>
1	Water Testing Expense	<u>\$ 6,087</u>	<u>\$ (3,129)</u>	<u>\$ 2,958</u>

References:

Column (A), Company Schedule C-1

Column (B): Testimony GWB

Column (C): Column (A) + Column (B)

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Schedule GWB-13

OPERATING INCOME ADJUSTMENT #2 - FUEL & POWER EXPENSE

<u>LINE NO.</u>	<u>DESCRIPTION</u>	<u>[A] COMPANY PROPOSED</u>	<u>[B] STAFF ADJUSTMENTS</u>	<u>[C] STAFF RECOMMENDED</u>
1	Fuel & Power	<u>\$ 28,895</u>	<u>\$ 1,521</u>	<u>\$ 30,416</u>

References:

Column (A), Company Schedule C-1
Column (B): Testimony GWB
Column (C): Column (A) + Column (B)

OPERATING INCOME ADJUSTMENT #3 - EXPENSE RECLASSIFICATION

<u>LINE NO.</u>	<u>DESCRIPTION</u>	<u>[A] COMPANY PROPOSED</u>	<u>[B] STAFF ADJUSTMENTS</u>	<u>[C] STAFF RECOMMENDED</u>
1	Outside Services	\$ 108,755	\$ 2,800	\$ 111,555
2	General Office Expense	\$ 13,079	\$ (2,800)	\$ 10,279

References:

Column (A), Company Schedule C-1

Column (B): Testimony GWB

Column (C): Column (A) + Column (B)

OPERATING INCOME ADJUSTMENT #4- DEPRECIATION EXPENSE

LINE NO.	ACCT. NO.	DESCRIPTION	[A] PLANT BALANCE	[B] DEPRECIATION RATE	[C] DEPRECIATION EXPENSE
1		<u>PLANT IN SERVICE:</u>			
2	303000	Land & Land Rights SS	1,070	0.00%	-
3	304000	Struct & Imp SS	4,388	3.33%	146
4	307000	Wells & Springs	30,144	3.33%	1,004
5	311000	Pump Equipment	75,674	12.50%	9,459
6	320200	Solution Chemical Feeders	4,732	20.00%	946
7	330100	Storage Tanks	375,930	2.22%	8,346
8	331000	TD Mains	209,091	2.00%	4,182
9	333000	Services	41,070	3.33%	1,368
10	334000	Meters & Meter Installations	64,853	8.33%	5,402
		Total Plant in Service, Staff Adjusted, GWB-11	806,952		30,853
11		CIAC Amortization, line 21 below			(241)
12		Net Depreciation & Amortization, Staff Adjusted			30,612
13		As filed by Company, Schedule GWB-11			73,199
14		Staff Adjustment			(42,587)
15		Gross CIAC, Per Staff			84,774
16		CIAC fully amortized, Per Co		93,745	
17		Less: Staff Adjustment		21,024	
18		CIAC fully amortized, Per Staff			72,721
19		Unamortized Gross CIAC			12,053
20		Depreciation Rate of Associated Plant			2.00%
21		CIAC Amortization, to line 11, above			241

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Schedule GWB-16

OPERATING INCOME ADJUSTMENT #5 - INCOME TAXES

<u>LINE NO.</u>	<u>DESCRIPTION</u>	<u>[A] COMPANY PROPOSED</u>	<u>[B] STAFF ADJUSTMENTS</u>	<u>[C] STAFF RECOMMENDED</u>
1	Income Taxes	<u>\$ (77,225)</u>	<u>\$ 45,760</u>	<u>\$ (31,465)</u>

References:

Column (A), Company Schedule C-2
Column (B): Testimony GWB
Column (C): Column (A) + Column (B)

OPERATING INCOME PROPERTY TAX EXPENSE GRFC COMPONENT

LINE NO.	DESCRIPTION	[A] STAFF AS ADJUSTED	[B] STAFF RECOMMENDED
1	Staff Adjusted Test Year Revenues - 2007	\$ 140,411	\$ 140,411
2	Weight Factor	2	2
3	Subtotal (Line 1 * Line 2)	280,822	280,822
4	Staff Adjusted Test Year Revenues - 2007	140,411	
5	Staff Recommended Revenue		284,608
6	Subtotal (Line 4 + Line 5)	421,233	565,430
7	Number of Years	3	3
8	Three Year Average (Line 5 / Line 6)	140,411	188,477
9	Department of Revenue Multiplier	2	2
10	Revenue Base Value (Line 7 * Line 8)	280,822	376,953
11	Plus: 10% of CWIP - 2008		-
12	Less: Net Book Value of Licensed Vehicles	-	-
13	Full Cash Value (Line 9 + Line 10 - Line 11)	280,822	376,953
14	Assessment Ratio	23.0%	23.0%
15	Assessment Value (Line 12 * Line 13)	64,589	86,699
16	Composite Property Tax Rate	11.71%	11.71%
17	Staff Test Year Adjusted Property Tax Expense (Line 14 * Line 15)	\$ 7,565	
18	Company Proposed Property Tax	\$ 7,632	
19	Staff Test Year Adjustment (Line 16 - Line 17) - Immaterial	\$ (67)	
20	Property Tax on Staff Recommended Revenue (Line 14 * Line 15)		\$ 10,155
21	Staff Test Year Adjusted Property Tax Expense (Line 16)		\$ 7,565
22	Increase in Property Tax Due to Increase in Revenue Requirement		\$ 2,590
23	Increase in Property Tax Due to Increase in Revenue Requirement (Line 21)		\$ 2,590
24	Increase in Revenue Requirement		\$ 144,197
25	Increase in Property Tax Per Dollar Increase in Revenue (Line 22 / Line 23)		1.79592%

REFERENCES:

Line 15: Composite Tax Rate, per Company
Line 17: Company Schedule C-1, Line 27
Line 21: Line 19 - Line 20
Line 23: Schedule GWB-1, Line 8

0

MEMORANDUM

TO: Gerald Becker
Public Utilities Analyst V
Utilities Division

FROM: Trish Meeter
Public Utilities Consumer Analyst I
Utilities Division

THRU: Connie Walczak
Consumer Services Supervisor
Utilities Division

DATE: July 14, 2010

RE: Southland Utilities Company, Inc.
Docket No. W-02062A-09-0515
W-02062A-09-0466

COMPANY HISTORY

Southland Utilities Company, Inc. (Company") filed an application for a rate increase with the Arizona Corporation Commission on November 5, 2009. The current rates for the Company have been in effect since January 7, 1999 per Decision No. 61335.

COMPLAINT HISTORY

A search of the Consumer Services database from January 1, 2007 to current revealed:

2007 – Zero Complaints, Inquiries or Opinions

2008 – One Complaint (quality of service), 2 Inquiries (rates) and zero Opinions

2009 – One Complaint (billing), Zero Inquiries or Opinions

2010 – One Complaint (billing), Seven Inquiries (Five ACC questions, One rate case item, One quality of service), Nine Opinions opposed to this application

All complaints have been resolved and closed.

SUFFICIENCY STATUS

The Company's application met sufficiency status on December 18, 2009.

AFFIDAVIT OF MAILING

The Company's Affidavit of Mailing of the customer notification was filed on May 19, 2010.

BILL FORMAT COMPLIANCE

A review of the Company's bill format indicates compliance with R14-2-409.B.2.a thru R14-2-409.B.2.j of the Arizona Administrative Code, Title 14, and Chapter 2.

The Company has provided staff an updated bill copy for Commission records.

CORPORATIONS DIVISION STATUS

On July 14, 2010 the Corporations Division of the Commission reflects that the Company is in Good Standing.

CROSS-CONNECTION/ BACKFLOW TARIFF

The Company does not have a Cross-Connection/Backflow tariff on file. Company staff has been contacted regarding this matter.

CURTAILMENT TARIFF AND RECOMMENDATION

The Company has an approved Curtailment tariff on file effective August 16, 2009.

HEARING DATE

A hearing date was scheduled for August 31, 2010.

INTERVENORS

No requests to intervene have been received.

cc: File

BEFORE THE ARIZONA CORPORATION COMMISSION

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

IN THE MATTER OF THE APPLICATION OF)
SOUTHLAND UTILITIES COMPANY, INC.)
FOR AUTHORITY TO INCUR LONG-TERM)
DEBT.)

DOCKET NO. W-02062A-09-0466

IN THE MATTER OF THE APPLICATION OF)
SOUTHLAND UTILITIES COMPANY, INC.)
FOR A RATE INCREASE)

DOCKET NO. W-02062A-09-0515

(RATE DESIGN)

DIRECT

TESTIMONY

OF

GERALD W. BECKER

PUBLIC UTILITIES ANALYST V

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

JULY 19, 2010

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EXECUTIVE SUMMARY
SOUTHLAND UTILITIES COMPANY, INC.
DOCKET NOS. W-02062A-09-0515 AND W-02062A-09-0466

Southland Utilities Company, Inc. ("Southland" or "Company") is an Arizona public service corporation that provides water utility service to an average of 612 customers in an area located approximately five miles south of Sierra Vista, Arizona. The Company utilized a test year ended December 31, 2008.

In its rate application, the Company seeks an increase to cover both a usual rate increase and additional funds to cover a proposed WIFA loan. The Company's amended rate application requested a revenue increase of \$358,072, or 255.02 percent, over test year revenue of \$140,411. The Company's proposed rates, as amended, produce operating revenues of \$498,483 for an operating income of \$180,706 and for an operating margin of 36.26 percent. The Company's requested rates would increase the typical 5/8-inch meter residential bill with a median usage of 3,756 gallons from \$15.00 to \$53.69 for an increase of \$38.69, or 258.02 percent.

Staff recommends total revenue of \$369,204 comprised of a permanent component increasing base rates and a surcharge component. The permanent component is intended to support ordinary operations while the surcharge component would support the principal and interest on a Water Infrastructure Finance Authority of Arizona ("WIFA") loan. The permanent component represents a \$144,197, or 102.70 percent, increase over test year revenue of \$140,411. In addition, Staff recommends a surcharge of \$84,596, or 60.25 percent of test year revenues of \$140,411. The sum of the two components represents a total increase of \$228,793, or 162.96 percent, over test year revenue of \$140,411. Staff's recommended rates for the permanent component would increase the typical 5/8-inch meter residential bill with a median usage of 3,756 from \$15.00 to \$24.37 for an increase of \$9.37, or 62.5 percent. Staff's recommended WIFA surcharge would add \$10.51 to the typical 5/8-inch meter residential bill. Combined, Staff's recommended permanent and WIFA surcharge revenue components would increase the typical 5/8-inch meter residential bill by \$19.88, or 132.59 percent, from \$15.00 to \$34.88.

Staff's recommended permanent revenue component would provide a 10.00 percent rate of return on a \$417,978 rate base. Combined, Staff's recommended permanent and WIFA surcharge revenue components would provide a 33.84 percent rate of return on a \$417,798 rate base.

Staff's permanent revenue component is sufficient to cover all operating expenses but only \$780,000 of the proposed WIFA loan of \$1,825,941. The WIFA surcharge component is necessary to provide adequate funds for Southland to comply with WIFA's Debt Service Coverage ("DSC") requirement on the amount over \$780,000, or \$1,045,941, of the total proposed WIFA loan of \$1,825,941. In order to provide adequate DSC for the entire loan amount, the Company needs an annual surcharge of approximately \$84,596.

1 **INTRODUCTION**

2 **Q. Please state your name, occupation, and business address.**

3 A. My name is Gerald Becker. I am a Public Utilities Analyst V employed by the Arizona
4 Corporation Commission (“ACC” or “Commission”) in the Utilities Division (“Staff”).
5 My business address is 1200 West Washington Street, Phoenix, Arizona 85007.

6
7 **Q. Briefly describe your responsibilities as a Public Utilities Analyst V.**

8 A. I am responsible for the examination and verification of financial and statistical
9 information included in utility rate applications. In addition, I develop revenue
10 requirements, and prepare written reports, testimonies, and schedules that include Staff
11 recommendations to the Commission. I am also responsible for testifying at formal
12 hearings on these matters.

13
14 **Q. Please describe your educational background and professional experience.**

15 A. I received a Masters of Business Administration with an emphasis in Accounting from
16 Pace University. I am a Certified Public Accountant and a Certified Internal Auditor.

17
18 I have participated in multiple rate, financing and other regulatory proceedings. I attended
19 the National Association of Regulatory Utility Commissioners (“NARUC”) Utilities Rate
20 School.

21
22 I began employment with the Commission as a utilities regulatory analyst in April 2006.
23 Prior to joining the Commission, I worked as an Auditor at the Department of Economic
24 Security and Department of Revenue in the Taxpayer Assistance Section. Prior to those
25 jobs, I worked for 15 years as an Auditor, Analyst, Financial Analyst, and Budget
26 Manager at United Illuminating, an investor-owned electric company in New Haven, CT.

1 **Q. What is the scope of your testimony in this case?**

2 A. I am presenting Staff's analysis and recommendations in the areas of rate base, operating
3 revenues and expenses, and the permanent as well as the surcharge component of the
4 recommended revenue requirement, regarding the application of Southland Utilities
5 Company, Inc. The application was consolidated with an application to incur long term
6 debt, Docket No. W-02062A-09-0466. Staff witness Juan Manrique is presenting Staff's
7 analysis and recommendations regarding the Company's application to incur long term
8 debt. Staff witness Katrin Stukov is presenting Staff's engineering analysis and
9 recommendations.

10

11 **Q. What is the scope of your testimony in this case?**

12 A. I am presenting Staff's analysis and recommendations regarding Arizona Water
13 Company's ("Company" or "Arizona Water") application for a permanent increase in its
14 rates and charges throughout Arizona. I am presenting testimony and schedules
15 addressing rate design.

16

17 **Q. What is the basis of your testimony in this case?**

18 A. Based on the adjustments and revenue requirement recommended by Staff, I will present
19 Staff's recommended rate design. I will also present the rate design implications that will
20 result from an approval for Southland to incur long term debt in Docket No. W-02062A-
21 09-0466.

1 **BACKGROUND**

2 **Q. Please describe the Company.**

3 A. Southland is an Arizona public service corporation that provides water utility service to an
4 average of 612 customers in an area located approximately five miles south of Sierra
5 Vista, Arizona.

6
7 **RATE DESIGN**

8 **Q. Have you prepared a schedule summarizing the present, Company proposed, and**
9 **Staff recommended rates and service charges?**

10 A. Yes. A summary of the present, Company-proposed, and Staff-recommended rates are
11 presented in the attached schedules.

12
13 **Q. Would you please summarize the present rate design?**

14 A. The present monthly minimum charges by meter size are as follows: 5/8 x 3/4-inch
15 \$10.00; 3/4-inch \$11.00; 1-inch \$15.00; 1 1/2-inch- \$20.00; 2-inch \$23.00; 3-inch \$49.00;
16 4-inch \$70.00; and 6-inch \$100.00. No gallons are included in the monthly minimum
17 charge. The present commodity rate is \$1.33 per thousand gallons for all usage and all
18 meter sizes.

19
20 **Q. Would you please summarize the Company's proposed rate design?**

21 A. The Company's proposed monthly minimum charges by meter size are as follows: 5/8 x
22 3/4-inch \$42.00; 3/4-inch \$45.00; 1-inch \$80.00; 1 1/2-inch \$125.00; 2-inch \$175.00; 3-
23 inch \$375.00; 4-inch \$475.00; and 6-inch \$775.00. Zero gallons are included in the
24 monthly minimum charge. The Company proposes a 3-tier inverted commodity rate for
25 the 5/8 x 3/4-inch customers and 3/4-inch customers for both residential and commercial.
26 The Company proposes commodity charges of \$2.90 per thousand gallons for zero to

1 3,000 gallons, \$3.95 per thousand gallons for 3,001 to 12,000 gallons, and \$5.301 per
2 thousand gallons for any consumption over 12,000 gallons. The other proposed
3 commodity rate tiers vary by meter size, but are \$3.95 per thousand gallons for the first
4 tier and \$5.301 per thousand gallons for any consumption over the first tier. The
5 Company does not differentiate between residential or commercial.

6
7 **Q. Would you please summarize Staff's recommended rate design?**

8 A. Staff recommends total revenue of \$369,204 comprised of a permanent component
9 increasing base rates and a surcharge component. The permanent component of \$284,608
10 is intended to support ordinary operations and a portion of the proposed WIFA loan.
11 Staff's permanent revenue component is sufficient to cover all operating expenses but
12 only \$780,000 of the proposed WIFA loan of \$1,825,941. The WIFA surcharge
13 component of \$84,596 is necessary to provide additional funds for Southland to comply
14 with WIFA's Debt Service Coverage ("DSC") requirement on the indebtedness over
15 \$780,000, or \$1,045,941, of the total proposed WIFA loan of \$1,825,941. In order to
16 provide adequate DSC for the entire loan amount, the Company needs an annual surcharge
17 of approximately \$84,596.

18
19 The permanent component represents a \$144,197, or 102.70 percent, increase over test
20 year revenue of \$140,411. In addition, Staff recommends a surcharge of \$84,596, or
21 60.25 percent of test year revenues of \$140,411. The sum of the two components
22 represents a total increase of \$228,793, or 162.96 percent, over test year revenue of
23 \$140,411. Staff's recommended rates for the permanent component would increase the
24 typical 5/8-inch meter residential bill with a median usage of 3,756 from \$15.00 to \$24.37
25 for an increase of \$9.37, or 62.50 percent. Staff's recommended WIFA surcharge would
26 add \$10.51 to the typical 5/8-inch meter residential bill. Combined, Staff's recommended

1 permanent rate and WIFA surcharge revenue components would increase the typical 5/8-
2 inch meter residential bill by \$19.88, or 132.59 percent, from \$15.00 to \$34.88.

3
4 The permanent component of Staff's rate design recommends monthly minimum charges
5 by meter size as follows: 5/8 x 3/4-inch \$16.00; 3/4-inch \$22.50; 1-inch \$37.50; 2-inch
6 \$120.00; 3-inch \$240.00; 4-inch \$375.00; and 6-inch \$750.00. Zero gallons are included
7 in the monthly minimum charge. Staff recommends an inverted tier rate design that
8 consists of four tiers for the 5/8 x 3/4-inch commodity rate of \$1.55 per thousand gallons
9 for 0 to 2,000 gallons, \$3.00 per thousand gallons for 2,001 to 6,000 gallons, \$4.00 per
10 thousand gallons for 6,001 to 12,000 gallons and \$6.000 per thousand gallons for any
11 consumption over 12,000 gallons. Staff's recommended larger residential, commercial,
12 and industrial commodity rates have two tiers and vary by meter size, set at \$4.00 per
13 thousand gallons for the first tier, and \$6.00 per thousand gallons for any consumption
14 over the second tier. Staff recommends increasing the monthly charge for fire sprinkler
15 service to the greater of \$10.00 or 2 percent of the monthly minimum charge for that meter
16 size.

17
18 **Q. What is the rate impact on a typical 5/8 x 3/4-inch meter residential customer?**

19 A. Staff's recommended rates for the permanent component would increase the typical 5/8-
20 inch meter residential bill with a median usage of 3,756 from \$15.00 to \$24.37, for an
21 increase of \$9.37, or 62.50 percent. Staff's recommended WIFA surcharge would add
22 \$10.51 to the typical 5/8-inch meter residential bill. Combined Staff's recommended
23 permanent and WIFA surcharge revenue components would increase the typical 5/8-inch
24 meter residential bill by \$19.88, or 132.59 percent, from \$15.00 to \$34.88. A typical bill
25 without the surcharge is shown on Schedule GWB-2. A typical bill analysis including the
26 surcharge is provided on Schedule GWB-3.

1 **Q. When should the surcharge become effective?**

2 A. It should become effective for all service rendered the first day of the month following the
3 closing of the WIFA loan.

4

5 **Q. What Water System service lines, meter installation charges, and service charges**
6 **does Staff recommend?**

7 A. A comparison of the current charges for Water System service lines, metered installation
8 charges, and service charges; the Company's proposed changes, and Staff's recommended
9 changes are presented on Schedule GWB-4. Staff's recommended charges are within
10 Staff's experience of what are reasonable and customary charges.

11

12 **Q. Does this conclude your direct testimony?**

13 A. Yes, it does.

	Present Rates	Proposed Rates- Co. (As Amended)	Proposed Rates- Staff
Monthly Usage Charge			
5/8" x 3/4" Meter	\$ 10.00	\$ 42.00	\$ 16.00
3/4" Meter	\$ 11.00	\$ 45.00	\$ 22.50
1" Meter	\$ 15.00	\$ 80.00	\$ 37.50
1½" Meter	\$ 20.00	\$ 125.00	\$ 75.00
2" Meter	\$ 23.00	\$ 175.00	\$ 120.00
3" Meter	\$ 49.00	\$ 375.00	\$ 240.00
4" Meter	\$ 70.00	\$ 475.00	\$ 375.00
6" Meter	\$ 100.00	\$ 775.00	\$ 750.00
WIFA Surcharge			
5/8" x 3/4" Meter	N/A	N/A	\$ 10.51
3/4" Meter	N/A	N/A	\$ 15.77
1" Meter	N/A	N/A	\$ 26.28
1½" Meter	N/A	N/A	\$ 52.55
2" Meter	N/A	N/A	\$ 84.08
3" Meter	N/A	N/A	\$ 168.16
4" Meter	N/A	N/A	\$ 262.75
6" Meter	N/A	N/A	\$ 525.51

Commodity Charge per 1,000 gallons			
Block			
All Gallons		\$ 1.33	
5/8 x 3/4 inch			
	1 to 3,000 gallons	\$ 2.900	
	3,001 to 12,000 gallons	\$ 3.950	
	Over 12,000 gallons	\$ 5.301	
	0 to 2,000 gallons		\$ 1.55
	2,001 to 6,000 gallons		\$ 3.00
	6,001 to 12,000 gallons		\$ 4.00
	Over 12,000 gallons		\$ 6.00
3/4 inch			
	1 to 3,000 gallons	\$ 2.900	
	3,001 to 12,000 gallons	\$ 3.950	
	Over 12,000 gallons	\$ 5.301	
	1 to 12,000 gallons	\$ 3.950	\$ 4.000
	Over 12,000 gallons	\$ 5.301	\$ 6.000
1 inch			
	1 to 30,000 gallons	\$ 3.950	\$ 4.000
	Over 30,000 gallons	\$ 5.301	\$ 6.000
1 1/2 inch			
	1 to 60,000 gallons	\$ 3.950	\$ 4.000
	Over 60,000 gallons	\$ 5.301	\$ 6.000
2 inch			
	1 to 90,000 gallons	\$ 3.950	\$ 4.000
	Over 90,000 gallons	\$ 5.301	\$ 6.000
3 inch			
	1 to 125,000 gallons	\$ 3.950	\$ 4.000
	Over 125,000 gallons	\$ 5.301	\$ 6.000
4 inch			
	1 to 200,000 gallons	\$ 3.950	\$ 4.000
	Over 200,000 gallons	\$ 5.301	\$ 6.000
6 inch			
	1 to 400,000 gallons	\$ 3.950	\$ 4.000
	Over 400,000 gallons	\$ 5.301	\$ 6.000

Typical Bill Analysis
Residential 5/8 X 3/4-Inch Meters

WITHOUT SURCHARGE

Produces Revenues of \$284,608 which closely approximates Staff revenue requirements on Rev. Requirement Schedule GWB-10

Company Proposed	Gallons	Present Rates	Proposed Rates	Dollar Increase	Percent Increase
Average Usage	6,030	\$ 18.02	\$ 62.67	\$ 44.65	247.77%
Median Usage	3,756	15.00	53.69	\$ 38.69	258.02%
Staff Recommended					
Average Usage	6,030	\$ 18.02	\$ 31.22	\$ 13.20	73.25%
Median Usage	3,756	15.00	24.37	\$ 9.37	62.50%

Present & Proposed Rates (Without Taxes)
Residential 5/8 X 3/4-Inch Meters

Consumption	Rates	Rates	Increase	Rates	Increase
-	\$ 10.00	\$ 42.00	320.00%	\$ 16.00	60.00%
1,000	11.33	\$ 44.90	296.29%	\$ 17.55	54.90%
2,000	12.66	\$ 47.80	277.57%	\$ 19.10	50.87%
3,000	13.99	\$ 50.70	262.40%	\$ 22.10	57.97%
4,000	15.32	\$ 54.65	256.72%	\$ 25.10	63.84%
5,000	16.65	\$ 58.60	251.95%	\$ 28.10	68.77%
6,000	17.98	\$ 62.55	247.89%	\$ 31.10	72.97%
7,000	19.31	\$ 66.50	244.38%	\$ 35.10	81.77%
8,000	20.64	\$ 70.45	241.33%	\$ 39.10	89.44%
9,000	21.97	\$ 74.40	238.64%	\$ 43.10	96.18%
10,000	23.30	\$ 78.35	236.27%	\$ 47.10	102.15%
11,000	24.63	\$ 82.30	234.15%	\$ 51.10	107.47%
12,000	25.96	\$ 86.25	232.24%	\$ 55.10	112.25%
13,000	27.29	\$ 91.55	235.47%	\$ 61.10	123.89%
14,000	28.62	\$ 96.85	238.41%	\$ 67.10	134.45%
15,000	29.95	\$ 102.15	241.08%	\$ 73.10	144.07%
16,000	31.28	\$ 107.45	243.52%	\$ 79.10	152.88%
17,000	32.61	\$ 112.76	245.77%	\$ 85.10	160.96%
18,000	33.94	\$ 118.06	247.84%	\$ 91.10	168.41%
19,000	35.27	\$ 123.36	249.75%	\$ 97.10	175.30%
20,000	36.60	\$ 128.66	251.52%	\$ 103.10	181.69%
25,000	43.25	\$ 155.16	258.76%	\$ 133.10	207.75%
30,000	49.90	\$ 181.67	264.06%	\$ 163.10	226.85%
35,000	56.55	\$ 208.17	268.12%	\$ 193.10	241.47%
40,000	63.20	\$ 234.68	271.33%	\$ 223.10	253.01%
45,000	69.85	\$ 261.18	273.92%	\$ 253.10	262.35%
50,000	76.50	\$ 287.69	276.06%	\$ 283.10	270.07%
75,000	109.75	\$ 420.21	282.88%	\$ 433.10	294.62%
100,000	143.00	\$ 552.74	286.53%	\$ 583.10	307.76%

Typical Bill Analysis
Residential 5/8 X 3/4-Inch Meters

WITH SURCHARGE
Produces Revenues of \$369,184

Company Proposed	Gallons	Present Rates	Proposed Rates	Dollar Increase	Percent Increase
Average Usage	6,030	\$ 18.02	\$ 62.67	\$ 44.65	247.77%
Median Usage	3,756	15.00	53.69	\$ 38.69	258.02%
Staff Recommended					
Average Usage	6,030	\$ 18.02	\$ 41.73	\$ 23.71	131.58%
Median Usage	3,756	15.00	34.88	\$ 19.88	132.59%

Present & Proposed Rates (Without Taxes)
Residential 5/8 X 3/4-Inch Meters

Consumption	Rates	Rates	Increase	Rates	Increase
-	\$ 10.00	\$ 42.00	320.00%	\$ 26.51	165.10%
1,000	11.33	44.90	296.29%	28.06	147.66%
2,000	12.66	47.80	277.57%	29.61	133.89%
3,000	13.99	50.70	262.40%	32.61	133.10%
4,000	15.32	54.65	256.72%	35.61	132.44%
5,000	16.65	58.60	251.95%	38.61	131.89%
6,000	17.98	62.55	247.89%	41.61	131.42%
7,000	19.31	66.50	244.38%	45.61	136.20%
8,000	20.64	70.45	241.33%	49.61	140.36%
9,000	21.97	74.40	238.64%	53.61	144.01%
10,000	23.30	78.35	236.27%	57.61	147.25%
11,000	24.63	82.30	234.15%	61.61	150.14%
12,000	25.96	86.25	232.24%	65.61	152.73%
13,000	27.29	91.55	235.47%	71.61	162.40%
14,000	28.62	96.85	238.41%	77.61	171.17%
15,000	29.95	102.15	241.08%	83.61	179.17%
16,000	31.28	107.45	243.52%	89.61	186.48%
17,000	32.61	112.76	245.77%	95.61	193.19%
18,000	33.94	118.06	247.84%	101.61	199.38%
19,000	35.27	123.36	249.75%	107.61	205.10%
20,000	36.60	128.66	251.52%	113.61	210.41%
25,000	43.25	155.16	258.76%	143.61	232.05%
30,000	49.90	181.67	264.06%	173.61	247.92%
35,000	56.55	208.17	268.12%	203.61	260.05%
40,000	63.20	234.68	271.33%	233.61	269.64%
45,000	69.85	261.18	273.92%	263.61	277.39%
50,000	76.50	287.69	276.06%	293.61	283.80%
75,000	109.75	420.21	282.88%	443.61	304.20%
100,000	143.00	552.74	286.53%	593.61	315.11%

Service Line and Meter Installation Charges:		Service Line	Meter Installation	Total	Service Line	Meter Installation	Total
5/8" x 3/4" Meter	\$ 225	\$ 445	\$ 155	\$ 600	\$ 430	\$ 130	\$ 560
3/4" Meter	\$ 300	445	255	\$ 700	430	230	660
1" Meter	\$ 350	495	315	\$ 810	480	290	770
1 1/2" Meter	\$ 500	550	525	\$ 1,075	535	500	1035
2"	\$ 625	N/A	N/A	N/A	N/A	N/A	N/A
2" Turbine Meter	N/A	830	1045	\$ 1,875	830	1045	\$ 1,875
2" Compound Meter	N/A	830	1890	\$ 2,720	830	1890	\$ 2,720
3"	\$ 900	N/A	N/A	N/A	N/A	N/A	N/A
3" Turbine Meter	N/A	1045	1670	\$ 2,715	1045	1670	\$ 2,715
3" Compound Meter	N/A	1165	2545	\$ 3,710	1165	2545	\$ 3,710
4"	\$ 1,450	N/A	N/A	N/A	N/A	N/A	N/A
4" Turbine Meter	N/A	1490	2670	\$ 4,160	1490	2670	\$ 4,160
4" Compound Meter	N/A	1670	3645	\$ 5,315	1670	3645	\$ 5,315
6"	\$ 3,000	N/A	N/A	N/A	N/A	N/A	N/A
6" Turbine Meter	N/A	2210	5025	\$ 7,235	2210	5025	\$ 7,235
6" Compound Meter	N/A	2330	6920	\$ 9,250	2330	6920	\$ 9,250
Service Charges							
Establishment	\$ 25.00	\$ 30.00			\$ 30.00		
Establishment (After Hours)	\$ 30.00	\$ 40.00			\$ 40.00		
Reconnection (Delinquent)	\$ 25.00	\$ 40.00			\$ 40.00		
Reconnection (Delinquent) after hours	N/A	\$ 50.00			\$ 50.00		
Meter Test (If Correct)	\$ 30.00	\$ 35.00			\$ 35.00		
Deposit	Note a	Per Rule*			Per Rule*		
Deposit Interest	Note a	Per Rule*			Per Rule*		
Re-Establishment (Within 12 Months)	Note b	Per Rule**			Per Rule**		
NSF Check	\$ 15.00	\$ 25.00			\$ 25.00		
Deferred Payment	Note c	1.5% per month			1.5% per month		
Meter Re-Read (If Correct)	\$ 15.00	\$ 20.00			\$ 20.00		
Late Fee	Note d	1.5% / Mo.			1.5% / Mo.		
Main Extension	N/A	Cost			N/A		
Monthly Service Charge for Fire Sprinkler	N/A	***			****		
<p>Note a: Deposits per Commission Rules §-14-2-403(B)(7)(a), (b), and (c); Interest per Commission Rules R14-2-403(D).</p> <p>Note b: Service Establishments re-establishments or reconnection charges per Commission Rule R14-2-403(D)</p> <p>Note c: Deferred Payments Per Commission Rules R14-2-409(G)(6)</p> <p>Note d: Late payment penalty of 1.5 percent of the unpaid balance.</p> <p>* Per Commission Rules R14-2-403.B</p> <p>** Months off the system times the monthly minimum per R14-2-403.D</p> <p>*** 1% of monthly minimum for a comparable sized meter connection, but less than \$5.00 per month. The service charge for fire sprinklers is only applicable for service lines separate and distinct from the primary service line.</p> <p>**** 2% of monthly minimum for a comparable sized meter connection, but less than \$10.00 per month. The service charge for fire sprinklers is only applicable for service lines separate and distinct from the primary service line.</p>							

BEFORE THE ARIZONA CORPORATION COMMISSION

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

IN THE MATTER OF THE APPLICATION OF) DOCKET NO. W-02062A-09-0466
SOUTHLAND UTILITIES COMPANY, INC.)
FOR AUTHORITY TO INCUR LONG-TERM DEBT)
_____)

IN THE MATTER OF THE APPLICATION OF) DOCKET NO. W-02062A-09-0515
SOUTHLAND UTILITIES COMPANY, INC.)
FOR A RATE INCREASE)
_____)

DIRECT
TESTIMONY
OF
KATRIN STUKOV
UTILITIES ENGINEER
ARIZONA CORPORATION COMMISSION
UTILITIES DIVISION

JULY 19, 2010

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EXHIBIT

ENGINEERING REPORT	EXHIBIT KS
--------------------------	------------

1 **INTRODUCTION**

2 **Q. Please state your name, place of employment and job title.**

3 A. My name is Katrin Stukov. My place of employment is the Arizona Corporation
4 Commission ("Commission"), Utilities Division, 1200 West Washington Street, Phoenix,
5 Arizona 85007. My job title is Utilities Engineer.

6
7 **Q. How long have you been employed by the Commission?**

8 A. I have been employed by the Commission since June 2006.

9
10 **Q. Please list your duties and responsibilities.**

11 A. As a Utilities Engineer, specializing in water and wastewater engineering, I inspect and
12 evaluate water and wastewater systems; obtain data, prepare reports; suggest corrective
13 action, provide technical recommendations on water and wastewater system deficiencies;
14 and provide written and oral testimony on rate and other cases before the Commission.

15
16 **Q. How many cases have you analyzed for the Utilities Division?**

17 A. I have analyzed over 50 cases covering various responsibilities for the Utilities Division.

18
19 **Q. What is your educational background?**

20 A. I graduated from the Moscow University of Civil Engineering with a Bachelor of Science
21 degree in Civil Engineering with a concentration in water and wastewater systems.

22
23 **Q. Briefly describe your pertinent work experience.**

24 A. Prior to my employment with the Commission, I was a design review environmental
25 engineer with the Arizona Department of Environmental Quality ("ADEQ") for twenty
26 years. My responsibilities with ADEQ included review of projects for the construction of

1 water and wastewater facilities. Prior to that, I worked as a civil engineer in several
2 engineering and consulting firms, including Bechtel, Inc. and Brown & Root, Inc., in
3 Houston, Texas.

4
5 **PURPOSE OF TESTIMONY**

6 **Q. Were you assigned to provide the Utilities Division Staff's ("Staff") engineering**
7 **analysis and recommendations for this Southland Utilities Company ("Southland" or**
8 **"Company") rate and finance case proceeding?**

9 A. Yes. I reviewed the Company's application and responses to data requests, and I visited
10 the Company's water system. This testimony and its attachment present Staff's
11 engineering evaluation.

12
13 **ENGINEERING REPORT**

14 **Q. Please describe the attached Engineering Report, Exhibit KS.**

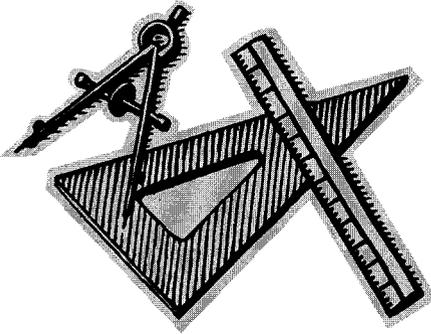
15 A. Exhibit KS presents the Company's water system' details and Staff's analysis and
16 findings, and is attached to this direct testimony. Exhibit KS contains the following major
17 topics: (1) a description and analysis of the water system, (2) water use, (3) growth, (4)
18 compliance with the rules of the ADEQ and Arizona Department of Water Resources, (5)
19 depreciation rates and (6) Staff's conclusions and recommendations.

20
21 **Q. Please summarize Staff's engineering conclusions and recommendations.**

22 A. Such a summary is provided at the beginning of Exhibit KS.

23
24 **Q. Does this conclude your direct testimony?**

25 A. Yes, it does.



**Engineering Report For
Southland Utilities Company, Inc.
Docket No. W-02062A-09-0515 (Rates) and
W-02062A-09-0466 (Finance)
May 26, 2010**

Conclusions

1. The Arizona Department of Environmental Quality (“ADEQ”) has reported that the Southland Utilities Company, Inc. (“Company” or “Southland”) water system has no deficiencies and the system is currently delivering water that meets water quality standards required by Arizona Administrative Code, Title 18, and Chapter 4.
2. The Company’s water system operates at a 6.5 percent water loss. This percentage is within acceptable limits of 10 percent.
3. Staff concludes that the Company’s water system has adequate source and storage capacities to serve the present customer base and anticipated growth.
4. Arizona Department of Water Resources (“ADWR”) has determined that Southland is currently in compliance with ADWR requirements governing water providers and/or community water systems.
5. A check of the Compliance Section database showed that there are currently no delinquent compliance items for the Company.
6. The Company has an approved curtailment plan tariff.
7. The proposed capital improvement project and estimated costs associated with the financing request totaling \$1,331,320 as delineated in Table D of the Engineering Report appear to be reasonable and appropriate. No “used and useful” determination of the proposed project items were made and no particular treatment should be inferred for rate making or rate base purposes in the future.

Recommendations

1. Staff recommends that Southland be ordered to monitor and assure that its well pump meters are operating properly. The Company should repair or replace any meter not operating properly immediately.

2. Southland does not have a backflow prevention tariff. Staff recommends that the Company file a backflow prevention tariff with Docket Control, as a compliance item in this same docket, within 45 days after the effective date of the decision in this case for the review and certification of Staff. Staff further recommends that this tariff shall generally conform to the sample tariff found on the Commission's web site at www.azcc.gov/divisions/utilities/forms/CrossConnection/BackflowTariff.pdf. Staff recognizes that the Company may need to make minor modifications to the sample tariff according to its specific management, operational, and design requirements as necessary and appropriate.
3. Staff recommends its annual water testing expense estimate of \$2,958 be used for this proceeding.
4. Staff recommends that the Company use depreciation rates by individual NARUC plant category as delineated in Table B.
5. Staff recommends acceptance of the Company's proposed service line and meter installation charges as shown in Table C.
6. Staff concludes that the storage tank and booster pump station constructed at Site 2 and related costs totaling \$348,147.92 appear to be reasonable and appropriate. The storage tank at Site 3 and related costs totaling \$257,703.52 appear to be reasonable and appropriate. Staff obtained from the Company a cost breakdown to support these costs. Staff has reviewed the cost breakdown and recommends that the Company's engineering and construction cost allocations be adjusted as summarized in Table E of the Engineering Report. No particular treatment of the storage tank at Site 3 for future rate making or rate base purposes should be inferred.

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I. INTRODUCTION AND LOCATION OF COMPANY

On September 29, 2009, Southland Utilities Company, Inc. (“Company” or “Southland”) filed for authority to incur long-term debt with the Arizona Corporation Commission (“ACC” or “Commission”).¹ On November 5, 2009, Southland filed for an increase in its water rates.² The Company’s current rates were approved in Commission Decision No. 61335, dated January 7, 1999. The ACC Utilities Division Staff (“Staff”) engineering review and analysis of the applications are presented in this report.

The Company provides water service to approximately 600 customers in a subdivided area located approximately five miles south of Sierra Vista, in Cochise County.

The plant facilities were visited on February 18, 2010, by Katrin Stukov, Staff Utilities Engineer, accompanied by Company operation representatives Eddy Morales, Operations Manager, Keith Dojaquez, Assistant Operations Manager, Gary Newman, Field Technician and the Company engineers Greg Carlson and James McMurtrie.

Figure 1 shows the location of Southland within Cochise County and Figure 2 delineates the eastern and western portions the Company’s certificated area (“CC&N”) which covers approximately 9.4 square-miles or 6,030 acres. The current service area for the existing water system is within the approximate 1.8 square-miles or 1,150 acres of the western portion of CC&N shown on Figure 2. In response to KS-3.1, the Company indicated that it currently does not serve landowners in the eastern portion of its CC&N, and the Company believes that these residents receive water from private wells or haul water³.

¹ Southland subsequently amended its financing application on April 12, 2010.

² Southland subsequently amended its rate application on November 23, 2009 and April 12, 2010.

³ The Southland water distribution system does not currently extend to the eastern portion of the CC&N.

Figure 1

COCHISE COUNTY

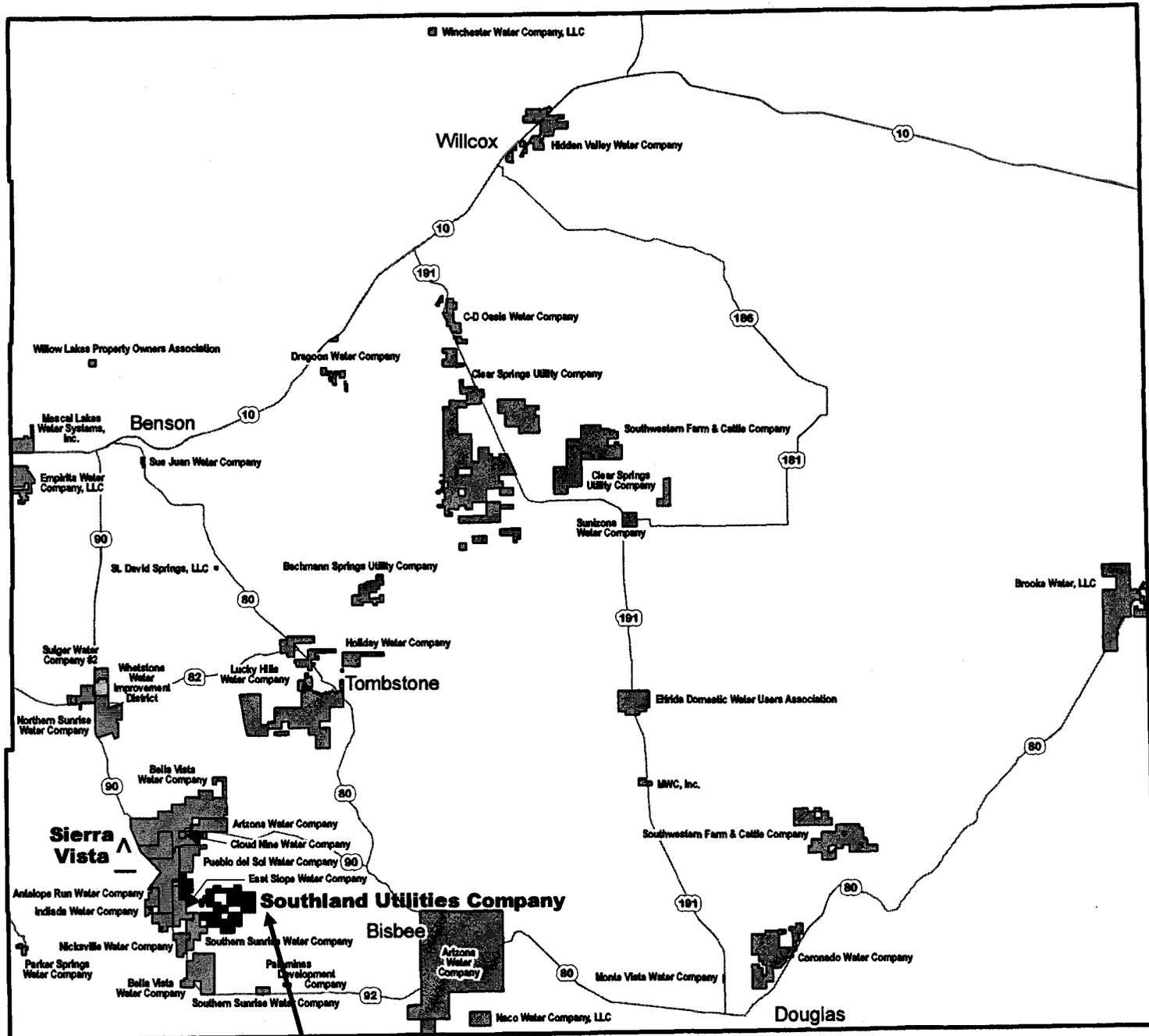
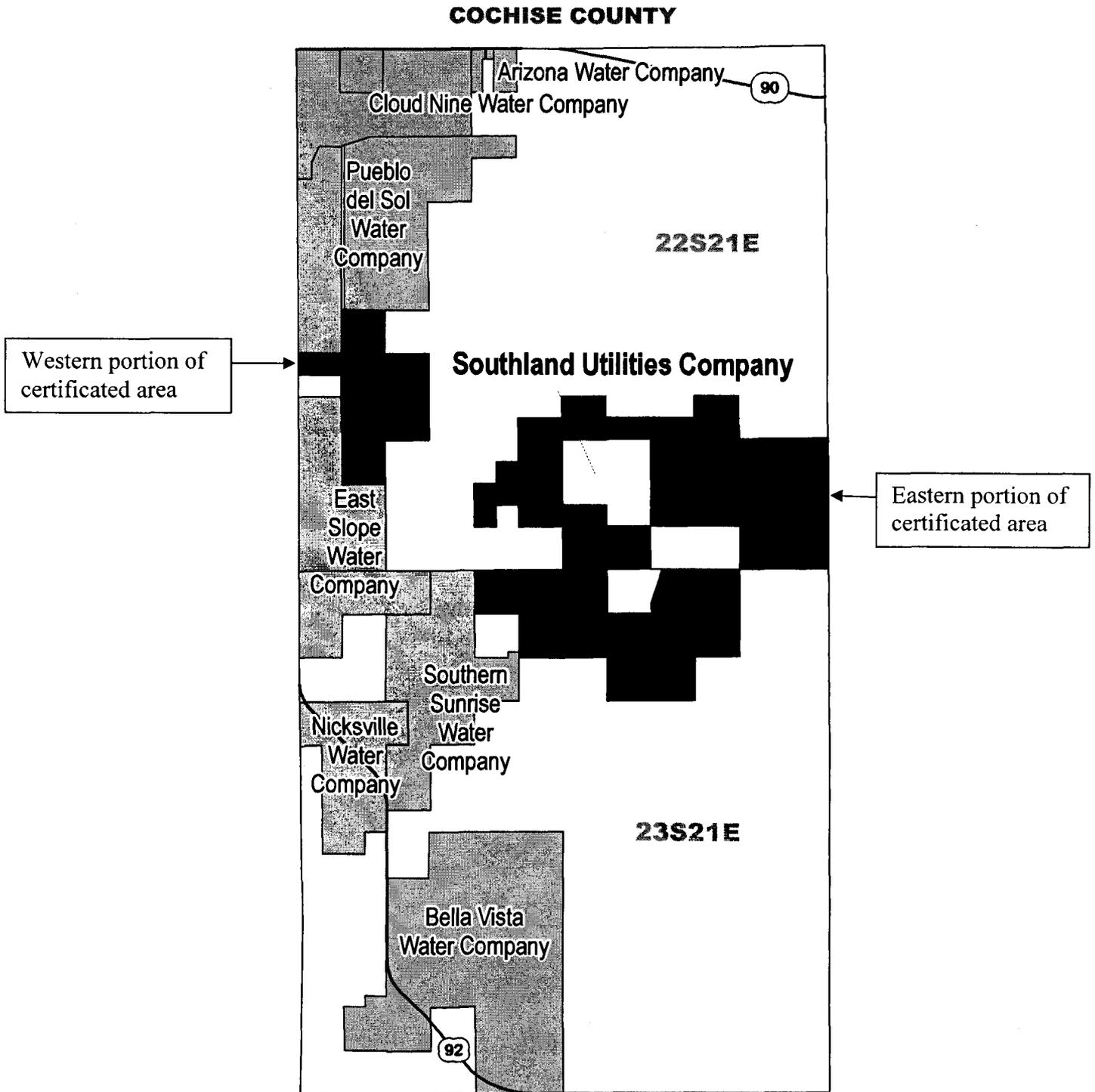


Figure 2



II. WATER SYSTEM

1. Description of the Water System

The Southland water system's plant is located on three separate sites and includes two wells, three storage tanks (only two storage tanks were in-service at the time of Staff's inspection), five booster pumps, a pressure tank, a bladder tank and a distribution system serving approximately 600 connections in the western portion of the Southland certificated area. A water system schematic is shown in Figure 3 and a plant facilities summary⁴ is tabulated below:

Wells

Plant Location	ADWR Well ID	Pump (HP)	Pump Yield (GPM)	Casing Depth (feet)	Casing Diameter (inches)	Meter Size (inches)	Year Drilled
Site 1	55-626149	40	150	600	12	4	1967
Site 2	55-626150	50	170	600	14-12-10	6	1968

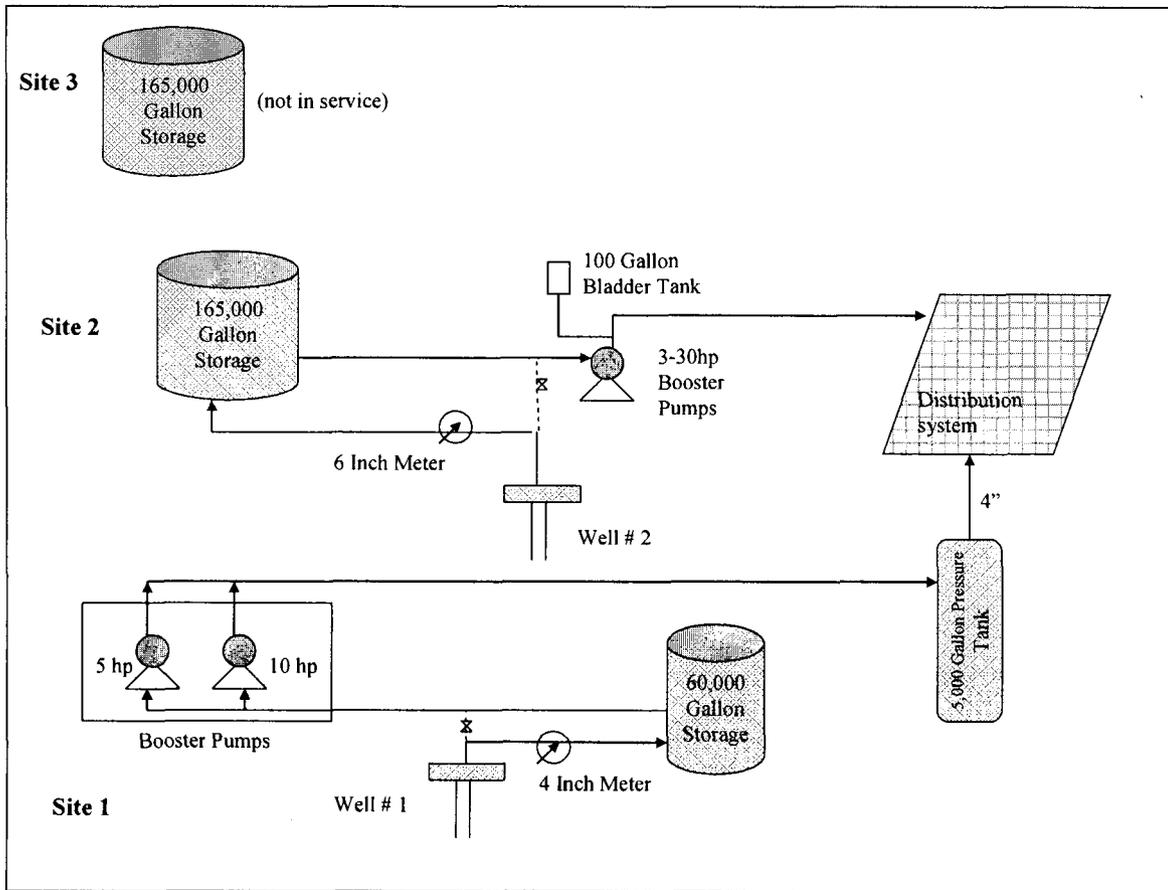
Plant Location	Storage Tanks		Pressure Tanks		Booster Pumps	
	Capacity (gallons)	Quantity	Capacity (gallons)	Quantity	Capacity (HP)	Quantity
Site 1	60,000	1	5,000	1	5 10	1 1
Site 2	165,000	1 (2008)	100 Bladder tank	1 (2008)	30	3 (2008)
Site 3	165,000 (Plant is not in service ⁵)	1 (2008)				

Mains			Customer Meters		Fire Hydrants	Treatment and Site Improvements
Size (inches)	Material	Length (feet)	Size (inches)	Quantity	Quantity	
2	Steel	1,000	5/8x3/4	620	36	2 Automated Chlorinators
4	AC	18,122	2	3		554 feet of 5 foot tall chain link fence
6	AC	28,260	Turbo 3	1		10'x 12' storage structure(brick)
6	PVC	2,711	Turbo 4	1		

⁴ Per Company's responses to Data Requests and Staff observations during its site visit

⁵ See Section VIII (Financing) in this report for more details.

Figure 3
Southland System Schematic

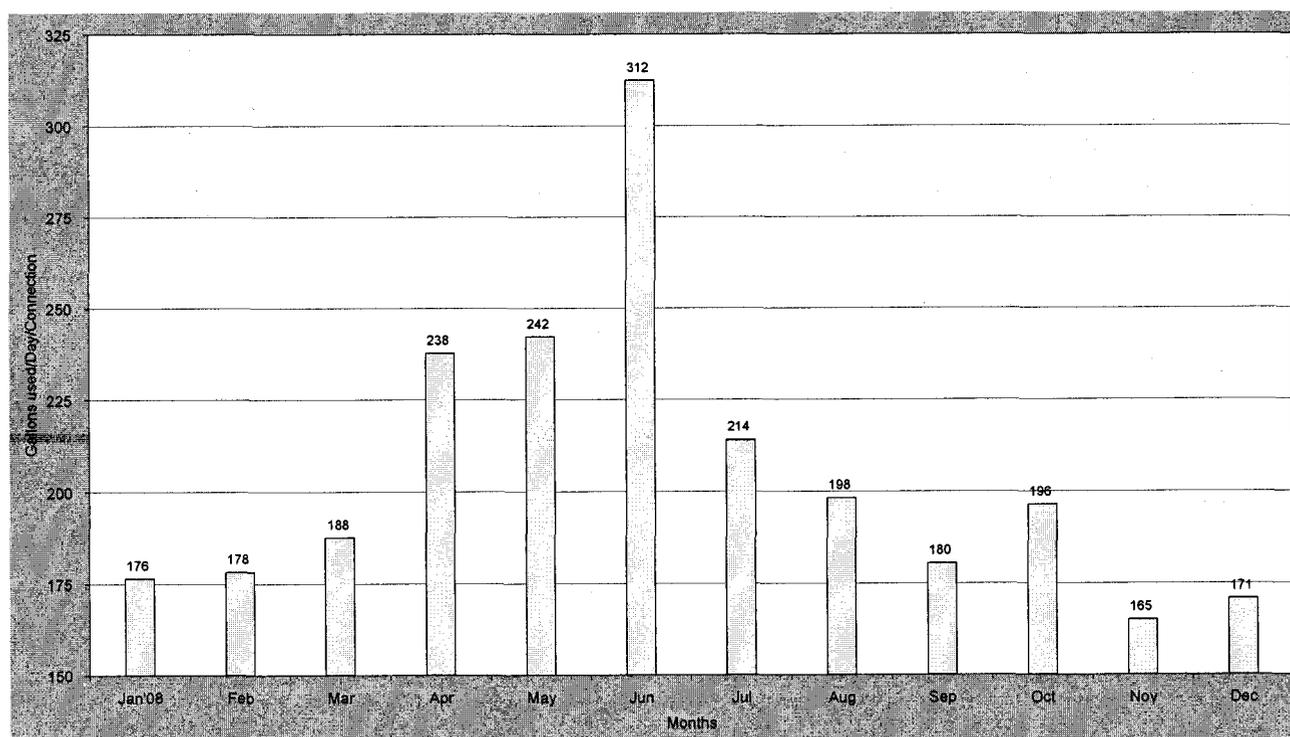


2. Water Use

Water Sold

Figure 4 represents the water consumption data provided by the Company in its water use data sheet for the test year ending December 31, 2008. Customer consumption included a high monthly water use of 312 Gallons Per Day (“GPD”) in June, and the low water use was 165 GPD per connection in November. The average annual use was 205 GPD per connection.

Figure 4 Water Use



Non-account Water

Non-account water should be 10 percent or less, and never more than 15 percent. It is important to be able to reconcile the difference between water sold and the water produced by the source. A water balance will allow a company to identify water and revenue losses due to leakage, theft and flushing.

The Company did not provide Gallons Pumped Data from January through October in 2008 in its water use data sheet for 2008. The Company explained that this data is not available because records from January to July 2008 were destroyed in a fire. In addition, the Well #1 meter was inoperable from August to October 2008. Staff requested the Company provide water use data for 2009 to evaluate a full 12 months of more recent data. In response, the Company

reported 54,633,000 gallons pumped and 51,101,000 gallons sold in 2009⁶, resulting in a water loss of 6.5 percent. This percentage is within acceptable limits of 10 percent.

Staff recommends that the Company be ordered to monitor and assure that its well pump meters are operating properly. The Company should repair or replace any meter not operating properly immediately.

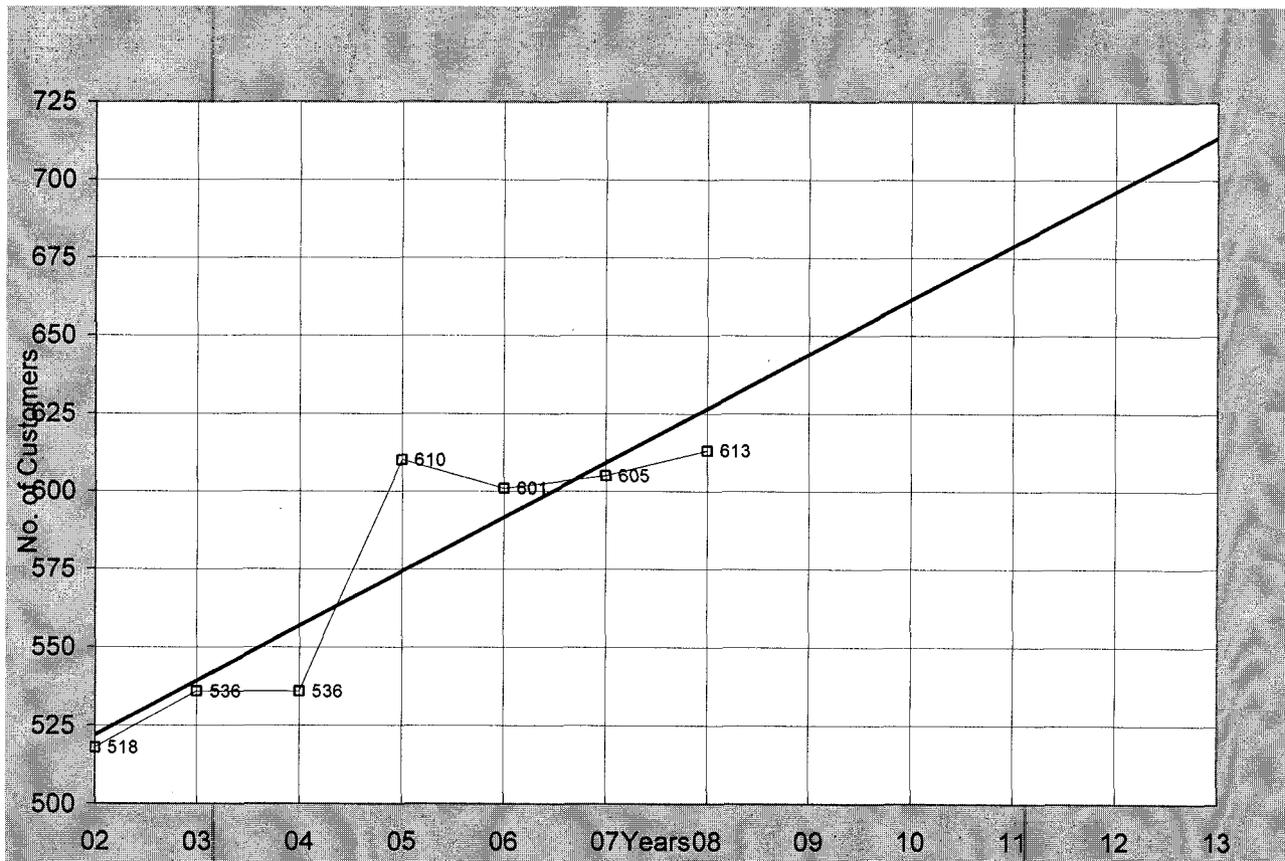
3. System Analysis

Based on the data provided by the Company for the Test Year, Staff concludes that the system's well total production capacity of 320 GPM, and total storage capacity of 225,000 gallons (in service) is adequate to serve the present customer base and reasonable growth.

4. Growth

Based on customer data obtained from the Company's Annual Reports, it is projected that the Company could have over 700 customers by 2013. Figure 5 depicts actual growth from 2002 to 2008 and projects an estimated growth for the next five years using linear regression analysis.

Figure 5 Growth Projection



⁶ Per Company's e-mail dated April 27, 2010

III. ARIZONA DEPARTMENT OF ENVIRONMENTAL QUALITY (“ADEQ”) COMPLIANCE

Compliance

ADEQ regulates the Southland water system under ADEQ Public Water System (“PWS”) No. 02-029. ADEQ has reported that the Company’s water system has no deficiencies and the system is currently delivering water that meets water quality standards required by Arizona Administrative Code, Title 18, and Chapter 4.⁷

Water Testing Expense

Participation in the ADEQ Monitoring Assistance Program (“MAP”) is mandatory for water systems which serve less than 10,000 persons (approximately 3,300 service connections).

Based on data provided by the Company⁸, Staff’s estimated average water testing expenses for the Southland water system at \$2,958. Table A shows average annual monitoring expense estimate totaling \$2,717 with participation in the MAP (ADEQ - MAP invoice for the 2009 Calendar Year rounded was \$1,638).

Staff recommends its annual water testing expense estimate of \$2,958 be used for purposes of this rate proceeding.

Table A. Water Testing Cost

Southland Water System (PWS#02-029)

Monitoring	Cost per Sample	No of samples per year	Average Annual Cost
Total coliform - monthly	\$25	24	\$600
TTHM-annualy	\$150	2	\$300
HAA5-annualy	\$155	2	\$310
Lead & Copper – per 3 years	\$33	10/3-yrs	\$110
MAP – IOCs, SOCs, VOCs, Radiochemical, Nitrate, Nitrite, Asbestos- annualy	MAP	MAP	\$1,638
Total			\$2,958

⁷ Per ADEQ Compliance Status Report dated November 3, 2009.

⁸ Per Company’s response to Staff’s first set of data requests KS 1.1(Rates).

IV. ARIZONA DEPARTMENT OF WATER RESOURCES (“ADWR”) COMPLIANCE

The Company’s system is not located in an ADWR designated Active Management Area. ADWR has determined that the Company’s water system is currently in compliance with ADWR requirements governing water providers and/or community water systems.⁹

V. ACC COMPLIANCE

A check of Utilities Division Compliance Section database showed that there are currently no delinquent compliance items for the Southland.¹⁰

VI. DEPRECIATION RATES

Southland has been using a depreciation rate of 5.00 percent in every National Association of Regulatory Utility Commissioners (“NARUC”) plant category. In recent orders, the Commission has been adopting Staff’s typical and customary depreciation rates which vary by NARUC plant category. These rates are presented in Table B and it is recommended that the Company use these depreciation rates by individual NARUC plant category.

⁹ Per ADWR Compliance Status Report dated November 24, 2009.

¹⁰ Per ACC Compliance status check dated November 30, 2009.

**TABLE B
DEPRECIATION RATE TABLE FOR WATER COMPANIES**

NARUC Account No.	Depreciable Plant	Average Service Life (Years)	Annual Accrual Rate (%)
304	Structures & Improvements	30	3.33
305	Collecting & Impounding Reservoirs	40	2.50
306	Lake, River, Canal Intakes	40	2.50
307	Wells & Springs	30	3.33
308	Infiltration Galleries	15	6.67
309	Raw Water Supply Mains	50	2.00
310	Power Generation Equipment	20	5.00
311	Pumping Equipment	8	12.5
320	Water Treatment Equipment		
320.1	Water Treatment Plants	30	3.33
320.2	Solution Chemical Feeders	5	20.0
330	Distribution Reservoirs & Standpipes		
330.1	Storage Tanks	45	2.22
330.2	Pressure Tanks	20	5.00
331	Transmission & Distribution Mains	50	2.00
333	Services	30	3.33
334	Meters	12	8.33
335	Hydrants	50	2.00
336	Backflow Prevention Devices	15	6.67
339	Other Plant & Misc Equipment	15	6.67
340	Office Furniture & Equipment	15	6.67
340.1	Computers & Software	5	20.00
341	Transportation Equipment	5	20.00
342	Stores Equipment	25	4.00
343	Tools, Shop & Garage Equipment	20	5.00
344	Laboratory Equipment	10	10.00
345	Power Operated Equipment	20	5.00
346	Communication Equipment	10	10.00
347	Miscellaneous Equipment	10	10.00
348	Other Tangible Plant	----	----

NOTES:

1. These depreciation rates represent average expected rates. Water companies may experience different rates due to variations in construction, environment, or the physical and chemical characteristics of the water.
2. Acct. 348, Other Tangible Plant may vary from 5 percent to 50 percent. The depreciation rate would be set in accordance with the specific capital items in this account.

VII. OTHER ISSUES

1. Service Line and Meter Installation Charges

In its application the Company has requested changes to its service line and meter installation charges. These charges are refundable advances and the Company's proposed charges are within Staff's recommended range for these charges. Therefore, Staff recommends the acceptance of the Company's proposed installation charges as shown in Table C.

**TABLE C
SERVICE LINE AND METER INSTALLATION CHARGES**

Meter Size	Present Installation Charges for Sonoita	Company's Proposed Installation Charges		
		Service Line Installation Charges	Meter Installation Charges	Total Charges
5/8"x 3/4"	\$225	\$445	\$155	\$600
3/4"	\$300	\$445	\$255	\$700
1"	\$350	\$495	\$315	\$810
1-1/2"	\$500	\$550	\$525	\$1,075
2"	\$625	N/A	N/A	N/A
2"- Turbine	N/T	\$830	\$1,045	\$1,875
2"- Compound	N/T	\$830	\$1,890	\$2,720
3"	\$900	N/A	N/A	N/A
3"- Turbine	N/T	\$1,045	\$1,670	\$2,715
3"- Compound	N/T	\$1,165	\$2,545	\$3,710
4"	\$1,450	N/A	N/A	N/A
4"- Turbine	N/T	\$1,490	\$2,670	\$4,160
4"- Compound	N/T	\$1,670	\$3,645	\$5,315
6"	\$3,000	N/A	N/A	N/A
6"-Turbine	N/T	\$2,210	\$5,025	\$7,235
6"-Compound	N/T	\$2,330	\$6,920	\$9,250

Note: "N/T"- No Tariff; "N/A"- Not Applicable

2. Curtailment Plan Tariff

The Company has an approved curtailment plan tariff.

3. Backflow Prevention Tariff

Southland does not have an approved backflow prevention tariff. Staff recommends that the Company file a backflow prevention tariff with Docket Control, as a compliance item in this same docket, within 45 days after the effective date of the decision in this case for the review and certification of Staff. Staff further recommends that this tariff shall generally conform to the sample tariff found on the Commission's web site at www.azcc.gov/divisions/utilities/forms/CrossConnection/BackflowTariff.pdf. Staff recognizes that the Company may need to make minor modifications to the sample tariff according to its specific management, operational, and design requirements as necessary and appropriate.

VIII. FINANCING

The Company submitted a financing application to incur long term debt requesting the Commission's approval to borrow \$1,825,942 from the Water Infrastructure and Financing Authority ("WIFA") to fund capital improvements to the Southland water system. This amount includes \$1,331,320 (rounded) for acquiring a portable on-site generator, distribution system replacements and upgrades needed to provide fire protection, piping and a booster pump station at Site 3, the installation of fire hydrants, the installation of pressure-relief valves ("PRVs"), and \$494,622 for refinancing a prior short-term loan used to fund the addition of two storage tanks. The Company borrowed \$494,622 from Tucson/Sierra Properties, LLC in 2008 to install storage tanks at Sites 2 & 3 and a booster pump station at Site 2. During its site inspection Staff observed that the storage tank and associated booster pump station at Site 2 were completed and in-service. Construction of the storage tank at Site 3 had not been completed. Piping and a booster station must be constructed before this tank can be placed into service (see Table D below for more detail about the plant required to complete the tank construction at Site 3).

1. Proposed Upgrades and Improvements (financing request of \$1,331,320)

The Company's proposed improvements as summarized in the prior paragraph are delineated in more detail in Table D below. The Company submitted an initial modeling of the distribution system and an Opinion of Probable Costs ("OPC") prepared by Greg Carlson Engineering, L.L.C. The OPC outlined the following capital improvements and costs.

TABLE D

Priority	Item No	Item Description	Quantity	Unit	Unit Price	Extended Price
1	Portable Back-up Generator					
	1	Onsite Generator 350 KW	1	LS	\$64,500.00	\$64,500.00
2	Distribution System Upgrades					
	<i>Replace/Upgrade Distribution Mains</i>					
	2	12-inch pipe along Campobello Ave alignment between Goldfinch Cr and Wakefield St	Approx 3,350'	LF	\$60.00	\$201,000.00
	3	6-inch pipe Kensington St	Approx 1,350'	LF	\$28.00	\$37,800.00
	4	6-inch pipe Kevin St	Approx 1,350'	LF	\$28.00	\$37,800.00
	5	6-inch pipe Bevers/San Pedro	Approx 1,525'	LF	\$28.00	\$42,700.00
	6	12-inch pipe along Golden Acres Drive	Approx 3,500'	LF	\$60.00	\$210,000.00
	7	8-inch pipe to replace 2" pipe running south from Golden Acres Drive near Self Storage area.	Approx 420'	LF	\$45.00	\$18,900.00
	8	8-inch pipe from Finch Cr to Buffalo Soldier	Approx 2,509'	LF	\$45.00	\$112,905.00
	9	8-inch pipe to replace some of 2" & 4" east-west pipes near Bufffalo Soldier	Approx 1,200'	LF	\$45.00	\$54,000.00
	10	12-inch pipe from Bevers to Penny Lane	Approx 650'	LF	\$60.00	\$39,000.00
	11	6-inch pipe Penny Lane	Approx 350'	LF	\$28.00	\$9,800.00
	12	8-inch pipe Penny Lane	Approx 380'	LF	\$45.00	\$17,100.00
	13	12-inch pipe Penny Lane	Approx 1,325'	LF	\$60.00	\$79,500.00
	14	8-inch pipe Penny to San Mateo	Approx 650'	LF	\$45.00	\$29,250.00
	15	8-inch San Mateo to alley south of San Mateo	Approx 350'	LF	\$45.00	\$15,750.00
	16	8-inch pipe Alley south of San Mateo to San Molino	Approx 700'	LF	\$45.00	\$31,500.00
17	8-inch pipe San Molino	Approx 1,650'	LF	\$45.00	\$74,250.00	
					<i>Subtotal</i>	<i>\$1,011,255.00</i>

<i>Piping for storage tank at Site 3</i>					
18	New 6" tank fill line	Approx 250'	LF	\$28.00	\$7,000.00
19	8" discharge pipe from tank to Golden Acres Drive	Approx 250'	LF	\$55.00	\$13,750.00
<i>Subtotal</i>					<i>\$20,750.00</i>
<i>New booster station for storage tank at Site 3</i>					
20	Booster Pumps End Suction	2 @ 350gpm	LS	\$877.00	\$1,754.00
21	Fittings, valves, check valve and manifold setup	---	LS	\$15,000.00	\$15,000.00
22	Electrical for site 3	1	LS	\$45,000.00	\$45,000.00
<i>Subtotal</i>					<i>\$61,754.00</i>
<i>Install Fire Hydrants</i>					
23	Hydrants (Kensington between San Pedro and Louise)	3	EA	\$1,640.00	\$4,920.00
24	Hydrants (Kevin between San Pedro and Louise)	3	EA	\$1,640.00	\$4,920.00
25	Hydrants (Beverly between San Pedro and Louise)	3	EA	\$1,640.00	\$4,920.00
26	Hydrant (San Pedro north of Kensington)	1	EA	\$1,640.00	\$1,640.00
27	Hydrants (500' intervals in Golden Meadows No. 2)	10	EA	\$1,640.00	\$16,400.00
28	Hydrants (Near/in development near bus barn off of Buffalo Soldier)	3	EA	\$1,640.00	\$4,920.00
29	Hydrants (Penny Lane)	5	EA	\$1,640.00	\$8,200.00
30	Hydrants (San Mateo)	5	EA	\$1,640.00	\$8,200.00
31	Hydrants (San Molino)	5	EA	\$1,640.00	\$8,200.00
<i>Subtotal</i>					<i>\$63,135.00</i>
<i>Combine Two Pressure Zones</i>					
32	Individual Private PRVs	Approx 10	EA	\$81.50	\$815.00
Subtotal					\$1,221,394.00
Administration and legal fees		2% of Construction Cost		\$24,427.88	
Engineering Fees		5% of Construction Cost		\$61,069.70	
Survey, Geotech, etc		1% of Construction Cost		\$12,213.94	
Project inspection fees		1% of Construction Cost		\$12,213.94	
Total					\$1,331,319.46

Staff concludes the proposed upgrades and improvements and estimated costs totaling \$1,331,320 appear to be reasonable and appropriate. No "used and useful" determination of the proposed project items were made and no particular treatment should be inferred for rate making or rate base purposes in the future.

2. Completed Tank Improvements (refinancing request of \$494,622)

The completed tank improvements included replacement of a leaking 25,000 gallon storage tank with a new 165,000 gallon tank and booster pump station at Site 2 and, the installation of a new 165,000 gallon tank at Site 3. ADEQ AOC certificates for these improvements were issued on September 18, 2008.

According to the Company, the storage tank at Site 3, when completed, will provide additional storage for fire flow and will help to alleviate water shortages when wells become inoperable due to mechanical failure or in the event well production declines during times of peak demand.

Through data requests, Staff obtained from the Company a cost breakdown to support the financing request of \$494,622. The Company reported a total project cost for the tank improvements of \$605,851.43. Staff has reviewed the cost breakdown¹¹ and has adjusted the Company's engineering and construction cost allocations. The Company's cost breakdown, as adjusted by Staff, is summarized in Table E below.

TABLE E

Description	Site 2 Improvements (Company)	Site 2 Improvements (Staff)	Site 3 Improvements (Company)	Site 3 Improvements (Staff)	Totals Improvements Sites 2 & 3
Tank materials	\$114,384.60	\$114,384.60	\$114,384.60	\$114,384.60	\$228,769.20
Engineering	\$47,042.30 (80%)	\$28,155.20 (50%)	\$9,268.09 (20%)	\$28,155.20 (50%)	\$56,310.39
Construction contractor	\$266,300.67	\$189,731.15	\$31,407.63	\$107,977.15	\$297,708.30
Structural contractor (Retaining Wall)	-	-	\$8,186.57	\$8,186.57	\$8,186.57
Electric line extension	\$9,764.97	\$9,764.97	-	-	\$9,764.97
On-site security service	\$5,112.00	\$5,112.00	-	-	\$5,112.00
Totals	\$442,604.54	\$348,147.92	\$163,246.89	\$257,703.51	\$605,851.43

¹¹ Submitted by the Company on May 26, 2010

Staff concludes that the storage tank and booster pump station constructed at Site 2 and related costs totaling \$348,147.92 appear to be reasonable and appropriate. The storage tank at Site 3 and related costs totaling \$257,703.52 appear to be reasonable and appropriate. No particular treatment of the storage tank at Site 3 for future rate making or rate base purposes should be inferred.