

OPEN MEETING AGENDA ITEM



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BEFORE THE BLACK MOUNTAIN CORPORATION COMMISSION

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EXCEPTION

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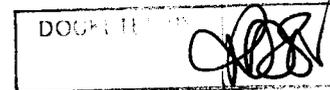
IN THE MATTER OF THE APPLICATION OF SEWER COMPANY, AN BLACK MOUNTAIN CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY, AND FOR ADJUSTMENTS TO ITS RATES AND CHARGES FOR UTILITY SERVICE AND FOR CERTAIN RELATED APPROVALS BASED THEREON.

Docket No. SW-02361A-08-0609

Arizona Corporation Commission

DOCKETED

AUG 12 2010



EXCEPTIONS OF THE RESIDENTIAL UTILITY CONSUMER OFFICE

The Residential Utility Consumer Office ("RUCO") makes the following Exceptions to the Recommended Opinion and Order ("ROO") on Black Mountain Water Company's ("Black Mountain" or "Company's") application for a rate increase.

1. The Commission should reject the Surcharge Proposed by BHOA and the Company as a means of effectuating the Closure.

Under the terms of the settlement agreement with the Boulder's Homeowner Association ("BHOA"), the Company says it will close the wastewater treatment plant if the Commission authorizes a surcharge to cover their costs. No surcharge, no closure. All the homeowners want is for the bad odor to go away. The method of cost recovery doesn't matter to the

1 homeowners. If the Company insists it will only close the plant if it gets a surcharge, then the
2 homeowners want the surcharge.

3 The two questions for RUCO are:

4 Will closing the wastewater treatment plant solve the odor problem?

5 Why can't Black Mountain close the plant and seek traditional rate relief
6 instead of the extraordinary relief of a surcharge?

7
8 **A. Evidence in the record shows that closure of the wastewater treatment plant
9 may not solve the odor problem.**

10 RUCO supports the elimination of the odor and noise. If the decommissioning of the
11 plant would eliminate the odor and the noise issue RUCO would support the decommissioning
12 of the plant. RUCO, however, does not have engineers on its staff and relies on other
13 engineering reports to ascertain whether decommissioning the plant would solve the odor
14 problem. RUCO relied on the Staff's engineering report submitted in this record. And that
15 report indicates that there is some question as to whether decommissioning the plant will result
16 in the elimination of the odor and noise problem. Staff's engineer testified that the wastewater
17 treatment plant itself may not be the source of all odors.¹ Ms. Hains testified that the odor
18 issues arose not just from the wastewater treatment plant, but also from the multiple lift stations
19 which are located throughout the subdivision.² In closing, Staff argued *inter alia*, it is difficult to
20 justify removal of plant which is currently used and useful and functioning properly when the
21 problems of the plant are related to its proximity to homes rather than mechanical problems.³

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23 _____
24 ¹ T: 640-641
² *Id.*
³ Staff's Initial Brief at 25-26.

1 Further, Staff opined, as RUCO does here, that "where reliability and compliance are being met,
2 it is difficult to justify such an exorbitant price tag [estimated at \$1.5 and \$2.5 million] as a
3 simple gesture of good will." ⁴

4 Staff's and RUCO's position is further supported by the communications between BHOA
5 and BMSC. Correspondence with attorneys representing ACC Staff, BMSC and BHOA
6 indicates that there is no firm determination as to the actual source of the odor problem.⁵ Nor is
7 there any firm determination as to whether or not the removal of the treatment plant, as
8 provided for in the Agreement, would solve the odor problem cited in Mr. Peterson's testimony.
9 RUCO cannot simply ignore this testimony.

10 **B The Commission can order the closure of the plant without authorizing**
11 **a surcharge.**

12 Should the Commission decide that the closure of the plant is in the ratepayer's best
13 interests, RUCO disagrees that an adjustor mechanism which will add up to \$15.00 per month
14 to the rates of all ratepayers is the proper cost recovery method to effectuate the closure. The
15 surcharge proposed by the Company is an adjustor mechanism. Adjustor mechanisms are
16 extraordinary rate recovery devices that are permitted for certain narrow circumstances and
17 should not be implemented in lieu of a full rate case proceeding that allows for a proper
18 analysis of all the ratemaking elements that need to be considered before implementing new
19 rates.

20 The surcharge would isolate costs associated with the retirement of BMSC's treatment
21 facility, without providing an idea of what the full impact of the proposed retirement will have on
22 other system operating costs such as labor, purchased power, line maintenance, etc. While

23 _____

24 ⁴ *Id.*

⁵ Surrebuttal Testimony of William Rigsby at 4.

1 the Company can recover these costs, there is no corresponding deduction for these
2 associated savings. In other words, the costs authorized in the surcharge will not “match” the
3 savings realized by the Company.

4 RUCO believes that cost recovery mechanisms should be given the same weight as the
5 Commission has given adjustor mechanisms in the past.⁶ In Decision No. 68302 the
6 Commission denied Arizona Water’s request for an adjustor stating:

7
8 There is a danger of piecemeal regulation inherent in adjustment
9 mechanisms. Because they allow automatic increases in rates without a
10 simultaneous review of a utility’s unrelated costs, adjustment mechanisms
11 have a built-in potential of allowing a utility to increase rates based on certain
12 isolated costs when its other costs are declining, or when overall revenues
13 are increasing faster than costs due to customer growth. Adjustment
14 mechanisms should therefore be used only in extraordinary circumstances to
15 mitigate the effect of uncontrollable price volatility or uncertainty in the
16 marketplace.⁷

17 RUCO recommends that the Commission reject the cost recovery mechanism proposal.
18 A better alternative would be to allow BMSC to retire the treatment facility and require the
19 Company to file a general rate case application twelve months after the retirement. This would
20 provide ACC Staff, RUCO and any other intervenors the opportunity to conduct a full analysis
21 of all of the ratemaking elements associated with BMSC’s system, and to see what impact the
22 retirement of the treatment facility has had on BMSC’s cost of providing service. It would also
23 give ACC Staff, RUCO and other intervenors the ability to provide the Commission with the
24 information that is needed to set just and reasonable rates for all of the Company’s ratepayers.

⁶ Id. at 5.

⁷ See Exhibit R-7 Rigsby’s Surrebuttal Testimony at 5-6, citing *In the Matter of Arizona Water*, Docket No. W-01445A-04-0650, Decision No. 68302 dated September 8, 2004.

1 Another important consideration is that although 500 hundred people have voiced their
2 support for the Agreement, there are 2,100 customers in the Company's service area.⁸ Of
3 those 2,100 customers, 332 customers live in the BHOA. The remainder of the customers live
4 outside of BHOA and ostensibly are not affected by the odor issues, but will be required to pay
5 for the plant closure. There are 1,600 customers who will be paying for the decommissioning
6 of the plant who will receive no benefit.

7 If the Commission believes that closure of the plant is warranted, but adoption of the
8 surcharge mechanism is not, RUCO requests the Commission adopt Amendment 1, attached
9 hereto.

10 **2. A cost of equity ("COE") between 9.0 and 10.0 should be adopted.**

11 The ROO adopts the Staff's cost of equity of 10.2 percent. RUCO believes a lower cost
12 of equity is just and reasonable and recommends an 8.2 percent cost of equity. In what
13 appears to be the Commission's recognition of the current "financial crisis" the Commission
14 has started to reduce the cost of equity awards from the Commission's usual 10 percent.

15 The Commission has approved or has ROO's pending before it recommending the
16 following cost of equity percentages in recent rate cases:

18	Arizona Water	9.5%	(ROO in Docket No. W-01445A-08-0440) ⁹
19	Global Water	9.8%	(ROO in Docket No. SW-02445A-09-0077 et al.)
20	UNS Gas	9.5%	(Decision No. 71623)
21	Arizona-American	9.9%	(Decision No. 71410)

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23 ⁸ Testimony of Les Peterson at 2 line 5

24 ⁹ The Commission approved the 9.5 percent COE recommended by the ROO at its meeting on August 11, 2010, but a Decision No. has not yet been assigned.

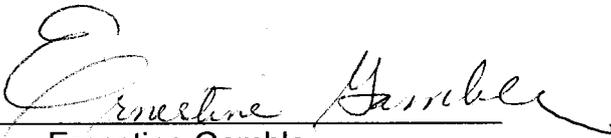
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Black Mountain Sewer Corporation
SW-02361A-08-0609
Proposed RUCO Amendment No. 1
Closure Agreement

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Although plant closure is appropriate given the abundance of complaints filed by BHOA homeowners, the surcharge mechanism proposed by the Company is not. The surcharge proposed by the Company is an adjustor mechanism. Adjustor mechanisms are extraordinary rate recovery devices that are permitted for certain narrow circumstances and should not be implemented in lieu of a full rate case proceeding that allows for a proper analysis of all the ratemaking elements that need to be considered before implementing new rates.

The surcharge would isolate costs associated with the retirement of BMSC's treatment facility, without providing an idea of what the full impact of the proposed retirement will have on other system operating costs such as labor, purchased power, line maintenance, etc. While the Company can recover these costs, there is no corresponding deduction for these associated savings. In other words, the costs authorized in the surcharge may not "match" the savings realized by the Company.

We believe that cost recovery mechanisms should be given the same weight as the Commission has given adjustor mechanisms in the past.² In Decision No. 68302 the Commission denied Arizona Water's request for an adjustor stating:

There is a danger of piecemeal regulation inherent in adjustment mechanisms. Because they allow automatic increases in rates without a simultaneous review of a utility's unrelated costs, adjustment mechanisms have a built-in potential of allowing a utility to increase rates based on certain isolated costs when its other costs are declining, or when overall revenues are increasing faster than costs due to customer growth. Adjustment mechanisms should therefore be used only in extraordinary circumstances to mitigate the effect of uncontrollable price volatility or uncertainty in the marketplace.³

We approve the closure agreement excluding the cost recovery mechanism proposal. In making this determination, we consider that 500 hundred people have voiced their support for the plant closure, but also consider that there are 2,100 customers in the Company's service area.⁴ Of those 2,100 customers, 332 customers live in the BHOA. The remainder of the customers live outside of BHOA and ostensibly are not affected by the odor issues, but if we approved the surcharge agreement would be required to pay for the plant closure. There are 1,600 customers who will be paying for the decommissioning of the plant who will receive no benefit.

BMSC is ordered to retire the treatment facility and required to file a general rate case application twelve months after the retirement. This will

² Id. at 5.

³ See Exhibit R-7 Rigsby's Surrebuttal Testimony at 5-6, citing *In the Matter of Arizona Water*, Docket No. Docket No. W-01445A-04-0650, Decision No. 68302 dated September 8, 2004.

⁴ Testimony of Les Peterson at 2 line 5

provide ACC Staff, RUCO and any other intervenors the opportunity to conduct a full analysis of all of the ratemaking elements associated with BMSC's system, and to see what impact the retirement of the treatment facility has had on BMSC's cost of providing service. It will also give ACC Staff, RUCO and other intervenors the ability to provide the Commission with the information that is needed to set just and reasonable rates for all of the Company's ratepayers.

Make all necessary conforming changes.

Black Mountain Sewer Corporation
SW-02361A-08-0609
Proposed RUCO Amendment No. 2
Cost of Equity

DELETE page 51, lines 15-21

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The cost of equity recommendations from parties range from 8.22 percent to 12.4 percent. In consideration of the current economic environment, we adopt a cost of equity of 9.5 percent. This is consistent with our decisions in Arizona Water (9.5%) Docket No. W-01445A-08-0440);¹ UNS Gas (9.5%), Decision No. 71623; and Arizona-American (9.9%) Decision No. 71410. There are no circumstances in this case, or nothing unique or unusual to the Company, which persuade us to change course here.

Make all necessary conforming changes.

¹ The Commission approved the 9.5 percent COE recommended by the ROO at its meeting on August 11, 2010, but a Decision No. has not yet been assigned.