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BEFORE THE ARIZONA CORPORATION COMMISSION
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2010 SEP 10 P 4: 27

ARIZONA CORPORATION COMMISSION
DOCKET CONTROL

IN THE MATTER OF THE APPLICATION OF
COMMUNITY WATER COMPANY OF
GREEN VALLEY FOR A DETERMINATION
THAT THE "AGREEMENT FOR PAST CAP
M&I WATER SERVICE CAPITAL CHARGES
(INSTALLMENT)" WITH CENTRAL
ARIZONA WATER CONSERVATION
DISTRICT IS NOT AN EVIDENCE OF
INDEBTEDNESS REQUIRING COMMISSION
APPROVAL UNDER A.R.S. §§ 40-301 AND
40-302; OR, IN THE ALTERNATIVE,
APPROVAL OF THAT AGREEMENT.

DOCKET NO. W-02304A-09-0575

Arizona Corporation Commission

DOCKETED

SEP 10 2010



STAFF'S RESPONSE TO COMPANY'S
RESPONSE TO STAFF REPORT

The Utilities Division ("Staff") of the Arizona Corporation Commission files its reply to the response filed by Community Water Company of Green Valley ("CWCGV" or "Company")) to the Staff Report dated August 17, 2010.

I. BACKGROUND.

The Company, a Class B water utility is a non profit, member owned cooperative providing service in the Green Valley, Arizona area. On September 5, 2008, CWCGV filed an application for authority to issue a long term debt of \$2,810,000.¹ The purpose of the \$2,810,000 was to pay off a balance of a non-revolving line of credit authorized by Decision No. 67515, and to fund \$310,000 of capital improvements. During the course of the review of the Company's financials, Staff learned that the Company had entered into a 5-year agreement with the Central Arizona Water Conservation District ("CAWCD") for an additional Central Arizona Project ("CAP") allocation.

On November 21, 2007, the Company entered into a long-term agreement with the CAWCD for an additional Central Arizona Project allocation ("Agreement"). To pay for this additional CAP

¹ In the Matter of the Application of Community Water Company of Green Valley, Docket No. W-020304A-09-0153.

1 allocation, the Company elected a five year payment plan with annual installments of \$222,995 as
2 opposed to a single lump-sum payment of \$1,015,665.² The payment of installments includes an
3 interest component of 5.2%. At that time, Staff recommended that the Company file an application,
4 so that the Commission could determine if the Agreement with the CAWCD falls under A.R.S. §§
5 40-301 and 40-302. Decision No. 71259 ordered the Company to file an application regarding the
6 necessity of Commission approval of the Company's long-term Agreement with CAWCD.

7 In compliance with Decision No. 71259, the Company filed an application for a determination
8 that the Agreement with the CAWCD is not an evidence of indebtedness under A.R.S. §§ 40-301 and
9 40-302 or, in the alternative, requesting approval of the Agreement. In its Staff Report dated August
10 17, 2010, Staff concluded that the installment payment plan is a note evidencing indebtedness,
11 requiring Commission approval pursuant to A.R.S. § 40-301 *et seq.* Staff also recommended
12 approval of the financing.

13 The Company continues to argue that the Agreement is not a debt requiring Commission
14 approval under A.R.S. § 40-301 *et seq.* In Docket No. W-020304A 09-0153, the Company argued
15 that the Agreement is "effectively a 5-year installment contract for the payment of past CAP M&I
16 water service capital charges" and that the Agreement is similar to a contract to purchase a good or
17 service with a set number of installment payments."³ The Company further asserted that the payment
18 of past CAP M&I water service charges is a no-risk contract that does not encumber any other assets
19 of CWCGV. The Company also argued that, in the event the Company decides it no longer wants the
20 additional CAP allocation, it is refunded any payments that it has made. Because of the foregoing,
21 the Company contended that the Agreement and the underlying financial transaction are not subject
22 to review by the Commission. The Company also asserted that it is unaware of any similar
23 arrangements as the one contemplated by the Agreement requiring Commission approval. The
24 Company is making the same arguments in the instant case. The Company's arguments neglect to
25 acknowledge one of the purposes of A.R.S. § 40-301 *et seq.*: to ensure the financial health by
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28 ² CWCGV Annual Report 2008 at 14.

³ Company response to Staff Report dated July 7, 2010 at 2; 3.

1 reviewing the amount of debt maintained by a public service corporation to ensure that service to the
2 public is not impacted.

3 **II. THE AGREEMENT IS A TRADITIONAL FINANCING ARRANGEMENT SUBJECT**
4 **TO A.R.S. § 40-301 ET SEQ.**

5 The Company has acknowledged that the Agreement has the characteristics of a loan. In its
6 2008 Annual Report to its members, the Agreement is described as a long term debt obligation. The
7 Commission has the statutory authority to review and approve such instruments. The Company's
8 reliance on the application of the statutory doctrine of *ejusdem generis* to disregard the Commission's
9 statutory authority is misplaced.

10 The doctrine of *ejusdem generis*, like other rules of statutory construction, is an aid in
11 ascertaining the legislative intent.⁴ Where the intent of the Legislature is apparent, it may not be used
12 to obscure and defeat the intent and purpose of the legislation.⁵ The doctrine of *ejusdem generis*,
13 however, is only a rule of construction, to be applied as an aid in ascertaining the legislative intent,
14 and does not control where it clearly appears from the statute as a whole that no such limitation was
15 intended. Nor does the doctrine apply where the specific words of a statute signify subjects greatly
16 different from one another, nor where the specific words embrace all objects of their class, so that the
17 general words must bear a different meaning from the specific words or be meaningless.⁶

18 While the installment arrangement may not be a stock or a bond, Staff would caution against
19 such a narrow reading of A.R.S. § 40-301, as proposed by the Company, in limiting the types of
20 financing arrangements and mechanisms that may be considered an "evidence of indebtedness".
21 Financing arrangements have evolved since the adoption of A.R.S. § 40-301 and may, or may not,
22 mirror traditional forms of indebtedness. Staff would argue that the Legislature intended to allow the
23 Commission flexibility in reviewing the debt obligations of the utilities it regulates to ensure their
24 financial health and to protect the public.

25 The need for flexibility is evident by the Commission's decision in Docket No. E-01345A-06-
26 0779. In that docket, Arizona Public Service Company ("APS") had requested blanket approval for

27 ⁴ *United States v. Gilliland*, 312 U.S. 86, 61 S.Ct. 518, 85 L.Ed. 598 (1941).

28 ⁵ *United States v. Alpers*, 338 U.S. 680, 70 S.Ct. 352, 94 L.Ed. 457 (1950).

⁶ *Arizona Superior Min. Co. v. Anderson*, 33 Ariz. 64, 262 P. 489 (1927).

1 certain of its financing activities and related increases to the debt limits imposed on APS by law and
2 by previous Commission orders. In order to avoid the need for further Commission approval, APS
3 asked the Commission to issue a declaratory order (i) confirming that only traditional indebtedness
4 for borrowed money constituted evidence of indebtedness pursuant to A.R.S. § 40-301, and (ii)
5 exempting from APS' debt limits certain agreements that did not constitute traditional indebtedness,
6 but which could be treated as debt by generally accepted accounting principles ("GAAP"), like
7 power-purchase agreements and long term fuel supply contracts.⁷ The Commission denied APS'
8 request to exempt a vehicle lease and trailer rental agreement from its debt limits.⁸ The Commission
9 retained the flexibility to determine what constitutes evidence of indebtedness, and retained
10 regulatory control to avoid the unintended consequences of providing a given utility with a
11 "mechanism for circumventing such regulatory controls."⁹

12 **III. THE COMMISSION IS NOT PRE-EMPTED FROM REVIEW OF THIS**
13 **TRANSACTION.**

14 The Company also asserts that the Commission is preempted from review and approval of the
15 Agreement. The Company argues that, under the doctrine of implied preemption, the Commission is
16 precluded from reviewing the underlying financial transaction that is the subject of the Agreement.
17 The Company did not make this argument in its application, but now raises the argument for the first
18 time.

19 **A. Background of Preemption.**

20 The Supremacy Clause of the United States Constitution states:

21 "Constitution, and the Laws of the United States... shall be the
22 Supreme Law of the Land; and the Judges in every State shall be bound
23 thereby, any Thing in the Constitution or Laws of any State to the
24 contrary notwithstanding."¹⁰

27 ⁷ Decision No. 69947 at 10-11.

⁸ *Id.* at 11

28 ⁹ See Staff Report at 5, Docket No. E-01345A-06-0779.

¹⁰ U.S. Const. art. 6, cl. 2.

1 Thus, when the federal government is exercising any of the powers enumerated in the
2 Constitution, federal law or action must prevail over any conflicting or inconsistent state exercise of
3 power.

4 Congress may displace, or preempt, state law whenever it intends to and whenever it is acting
5 within the scope of its constitutionally enumerated powers. There are three types of preemption:

- 6 1. Express Preemption: Congress has clearly declared its intent to preempt state
7 law.
- 8 2. Conflict Preemption: occurs when courts determine that there is an *actual*
9 *conflict* between state and federal law. An *actual conflict* is defined as a
10 circumstance where it is impossible to comply with both federal and state law
11 or where the state law stands as an obstacle to the execution of the full
12 purposes and objectives of Congress.
- 13 3. Field Preemption: Field preemption occurs when courts determine that
14 Congress impliedly intended to "occupy the field" so fully that it "left no room
15 for the States to supplement it." This intent can be found in three ways:
 - 16 • Pervasive federal regulation—Where the federal regulatory scheme
17 consists of multiple and comprehensive laws governing virtually
18 every activity within a given field, courts are likely to find field
preemption.
 - Dominant federal interest—The Act of Congress may touch a field
in which federal interest is so dominant that the federal system will
be assumed to preclude enforcement of state laws on the same
subject.
 - "Object and Character"—When the object sought to be obtained by
federal law and the character of obligations imposed by it may
reveal a congressional intent fully to occupy the field.

19 The Company's arguments that the Commission is preempted from action are without merit.

20 **B. There Is No Conflict Preemption.**

21 The Company argues that conflict preemption would result if the Commission were to reject
22 the Agreement, impose conditions that would make it impossible for CWCGV to comply with state
23 and federal law, or impede the full purposes of Congress. Staff cannot envision what type of
24 conditions would be imposed that would make it impossible for CWCGV to comply with federal or
25 state law. Staff would find it hard to believe that the Commission, in the exercise of its constitutional
26 and statutory authority, would impose conditions in contravention of state or federal law. Because
27 there is no state or federal requirement that mandates CWCGV to take a CAP allocation, there is no
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1 conflict between the purposes of A.R.S. § 40-301 and the myriad of laws governing the Colorado
2 River. The Company's arguments are not persuasive and should be rejected.

3 In the unlikely event that the Commission were to impose a condition that would make it
4 impossible for CWCGV to comply with federal law, the recourse would be an action in a court of
5 competent jurisdiction to determine whether the state law in this matter, A.R.S. 40-301, conflicts
6 with the federal law concerning the Colorado River. Absent such an occurrence, the issue of whether
7 conflict preemption exists is not ripe for determination at an administrative level and does not require
8 a complete abdication of Commission jurisdiction.

9 **C. There Is No Field Preemption.**

10 There is no dispute that the Agreement stems from federal law authorizing the Company to
11 receive its additional allocation. Staff acknowledges that the Agreement is based on federal law of the
12 Colorado River. But the "field" at issue in this matter is the regulation of certain financial
13 transactions of public service corporations, not the regulation of the Colorado River. The genesis of
14 the Agreement in no way impacts the ability of the Commission to decide if the Company has the
15 financial wherewithal to meet the debt obligations in the Agreement and sustain its public service to
16 its customers. Staff's recommendation in this matter in no way changes a term or condition of the
17 Agreement. Staff's review was to determine if the Company had sufficient debt service coverage
18 ("DSC"). In fact, because of the rates approved for CWCGV in Decision No. 71478 (February 3,
19 2010), the Company has a DSC ratio that is more than sufficient for the Company to meet its
20 obligations with cash generated from operations.¹¹

21 The Commission has been supportive of water utilities in pursuing CAP allocations. In *Avra*
22 *Water Co-op*, the Commission authorized a surcharge to allow Avra to build the necessary treatment
23 facilities for its CAP allocation.¹² The Commission also structured rates to allow Avra sufficient
24 operating income to pay for its allocation.

25 The adoption of Staff's recommendations would not result in any of the dire consequences
26 listed in the Company's response. Staff has not recommended that the Commission take any action

27 _____
28 ¹¹ Staff determined that the DSC ration is 3.10. A DSC greater than 1.0 indicates that operating cash flow is sufficient to cover debt obligations.

¹² Docket No. W-02126A-06-0234, Tr at 32-34.

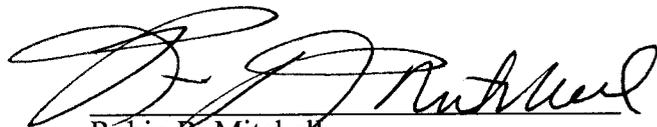
1 that would prevent CWCGV from complying with any term or condition of its agreement with
2 CAWCD. The Company seems to imply that the Commission's only recourse is to ignore the impact
3 of debt on a public services corporation's capital structure and would require the Commission to
4 ignore its constitutional and statutory authority to act to ensure the financial health of the utilities its
5 regulates and thus protect the public interest.

6 While CAP allocations are desirable and for some water utilities necessary, the adequacy of
7 the water supply for CWCGV to serve its customers was not an issue in the Company's last rate
8 case.¹³ In that case, Company witness Arturo Gabaldon testified that CWCGV has been planning to
9 use its allocation for almost a decade, but has yet to use any of its allocation until it develops a means
10 to bring in the CAP water from the source.¹⁴

11 **IV. CONCLUSION.**

12 Staff is puzzled at the Company's stance in this matter. Staff has recommended approval and
13 has not recommended any additional conditions. Staff would urge the Commission to reject the
14 Company's arguments and adopt Staff's recommendation as outlined in its Staff Report.

15 RESPECTFULLY SUBMITTED this 10th day of September, 2010.

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25 Original and thirteen (13) copies
26 of the foregoing were filed this
27 10th day of September, 2010 with:

28 Docket Control
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1200 West Washington Street
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¹³ See Docket No. W-02304A-08-0590.

¹⁴ Docket No. W-02304A-08-0590, Tr. at 57-58.

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