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BEFORE THE ARIZONA CORPORATION COMMISSION

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Docket No. W-00000C-06-0149

IN THE MATTER OF THE COMMISSION'S
GENERIC EVALUATION OF THE REGULATORY
IMPACTS FROM THE USE OF NON-
TRADITIONAL FINANCING ARRANGEMENTS
BY WATER UTILITIES AND THEIR AFFILIATES.

**RESIDENTIAL UTILITY CONSUMER OFFICE'S
COMMENTS**

The Residential Utility Consumer Office ("RUCO") RUCO submits these comments for review and discussion by the Commission and all interested parties regarding the appropriate accounting treatment of Infrastructure Coordination and Financing Agreements ("ICFAs").

OVERVIEW

In the recent *Global Utilities* rate application, over the strong objection of the utility, the Commission held that ICFAs constitute non-investor supplied capital and must be booked as CIAC. Decision No. 71878 described ICFAs as follows:

"ICFAs formalize the cooperation between the landowner and Global, but also provide fees which allow Global Parent to impress conservation and consolidation into the regional planning initiatives. These fees are intended to recover a portion of the carrying costs for the very expensive facilities required to implement effective water conservation and, in some cases, to fund Global Parent's acquisition of existing utilities." (Order at p. 12)

1 The Commission noted that the goals of total water management and acquisition of
2 struggling water companies are "laudable". RUCO wholeheartedly agrees. Yet, RUCO also
3 agrees with Staff's position that these goals can be achieved through other means, including
4 traditional ratemaking mechanisms. (Id. at p. 16).

5 Historically, non-investor supplied funds came from main line extension agreements or
6 from hook up fees. Third party developers provided funds to utilities for the purpose of
7 receiving water utility service. Those funds were properly booked as CIAC or AIAC and
8 treated as a deduction from rate base.

9 Now, the Commission is being asked to consider ICFAs as a brand new form of third
10 party cash that deserves different accounting treatment. The claim is that ICFA funds are not
11 being used for normal rate base assets but are for more lofty and conceptual (but no less
12 important) goals of water conservation, healthy water utility management and operations and
13 the acquisition of troubled water companies.

14 **SUMMARY**

15 RUCO remains suspicious that any developer would provide funds for purposes other
16 than the ultimate goal of providing plant to service their development. As the Commission
17 recognized in its Decision, "Staff submits that it does not seem reasonable to assume that
18 developers paid Global Parent millions of dollars, not for plant, but as a sort of donation to
19 insure that the Global Parent members receive a return on non rate-based plant and amounts
20 sufficient to pay taxes on the return." (p. 17)

21 RUCO was not persuaded by the utility's claim that if the Commission does not treat
22 ICFAs as revenue there will be no effort toward "total water management" or to acquire small
23 water companies. (Id. at 13,15) RUCO believes that the Commission and its Staff should not
24 be bullied by such thinly veiled threats. Furthermore, RUCO believes that in addition to

1 traditional ratemaking mechanisms, there are other options available for the Commission to
2 incent the industry to acquire troubled water companies.

3 RUCO is interested in hearing more from the industry during these workshops regarding
4 the specific details of its proposal to segregate and separately account for ICFA funds as well
5 as the possible uses for these monies that would then, in turn, be treated as revenues for
6 ratemaking purposes. RUCO will participate in these workshops with an open mind to
7 consider what the industry proposes.

8 **FUNGIBLE NATURE OF CASH / SEGREGATION OF ICFA FUNDS**

9 A primary obstacle for the Commission in Decision no. 71878 was that utility's parent
10 commingled monies obtained through ICFAs with other monies. The ALJ made it clear that
11 there was no easily traceable trail confirming the utility's claim that the ICFA funds were not
12 used for plant. At Open Meeting, there was much discussion whether maintaining segregated
13 accounts for ICFA funds and providing detailed accounting for the use of the ICFA monies
14 would provide sufficient transparency and allow the Commission, Staff, RUCO and other
15 interested parties the ability to "follow the money."

16 If the Commission finds that the fungible nature of cash is a fact that simply cannot be
17 overridden, then ICFAs cannot be given rate base treatment even if the funds are segregated
18 and separately accounted. Thus, since cash is fungible, the utility can re-direct the ICFA funds
19 to non-rate base expenses in order to free up investor supplied capital for plant.

20 The fungible nature of cash is a concern that should not be easily dismissed. At stake
21 is allowing utilities to earn a rate of return on investments that were made possible because a
22 third party, not the utility, provided funds for other utility expenses. A regulator provides a
23 reasonable rate of return to a utility because the utility took the risk of using its own funds. But
24 with ICFAs, that risk is mitigated if not eliminated.

1 The concern of the fungible nature of ICFA revenues can only be resolved if the
2 Commission is able to find that the ICFA funds are sufficiently attenuated from the investor-
3 supplied funds. If so, then, *at a minimum*, a utility must completely segregate monies
4 received by ICFAs and provide documentation regarding the use of those monies.

5 **QUESTIONS POSED FOR THE WORKSHOP**

6 **1. Whether ICFAs or other mechanisms, if properly segregated and accounted**
7 **for, could be utilized to finance the actual acquisition of troubled water**
8 **companies.**

8 RUCO has testified in several rate cases that all residents of Arizona deserve safe,
9 clean and reliable drinking water.¹ Yet, many Arizonans receive their water service from
10 troubled water companies that are out of compliance with ADEQ and/or Commission
11 standards. RUCO maintains that it is in the public interest for financially healthy and efficiently
12 operated water companies to acquire troubled and struggling companies.

13 RUCO is interested in reviewing the industry's proposal how ICFAs could encourage the
14 acquisition of these companies. RUCO expects the industry to provide a detailed road map on
15 how these funds would be used and why this is a preferred method of acquisition over other
16 mechanisms.

17 **2. Whether ICFAs, if properly segregated and accounted for, would be**
18 **appropriate for use in covering such expenses as a portion of the carrying**
19 **costs associated with unused regional water and wastewater facilities or**
20 **infrastructure.**

20 In Decision No. 71878 Global noted that "if ICFA fees are treated as CIAC as
21 recommended by RUCO and Staff, Global Parent will be unable to continue its commitment to
22 total water management, which entails significant carrying costs." (Id. at 13)

23 _____
24 ¹ Arizona Water, Docket No. W-014457A-08-0440; Bella Vista, Docket No. W-02465A-09-0411, Arizona-
American, Docket W-01303A-09-0343 No. Rate Consolidation Testimony of Jodi Jerich.

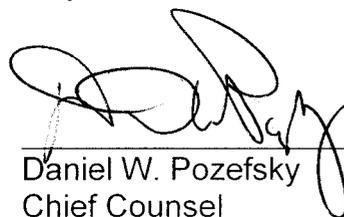
1 A utility incurs carrying costs when it provides investor-supplied capital or issues debt to
2 pay for infrastructure. Carrying costs accrue between the time the utility makes the investment
3 until it can recover its investment through a Commission-authorized increase in rates.
4 However, if a third party is providing the funds for the infrastructure, **then the utility has no**
5 **carrying costs.**

6 RUCO is interested in participating in the workshops to gain a better understanding of
7 the industry's claim that treating ICFA fees as CIAC will hinder its ability to meet total water
8 management goals due to significant carrying costs.

9 **3. Whether other mechanisms not addressed in the Global case would be**
10 **appropriate in inducing such regional water and wastewater infrastructure,**
11 **and the acquisition of troubled water companies, such as acquisition**
12 **adjustments, rate premiums, or Distribution System Investment Changes.**

13 RUCO finds that other mechanisms can provide appropriate rate relief for companies to
14 provide state of the art infrastructure as well as incentives to acquire troubled water
15 companies. This workshop is an appropriate forum to review the 2001 Staff Memorandum
16 regarding the recovery of acquisition costs for small water companies through (1) acquisition
17 premiums or (2) rate of return adjustments. Additionally, this workshop can continue the
18 discussion from the Arizona Water, Bella Vista and Arizona-American rate cases on how rate
19 consolidation can provide an incentive to acquire water companies. Finally, at the Open
20 Meeting where the Commission debated *Global Utilities*, there was discussion whether a
21 company should seek pre-approval for the accounting treatment of ICFA funds. This is also
22 another possible solution that could be discussed in these workshops.

23 RESPECTFULLY SUBMITTED this 29th day of October, 2010.

24 
Daniel W. Pozefsky
Chief Counsel

1 AN ORIGINAL AND THIRTEEN COPIES
2 of the foregoing filed this 29th day of
3 October, 2010 with:

4 Docket Control
5 Arizona Corporation Commission
6 1200 West Washington
7 Phoenix, Arizona 85007

8 COPIES of the foregoing hand delivered/
9 mailed this 29th day of October, 2010 to:

10 Lyn Farmer, Chief
11 Administrative Law Judge
12 Hearing Division
13 Arizona Corporation Commission
14 1200 West Washington
15 Phoenix, Arizona 85007

16 Janice Alward, Chief Counsel
17 Charles Hains
18 Legal Division
19 Arizona Corporation Commission
20 1200 West Washington
21 Phoenix, Arizona 85007

22 Steven M. Olea, Director
23 Utilities Division
24 Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

Elijah Abinah
Utilities Division
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

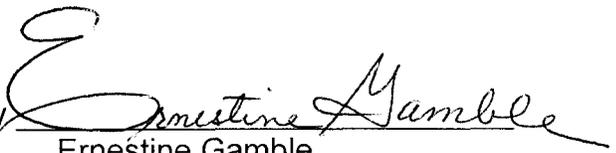
Nancy Scott
Arizona Corporation Commission
1200 West Washington
Phoenix, Arizona 85007

Thomas H. Campbell
Michael T. Hallam
Lewis and Roca LLP
40 North Central Avenue
Phoenix, AZ 85004

Thomas M. Broderick
Director, Rates & Regulation
American Water
2355 W. Pinnacle Peak Road, Suite 300
Phoenix, AZ 85027

Michelle Van Quathem
Ryley Carlock & Applewhite
One North Central, suite 1200
Phoenix, AZ 85004-4417

Graham Symmonds
21410 N. 19th Avenue, Suite 201
Phoenix, AZ 85027

By 
Ernestine Gamble
Secretary to Daniel Pozefsky