



1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

THE ARIZONA CORPORATION COMMISSION

RECEIVED

COMMISSIONERS

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

2010 DEC -9 P 3: 34

AZ CORP COMMISSION
DOCKET CONTROL

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS ANTHEM WATER DISTRICT AND ITS SUN CITY WATER DISTRICT.

DOCKET NO. W-01303A-09-0343

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS ANTHEM/ AGUA FRIA WASTEWATER DISTRICT, ITS SUN CITY WASTEWATER DISTRICT AND ITS SUN CITY WEST WASTEWATER DISTRICT.

DOCKET NO. SW-01303A-09-0343

EXCEPTIONS OF INTERVENER ANTHEM COMMUNITY COUNCIL
TO RECOMMENDED OPINION AND ORDER

Arizona Corporation Commission

DOCKETED

DEC 9 2010

DOCKETED BY

TABLE OF CONTENTS

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

PAGE

- I. SUMMARY OF RECOMMENDATIONS 1
- II. SUMMARY OF EXCEPTIONS 2
- III. DISCUSSION 3
 - A. Introduction 3
 - B. AAWC's 2007-2008 Refunds to Pulte Should Be Permanently Excluded from Rate Base and Denied Any Related Ratemaking Recognition 4
 - 1. The "Evidence of Indebtedness" Issue 4
 - 2. The A.A.C. R14-2-406 Issue 9
 - C. The Commission Should Establish "Just and Reasonable Rates and Charges" for Anthem Water and Wastewater Ratepayers in the Circumstances of the Instant Proceeding 13
 - D. The Commission Should Adopt a ROR Not to Exceed 6.37% 14
 - E. The Commission Should (i) Allocate a Smaller Portion of the Northwest Treatment Plant Cost to the Anthem/Agua Fria Wastewater District for Ratemaking Purposes and (ii) Order Deconsolidation of the Anthem/Agua Fria Wastewater District 16
 - 1. The Commission should reduce the portion of the Northwest Treatment Plant cost allocated to the Anthem/Agua Fria Wastewater District from 28% to 16.5% 16
 - 2. The Commission should order deconsolidation of the Anthem/Agua Fria Wastewater District. 17
 - F. The Commission Should Adopt the Stand-Alone Water and Wastewater Rate Design for Anthem Proposed by AAWC 17
- IV. CONCLUSION 19
 - Anthem Proposed Amendments No. 1 Attachment 1
 - Revised ROO Exhibit A, page vi Attachment 2

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

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 ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS ANTHEM WATER DISTRICT AND ITS SUN CITY WATER DISTRICT.

DOCKET NO. W-01303A-09-0343

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS ANTHEM/AGUA FRIA WASTEWATER DISTRICT, ITS SUN CITY WASTEWATER DISTRICT AND ITS SUN CITY WEST WASTEWATER DISTRICT.

DOCKET NO. SW-01303A-09-0343

EXCEPTIONS OF INTERVENER ANTHEM COMMUNITY COUNCIL TO RECOMMENDED OPINION AND ORDER

The Anthem Community Council, Inc. ("Anthem") hereby submits its Exceptions to the Recommended Opinion and Order ("ROO") issued November 30, 2010 by Administrative Law Judge Jibilian in the above-captioned and docketed proceedings ("instant proceeding").

I. SUMMARY OF RECOMMENDATIONS

For the reasons summarized in Section II below, and more fully discussed in Section III below, Anthem respectfully urges the Arizona Corporation Commission (the "Commission") to (i) reject all of the substantive recommendations applicable to the Anthem community set forth in the ROO, and (ii) instead issue an order providing for following:

- 1 (i) Permanent exclusion of all of Pulte Refund Payments (defined below) from
2 Arizona-American Water Company's ("AAWC" or the "Company") rate
3 base and denial of any related ratemaking recognition.
- 4 (ii) Adoption of a rate of return ("ROR") not to exceed 6.37%.
- 5 (iii) Reduction of the portion of the Northwest Treatment Plant cost to be
6 allocated to the Anthem/Agua Fria Wastewater District from 28% as
7 recommended in the ROO to 16.5%; and, in addition, prompt deconsolidation
8 of the Anthem/Agua Fria Wastewater District and the establishment of stand-
9 alone rates for each resulting district; and
- 10 (iv) Retention of AAWC's current fixed/commodity rate structures for the
11 Anthem Water District and the Anthem/Agua Fria Wastewater District, and
12 the application of any rate increases on an across-the-board basis within these
13 rate structures.

14 In the event that the Commission decides to adopt Anthem's recommendations, a form of
15 amendments to the ROO is attached as Attachment 1 hereto for the Commission's
16 convenience.

17 II. SUMMARY OF EXCEPTIONS

18 In the following Section III of these Exceptions, Anthem will discuss its following
19 objections to the ROO:

- 20 • The Infrastructure Agreement is "evidence of indebtedness" within
21 the plain meaning of Sections 40-301 *et seq.* of the Arizona Revised
22 Statutes which required Commission approval prior to its execution
23 and delivery. The requisite prior Commission approval was neither
24 sought nor obtained in this instance. As a result, the Infrastructure
25 Agreement and the Company's contractual obligation to pay the
26 Pulte Refund Payments thereunder are void as a matter of law.
- 27 • The Infrastructure Agreement is a main extension agreement within
28 the meaning of A.A.C. R14-2-406 which required Commission
approval. The Commission never approved the Infrastructure
Agreement. The Pulte Refund Payments were made pursuant to a
refund formula never approved by the Commission.
- Article 15, Section 3 of the Arizona Constitution authorizes and
requires the Commission to prescribe "just and reasonable rates and
charges." Anthem ratepayers are faced with the prospect of
substantial rate increases arising from the Pulte Refund Payments.

1 Recently discovered information suggests that the cost of Anthem
2 water and wastewater infrastructure funded through the
3 Infrastructure Agreement was previously included in the purchase
4 price(s) of homes in Anthem. The Commission should consider this
5 information incident to determining the Company's revenue
6 requirements.

- 7 • The adoption of an ROR not to exceed 6.37% results in a fair and
8 reasonable ROR, and mitigates, to some extent, the significant rate
9 increases otherwise to be experienced by Anthem residents.
- 10 • Staff customer growth projections for the Northeast Agua Fria area
11 adopted by the ROO result in a 41.98% customer count forecast
12 error with respect to the allocation of Northwest Treatment Plant
13 costs to Anthem/Agua Fria wastewater ratepayers. Anthem witness
14 Neidlinger's proposed cost allocation involves a forecast error of
15 only 1.68%.
- 16 • Logic does not support continued consolidation of two
17 geographically separate and unconnected wastewater districts into a
18 single Anthem/Agua Fria Wastewater District for ratemaking
19 purposes. Good public policy requires the Commission to correctly
20 assign cost responsibility to persons occasioning incurrence of such
21 costs. The current hypothesized consolidation fails to do so.
- 22 • The rate design concepts recommended in the ROO are based upon
23 inadequately studied Staff proposals, which would adversely affect
24 Anthem and Agua Fria wastewater customers. Such concepts and
25 results are also adversely discriminatory to Anthem vis-à-vis Sun
26 City wastewater ratepayers.

27 III. DISCUSSION

28 A. Introduction.

29 As they apply to ratepayers in the Anthem Water District and in the Anthem/Agua
30 Fria Wastewater District, the recommendations set forth in the ROO are unfair and
31 unreasonable. If the Commission adopts these recommendations without substantial
32 modification or mitigation, Anthem ratepayers will suffer significant financial harm. The
33 recommended increases to the revenue requirements will also allow the Company, a
34 wholly-owned subsidiary of the largest¹ investor-owned water and wastewater utility
35 company in the United States, to increase its gross revenues derived from service provided
36

37 ¹ As measured by both operating revenue and population served. In 2007, American Water Works Company, Inc.
38 ("American Water") generated approximately four times the operating revenue of the next largest investor-owned
company in the United States water and wastewater business. See American Water Works Company, Inc. Form 10-K
for the period ending December 31, 2008, Exh. Anthem-17 at 3.

1 in the Anthem Water District by 79.12% and its gross revenues derived from service
2 provided in the Anthem/Agua Fria Wastewater District by 58.25%. In each instance, these
3 revenue increases would be in addition to the double-digit increases to the Anthem Water
4 District revenue requirement and the Anthem/Agua Fria Wastewater District revenue
5 requirement that the Commission approved for the Company a little more than two years
6 prior to the Company's filing of its application for rate increases in the instant
7 proceeding.²

8 **B. AAWC's 2007-2008 Refunds to Pulte Should Be Permanently Excluded from**
9 **Rate Base and Denied Any Related Ratemaking Recognition.**

10 Two core issues are discussed below in connection with Anthem's request that the
11 Pulte Refund Payments should be permanently excluded from rate base and denied any
12 related ratemaking recognition. These issues are (i) the "evidence of indebtedness" issue,
13 and (ii) the "failure to comply with A.A.C. R14-2-406" issue.

14 1. The "Evidence of Indebtedness" Issue.

15 Sections 40-301 *et seq.* of the Arizona Revised Statutes ("A.R.S.") state that before
16 a public service corporation can issue stocks, stock certificates, bonds, notes and other
17 evidences of indebtedness that are payable more than 12 months from the date of issuance,
18 it must secure an order from the Commission authorizing the same. Any stock, stock
19 certificate, bond, note and other evidence of indebtedness issued without a prior valid order
20 of the Commission is void. The Infrastructure Agreement³ is a secured financing
21 agreement with repayment terms extending beyond one year, and therefore is "evidence of
22 indebtedness" within the plain meaning of the aforesaid statutory scheme. The
23 Commission did not issue an order authorizing the Infrastructure Agreement prior to its
24 execution and delivery. As a result, pursuant to A.R.S. § 40-303(A), the Infrastructure

25
26
27 ² See Arizona Corporation Commission Order 70372, Docket No. WS-01303A-06-0403 at 54.

28 ³ Infrastructure Agreement for the Villages At Desert Hills Water/Wastewater Infrastructure, dated September 29, 1997, between Citizens Water Resources ("Citizens"), as predecessor in interest to AAWC, and Del Webb Corporation ("Del Webb"), as predecessor in interest to Pulte Corporation ("Pulte"), as amended from time to time (the "Infrastructure Agreement").

1 Agreement is void as a matter of law. Similarly, AAWC's obligation to pay the June 29,
2 2007 \$3.1 and March 25, 2008 \$20.2 million refund payments (collectively, the "Pulte
3 Refund Payments") to Pulte pursuant to the Infrastructure Agreement was void from the
4 outset, or "*ab initio*." Therefore, the Commission should permanently exclude the Pulte
5 Refund Payments from AAWC's rate base and deny any associated ratemaking recognition
6 of the Pulte Refund Payments.

7 In connection with the foregoing, and importantly, A.R.S. §§ 40-301 *et seq.*, does
8 not contain any provision (i) exempting "private agreements," (ii) waiving the prior
9 approval requirement where a public utility has previously tried but failed to obtain the
10 required approval, (iii) allowing the Commission to ignore the application of the law if it
11 would be unfair to the public service corporation in question, or (iv) allowing the
12 Commission to ignore the law if following it would be administratively burdensome⁴ for
13 the Commission. Nevertheless, all of these excuses have been advanced in these
14 proceedings as justifications for disregarding the law.⁵ Rather, the correct legal analysis on
15 this issue in this instance entails the resolution of two questions: (1) Is the Infrastructure
16 Agreement "evidence of indebtedness"? (2) If so, did the Commission issue an order
17 approving the Infrastructure Agreement prior to its execution and delivery?

18 a. *The Infrastructure Agreement is "evidence of indebtedness."*⁶

19 With respect to the first question, the ROO relies upon two lines of arguments to
20 support its conclusion that the Infrastructure Agreement is not "evidence of indebtedness."
21

22 ⁴ In that regard, Staff and the Company have argued that adopting Anthem's interpretation of A.R.S. §§ 40-301 *et*
23 *seq.*, would result in "nearly every existing main extension and line extension agreement in the State of Arizona"
24 becoming invalid and that the Commission would be inundated with agreements that could potentially qualify as
25 "other evidence of indebtedness." However, all existing main extensions which have been reviewed and approved by
26 the Commission under A.A.C. R14-2-406 have satisfied the prior approval requirement of A.R.S. §§ 40-301 *et seq.*
Further, the Commission's determination in Decision No. 69947 that contracts classified as "debt" under generally
27 accepted accounting principals are subject to A.R.S. §§ 40-301 *et seq.* means that many routine contractual
28 arrangements which might not be characterized as "traditional" forms of indebtedness are already subject to
Commission review. See Decision No. 69947, Docket No. E-01345A-06-0779 at 11.

⁵ See ROO at 25-35.

⁶ As additional support for Anthem's positions set forth in this Section II(B)(1)(a), Anthem incorporates herein by
reference its April 16, 2010 Pre-hearing Memorandum on Disputed Refund Payment Issue, Section II(B) of its July 16,
2010 Initial Post-Hearing Brief, and Section II(A) of its August 6, 2010 Post-Hearing Response Brief.

1 The first is that because the Infrastructure Agreement “is not a stock or bond, but an
2 agreement that provides terms and conditions of service, as well as refund obligations, it is
3 not evidence of indebtedness.” This narrow interpretation of “evidence of indebtedness” is
4 supported neither by the Commission’s prior interpretation nor by the public interest.
5 Specifically, in Decision No. 69947, the Commission (i) expressly declined to confine
6 “evidence of indebtedness” to traditional indebtedness for borrowed money, and
7 (ii) recognized that non-traditional indebtedness is also subject to the controls set forth in
8 A.R.S. §§ 40-301 *et seq.*⁷ In fact, in the proceeding which resulted in Decision No. 69947,
9 Arizona Public Service Company (“APS”) had requested that a vehicle lease and a trailer
10 rental agreement be excluded from the statutory regime set forth in A.R.S. §§ 40-301 *et*
11 *seq.*⁸ The Commission denied APS’ request even though the parties to such agreements,
12 like the Infrastructure Agreement, involved only a regulated entity and non-regulated
13 entities (*i.e.*, “private agreements”) and the agreements did not include the issuance of
14 stocks or bonds. By recognizing that the term “evidence of indebtedness” includes non-
15 traditional forms of indebtedness, the Commission retains full regulatory control over
16 public service corporations and avoids the unintended consequence of providing a given
17 utility with “a mechanism for circumventing these controls.”⁹

18 Further, A.R.S. § 40-301(A) expressly states that the power of public service
19 corporations to issue stocks, bonds, notes and other evidences of indebtedness is:

20 “a special privilege, the right of supervision, restriction and control of
21 which is vested in the state, and such power shall be exercised as provided
22 by law and under rules, regulations and orders of the commission.”
23 (Emphasis added).
24
25

26 ⁷ Commission Decision No. 69947, Docket No. E-01345A-06-0779 at 2, 12 (stating “the purpose of long-term debt
27 limits would be frustrated if [a public service corporation] could structure the form of its debt to avoid those limits.”).
28 See also Anthem’s Post-Hearing Reply Brief at 3-4 for a discussion of various financing mechanisms deliberately
employed to avoid traditional debt limitations.

⁸ *Id.* at 27; Staff Report, Docket No. E-01345A-06-0779 at 3.

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

1 Against this statutory backdrop, Anthem submits that it is disingenuous and indefensible to
2 argue or conclude that a secured private financing arrangement on the order of
3 \$100,000,000,¹⁰ with concomitant future ratemaking consequences for a public service
4 corporation party thereto, should not be subject to the Commission's "supervision" and
5 "control." Yet, in this instance, the ROO has accepted that argument and reached that
6 conclusion with respect to the Infrastructure Agreement.

7 The second argument set forth in the ROO to support the conclusion that the
8 Infrastructure Agreement is not "evidence of indebtedness" is that the Infrastructure
9 Agreement "was not designed for the purpose of building up the utility's general and
10 permanent capital structure like an issuance of stock, but rather serves the specific and
11 limited purpose of placing the risks of development on the developer rather than the public
12 utility." However, vehicle leases and trailer rental agreements are not intended to build up
13 a public service corporation's permanent capital structure, yet in Decision No. 69947 the
14 Commission declined to exclude them from the scope of A.R.S. §§ 40-301 *et seq.*'s
15 requirements. Moreover, stocks, bonds, notes and other indebtedness do not merely serve
16 to build up a capital structure in some sort of passive sense. To the contrary, each of these
17 instruments is a financing mechanism, the proceeds of which are used for various corporate
18 purposes, including acquiring or constructing capital improvements. Likewise, the
19 Infrastructure Agreement is a financing mechanism which was used to acquire and
20 construct capital improvements.¹¹

21 In this instance, Pulte essentially made an interest-free loan to AAWC and AAWC
22 provided letters of credit to Pulte as security for its loan repayment obligations. It was not
23 entered into for "the specific and limited purpose of placing the risks of development on the
24 developer," as the ROO concludes. Significantly, in that regard, the original parties to the
25 Infrastructure Agreement intended it to be, among other things, a financing agreement

27 ¹⁰ The estimated cost of the facilities constructed pursuant to the Infrastructure Agreement is \$110.5 million and
28 AAWC's reimbursement obligations are estimated to be \$89 million. See Pulte's Response to RUCO's Questions
docketed in Docket No. WS-01303A-06-0403 on August 17, 2007 at 4-5.

¹¹ For a further discussion, see Anthem Post-Hearing Reply Brief at 4-5.

1 requiring Commission approval. For example, "A Proposal for The Villages at Desert Hills
2 Water/Wastewater Infrastructure," submitted by Citizens and Black & Veach to Del Webb
3 on February 28, 1997 as a precursor to the Infrastructure Agreement, contemplates three
4 scenarios for financing and constructing the infrastructure. Each of these scenarios
5 describes the financing arrangements as loans and contemplates repayment to Del Webb
6 through refunds.¹² Additionally, in response to a data request in AAWC's prior rate case
7 proceedings, Pulte's counsel characterized AAWC's refund payments as "debt repayment
8 obligations" and "debt under the agreement."¹³

9 Given the above considerations, the analysis and conclusion set forth in the ROO
10 that the Infrastructure Agreement is not "evidence of indebtedness" under A.R.S. §§
11 40-301 *et seq.* are simply erroneous. Accordingly, the Commission should instead
12 conclude that the Infrastructure Agreement is "evidence of indebtedness" within the
13 meaning of A.R.S. §§ 40-301 *et seq.*, which requires prior Commission approval. In doing
14 so, the Commission will avoid the surely unintended consequence of public utility
15 customers being saddled with exorbitant rate increases originating from an allegedly
16 "private agreement," where the parties thereto had no public accountability and unfettered
17 discretion to negotiate self-serving terms to the substantial detriment of unprotected third-
18 party ratepayers. If nothing else, the instant proceeding demonstrates the importance of the

19 _____
20 ¹² See Pulte's Response to RUCO's Questions docketed in Docket No. WS-01303A-06-0403 on August 17, 2007 at
Attach 1 at 2-4.

21 ¹³ The following is an excerpt of RUCO's data request and Pulte's response to RUCO's Data Request 1.1 docketed in
22 Docket No. WS-01303A-06-0403 on August 17, 2007: "With regard to the letter of Ben Dutton, Director of Planning
23 and Development, dated October 30, 2006 to Ernest G. Johnson, reference the following statements on page 3, last
24 paragraph: "RWE, American Water Works Company and AAWC presumably took those obligations into account in
determining the purchase price and forming their future business plans years ago." "Satisfaction of the infrastructure
reimbursement obligations is the responsibility of RWE, American Water Works Company and AAWC, not AAWC's
Anthem customers or Pulte/Del Webb's shareholders." Please explain the basis for each statement.

Response: 1.1 (a). Pulte has no knowledge regarding what matters Arizona-American or its affiliates took into
25 account in making a purchase price decision. Mr. Dutton's statements in the October 30, 2006 letter to Ernest Johnson
26 reflect his personal opinions generally, that a company acquiring the business operations or assets of another company
27 takes existing contractual obligations of the company to be acquired into account in reaching business decisions - in
other words, that a company plans ahead with respect to future debt repayment obligations. Mr. Dutton felt that
Arizona-American was unfairly asking Pulte at this late date to renegotiate a contract that Arizona-American assumed,
and that has been in place for years. In the letter, Mr. Dutton confirmed his belief that Arizona-American is
28 responsible to Pulte for the debt under the agreement, and Mr. Dutton expressed his belief that Arizona-American's
parent company should take action to ensure that repayment occurs. (Emphasis added).

1 oversight and prior approval authority granted to the Commission by A.R.S. §§ 40-301 *et*
2 *seq.*

3 b. *The Infrastructure Agreement did not receive prior Commission approval.*

4 There is no dispute that the Infrastructure Agreement was not approved by an order
5 of the Commission prior to its execution as required by A.R.S. §§ 40-301 *et seq.* In fact,
6 the original parties to the Infrastructure Agreement did not seek approval of the
7 Infrastructure Agreement until after the Infrastructure Agreement purportedly took effect.¹⁴
8 As a result, A.R.S. § 40-303(A) mandates that the Infrastructure Agreement is void as a
9 matter of law. As discussed in Section II(A)(3) in Anthem's August 6, 2010 Post-Hearing
10 Reply Brief, retroactive efforts by the Company and its predecessors in interest to have the
11 Infrastructure Agreement approved by the Commission are legally irrelevant because
12 (i) Commission approval prior to the effective date of the Infrastructure Agreement, as
13 explicitly required by A.R.S. §§ 40-301 *et seq.*, was neither sought nor obtained, and
14 (ii) Arizona statutory and case law do not permit retroactive regulatory approval.¹⁵
15 Similarly, because lack of prior Commission approval made the Infrastructure Agreement
16 void from inception, any claim of unfairness to AAWC due its reliance on the
17 Commission's repeated refusal to approve the Infrastructure Agreement during or
18 subsequent to 1997 is without merit.

19 2. The A.A.C. R14-2-406 Issue.

20 A.A.C. R14-2-406(A) provides that:

21 A. Each utility entering into a main extension agreement
22 shall comply with the provisions of this rule which
23 specifically defines the conditions governing main
24 extensions. (Emphasis added.)

25 In that regard, A.A.C. R14-2-406(B)(1) indicates that the concept of "main extensions"
26 within the context of this regulation includes substantially more than main extensions:

27 ¹⁴ The Infrastructure Agreement is dated as of September 29, 1997. On October 29, 1997 Citizens filed an
28 application requesting a CC&N and generally requesting Commission approval of the Infrastructure Agreement.

¹⁵ See Anthem's August 6, 2010 Post-Hearing Reply Brief at 5-6.

1 B. An applicant for the extension of mains may be required
2 to pay to the Company, as a refundable advance in aid of
3 construction, before construction is commenced, the
4 estimated reasonable cost of all mains, including all valves
5 and fittings.

6 1. In the event that additional facilities are required
7 to provide pressure, storage or water supply,
8 exclusively for the new service or services
9 requested, and the cost of the additional facilities is
10 disproportionate to anticipated revenues to be
11 derived from future consumers using these
12 facilities, the estimated reasonable cost of such
13 additional facilities may be included in refundable
14 advances in aid of construction to be paid to the
15 Company. (Emphasis added.)

16 Finally, and as one of the compliance provisions referenced within the above-quoted
17 subsection (A), A.A.C. R14-2-406(M) provides that: "All agreements under the rule shall
18 be filed with and approved by the Utilities Division of the Commission." Against this
19 regulatory backdrop, it is unequivocally clear that the Infrastructure Agreement at issue in
20 the instant proceeding is a main extension agreement which is subject to the requirements
21 of A.A.C. R14-2-406, including approval by the Commission's Utilities Division. In that
22 regard, a significant portion of the funds advanced by Pulte (and its predecessor in interest)
23 to AAWC (and its predecessor in interest) were advanced for the purpose of constructing
24 facilities that were "required to provide pressure, storage or water supply, exclusively for
25 the new service or services requested" for the Anthem master-planned community.

26 Equally clear is the fact that neither Citizens nor AAWC ever expressly requested
27 that the Commission's Utilities Division approve the Infrastructure Agreement pursuant to
28 A.A.C. R14-2-406. Nor, did either company obtain the Commission's approval of the
Infrastructure Agreement at any time under any circumstances. As a consequence, the
Pulte Refund Payments were made without the requisite Commission approval; and, as a
consequence, water and wastewater utility plant funded with advances which occasioned
those refunds should not be included in AAWC's rate base and accorded ratemaking
recognition.

1 The ROO observes that the aforesaid water and wastewater facilities are “used and
2 useful.” That may be the case. However, that fact does not legally excuse the failure of
3 AAWC (and its predecessor in interest) to obtain that approval of the Infrastructure
4 Agreement expressly required by A.A.C. R14-2-406(A) and (M).

5 The ROO also notes that no party has questioned the reasonableness of the cost of
6 the water and wastewater facilities constructed with funds advanced by Pulte (and its
7 predecessor in interest). However, the reasonableness of the cost of facilities constructed
8 with such funds also does not legally excuse the failure of AAWC (and its predecessor in
9 interest) to obtain the prescribed Commission approval of the Infrastructure Agreement
10 pursuant to A.A.C. R14-2-406(A) and (M).¹⁶ Furthermore, the ROO appears to accept the
11 argument made by certain parties to the effect that the approval requirement of A.A.C.
12 R14-2-406(A) and (M) is not applicable to the Infrastructure Agreement because that
13 document is in the nature of a “private agreement.” Suffice it to say, and without intending
14 a “pun,” that rationale simply “does not hold water.” More specifically, most (if not all)
15 main extension agreements are between private parties (i.e., an applicant for service and a
16 public service corporation), and thus are by their very nature “private agreements.” Thus, a
17 logical extension of this line of reasoning would exempt most (if not all) proposed main
18 extension agreements from the requirements of that rule by which the Commission intends
19 that such agreements be regulated. Clearly, that was not the result contemplated by the
20 Commission when it promulgated A.A.C. R14-2-406.

21 Finally, the ROO appears to find comfort in the fact that AAWC has fully refunded
22 amounts previously advanced by Pulte (and its predecessor in interest) pursuant to the
23 Infrastructure Agreement.¹⁷ In that regard, A.A.C. R14-2-406(M) does provide in part that
24

25 ¹⁶ Or, for that matter, pursuant to A.R.S. §§ 40-301 *et seq.*

26 ¹⁷ Commission approval also was not obtained for a “waiver” or deviation from A.A.C. R14-2-606(C)(5) which
27 requires that all funds advanced for sewer and wastewater infrastructure which are not refunded within five (5) years
28 from the date of advance become contributions in-aid-of construction (“CIAC”). Because a portion of the advances
made by Del Webb were not refunded within five years and therefore should have been designated as CIAC, they are
not includable in rate base. For a further discussion of A.A.C. R14-2-606, see Anthem’s April 16, 2010 Pre-hearing
Memorandum on Disputed Refund Payment Issue at 23.

1 “Where agreements for main extensions are not filed and
2 approved by the Utilities Division, the refundable advance
3 shall be immediately due and payable to the person making
4 the advance.”

5 However, this perceived “remedy” does not in fact fully address and compensate for the
6 situation now before the Commission.

7 More specifically, the purpose of the approval requirement prescribed in A.A.C.
8 R14-2-406 is to provide the Commission with an opportunity to examine all aspects of a
9 proposed main extension agreement (including the proposed refund formula) in order that
10 the Commission may insure that all aspects of the proposed agreement are consistent with
11 the “public interest.” In that regard, the immediate refund “remedy” set forth in A.A.C.
12 R14-2-406(M) would appear to address the concerns of the person or entity providing the
13 advance-in-aid-of-construction in question. However, this perceived “remedy” does not in
14 any manner address those aspects of a proposed main extension agreement which could
15 adversely impact the ratepayers of the public service corporation in question at some future
16 date. That is precisely the situation now before the Commission, where AAWC is seeking
17 rate base inclusion and ratemaking recognition of refund payments made by the Company
18 pursuant to an Infrastructure Agreement (and refund formula) never approved by the
19 Commission.

20 In conclusion, and in the circumstances of the instant proceeding, the only effective
21 “remedy” (from the Anthem water and wastewater ratepayers perspective) for the failure of
22 AAWC (and its predecessor in interest) to obtain Commission approval of the
23 Infrastructure Agreement required by A.A.C. R14-2-406(A) and (M) is for the Commission
24 to deny AAWC’s request (and the ROO’s recommendation) for rate base inclusion and
25 ratemaking recognition of the Pulte Refund Payments. In doing so, and as previously noted
26 in Section III(B)(1)(a) above, the Commission can shield Anthem’s water and wastewater
27 ratepayers from being saddled with an exorbitant rate increase originating from an
28 allegedly “private agreement,” where the parties thereto had no public accountability and

1 had unfettered discretion to negotiate self-serving terms to the substantial future detriment
2 of unprotected third party ratepayers.

3 **C. The Commission Should Establish “Just and Reasonable Rates and Charges”**
4 **for Anthem Water and Wastewater Ratepayers in the Circumstances of the Instant**
5 **Proceeding.**

6 Article 15, Section 3 of the Arizona Constitution provides in pertinent part that:

7 The Corporation Commission shall have full power to, and shall
8 prescribe . . . just and reasonable rates and charges to be made
and collected, by public service corporations within the State for
service rendered therein. . . (Emphasis added.)

9 In that regard, Arizona judicial decisions have consistently held that the Commission
10 possesses wide discretion in connection with the exercise of its ratemaking jurisdiction and
11 authority, provided that the Commission discharges its responsibility under Article 15,
12 Section 14 of the Arizona Constitution to determine and consider “fair value.”

13 The failure of prior Commissions to address and resolve the question of whether the
14 Infrastructure Agreement (and the refund formula provided for therein) should have been
15 approved presents the current members of the Commission with a situation where Anthem
16 water and wastewater ratepayers are now faced with the prospect of substantial rate
17 increases arising from the Pulte Refund Payments pursuant to a refund formula, which the
18 Commission might not have approved had it addressed and resolved in 1997 or 2000 the
19 threshold question of whether the provisions of the Infrastructure Agreement (and the
20 associated refund formula) were in the “public interest.”

21 This situation is further compounded by recently discovered information in which
22 Del Webb, Pulte’s predecessor in interest, disclosed to the Arizona Department of Real
23 Estate (the “Department”) that the estimated costs of water and wastewater infrastructure
24 financed through advances in-aid-of construction were to be included in the purchase prices
25 of homes to be sold by Del Webb to Anthem residents, who thereafter became water and
26 wastewater ratepayers of AAWC.¹⁸ In that regard, on November 9, 2010, the Residential
27

28

¹⁸ Del Webb’s disclosure also undercuts AAWC’s accusation that Anthem ratepayers have enjoyed the benefits of the
777674

1 Utilities Consumer Office (“RUCO”) and Anthem jointly docketed in these proceedings a
2 “Notice of Supplemental Information,” which included a copy of documentation from the
3 Department’s files indicating Del Webb’s intent to include the costs of Anthem water and
4 wastewater infrastructure in the purchase prices of homes Del Webb was constructing in
5 Anthem.

6 Against the preceding background, and in connection with an exercise of its
7 judicially acknowledged broad discretion in setting rates and charges, the Commission
8 must determine what would constitute “just and reasonable rates and charges” for
9 Anthem’s water and wastewater ratepayers, given that they may have already absorbed the
10 cost of the infrastructure by which they are served through the home purchase price(s) they
11 paid. Clearly, in Anthem’s view, the rates and charges (and underlying associated revenue
12 requirement) which would result under the ROO’s recommendations are not “just and
13 reasonable” in relation to the circumstances of Anthem’s water and wastewater ratepayers.
14 To the contrary, they are inordinately high, and should be significantly reduced.

15 The determination of what constitutes “just and reasonable rates and charges”
16 necessarily entails a balancing of interests between the applicant public service corporation
17 and its ratepayers. In the event that the Commission should ultimately conclude (despite
18 Anthem’s arguments to the contrary) that it is appropriate to include the Pulte Refund
19 Payments in AAWC’s rate base, then Anthem requests that the Commission exercise its
20 broad ratemaking discretion as to AAWC’s overall revenue requirement incident to
21 determining what constitutes “just and reasonable rates and charges” for Anthem’s water
22 and wastewater ratepayers.

23 **D. The Commission Should Adopt a ROR Not To Exceed 6.37%.**

24 The determination of the cost of capital ultimately requires an exercise of subjective
25 judgment by the Commission as between competing cost of capital expert opinion
26 testimony. In its July 16, 2010 Closing Brief, RUCO’s revised computations suggest that a

27 _____
28 Anthem infrastructure without paying for the same.

1 6.37% ROR is reasonable and appropriate, based on American Capital's lower cost of
2 short-term debt, as reported in American Water's most recent 10-K filing with the SEC.¹⁹
3 Further, investment expert Steven Puhr's written public comment in the instant proceeding
4 demonstrates that a 5.23% ROR is also reasonable and appropriate, after factoring in the
5 same lower commercial paper cost and making additional adjustments to select a more
6 comparable, and therefore more appropriate, data set.²⁰ While theoretical battles regarding
7 return on equity are commonplace in rate cases, the reality in this instance is that American
8 Water is the sole shareholder of AAWC and AAWC's stock is not publicly sold.²¹
9 Accordingly, any claim by AAWC that a higher return on equity and, correspondingly, a
10 higher ROR is needed in order to attract independent equity capital does not account for the
11 real-world phenomena in this instance.

12 Accordingly, and based on the entire record in this proceeding, Anthem
13 recommends the adoption of a ROR not to exceed 6.37% for the Company, which in this
14 instance results in a fair and reasonable ROR for AAWC that (i) accounts for the
15 Company's capital requirement, and (ii) at the same time mitigates, to some extent, the
16 significant rate increases to be experienced by Anthem residents as a result of these
17 proceedings if the ROO is not otherwise substantially revised.

18
19
20

¹⁹ See RUCO's Closing Brief at 44-53.

²⁰ See Opinion and supporting materials filed by Stephen P. Puhr as public comment with the Commission's Docket Control on April 28, 2010 in the instant proceeding.

²¹ AAWC and American Water Capital Corp. ("American Capital"), American Water's captive financing entity, are wholly-owned subsidiaries of American Water. Therefore, 100% of the stock of both AAWC and American Capital is owned by American Water and neither AAWC nor American Capital issues stock to any other person or entity. All profit and loss resulting from the operations of both AAWC and American Capital ultimately flow to American Water.

In that regard, and contrary to the testimony of AAWC's chief executive in this proceeding that if all of the Pulte Refund Payments were not immediately included in rate base and accorded ratemaking recognition, then American Capital would no longer provide funding to AAWC, AAWC filed a financing application on November 18, 2010 requesting Commission approval of one or more unsecured debt issues by American Capital in the aggregate principal amount of \$50,000,000, the proceeds of which would be loaned to and used by AAWC. AAWC's financing application also notes that AAWC may have the opportunity to seek "low-cost or tax advantaged government programs" and that interest rates are "at or near historically low levels," which is to be contrasted with AAWC's prior hearing testimony that stand-alone debt would be very expensive for AAWC. See Cross-Examination of Paul G. Townsley, Phase I Tr. at 375:24-376-6, and see Financing Application Arizona-American Water Company filed in Docket No. WS-013031-10-0470 on November 18, 2010.

1 **E. The Commission Should (i) Allocate a Smaller Portion of the Northwest**
2 **Treatment Plant Cost to the Anthem/Agua Fria Wastewater District for Ratemaking**
3 **Purposes and (ii) Order Deconsolidation of the Anthem/Agua Fria Wastewater**
4 **District.**

5 1. The Commission should reduce the portion of the Northwest Treatment Plant
6 cost allocated to the Anthem/Agua Fria Wastewater District from 28% to 16.5%.

7 With the objective of demonstrating that the recommended customer growth
8 projections set forth in the ROO for the Northeast Agua Fria area are inaccurate and do not
9 reasonably reflect future growth, as contrasted with Anthem's projections during the
10 hearing, on December 1, 2010, counsel for Anthem requested counsel for AAWC to
11 provide the number of wastewater customers actually served by AAWC in the Northeast
12 Agua Fria area of the Anthem/Agua Fria Wastewater District as of October 2010. On
13 December 3, 2010, AAWC's counsel responded indicating that 2,975 wastewater
14 customers were served in the aforesaid Northeast Agua Fria area as of October 2010. Staff
15 projections adopted in the ROO, as the basis for the 28% allocation recommended in the
16 ROO, assume 4,224 customers in that area at the end of 2010.²² This projection by Staff
17 included 1,249 more customers than the actual October 2010 count, resulting in a forecast
18 error of 41.98%. The Commission should not rely on projections that have no reliable
19 foundation and result in an unreasonable forecasting error. On the other hand, Anthem
20 witness Dan Neidlinger's projected customer count of 3,025 at the end of 2010 is only 50
21 more customers than the actual count.²³ This is a forecast error of only 1.68%.
22 Accordingly, Mr. Neidlinger's 16.5% allocation factor, which is supported by a known and
23 measurable change, is significantly closer to reality and should be adopted by the
24 Commission in this case.²⁴

25
26
27 ²² Cross-Examination of Dorothy M. Hains, Phase I Tr. at 799:23-24.

²³ See Anthem's Post-Hearing Reply Brief at 14.

²⁴ In that regard, it may be appropriate to reclassify the remaining 11.5% Northwest Treatment Plant cost, which should not be allocated to the Anthem/Agua Fria Wastewater District, as plant held for future use instead of reallocating it to the Sun City West Wastewater District.

1 2. The Commission should order deconsolidation of the Anthem/Agua Fria
2 Wastewater District.

3 Absent a decision by the Commission in the instant proceeding to consolidate all
4 AAWC's water and wastewater districts in the State of Arizona for ratemaking purposes,
5 there is no reason for the continued consolidation of these two geographically remote
6 wastewater districts for ratemaking purposes. In that regard, and as discussed in Section
7 IV(C)(3) in Anthem's July 16, 2010 Initial Post-Hearing Brief, the deconsolidation of the
8 Anthem/Agua Fria Wastewater District for cost allocation and rate design purposes should
9 be implemented as part of any final Commission decision in the instant proceeding. Good
10 public policy requires the Commission to correctly assign cost responsibility for all
11 ratemaking components in as expeditious manner as possible, and deconsolidation would
12 be consistent with such action. To accomplish deconsolidation, Anthem requests the
13 Commission to (i) order a rate design for the Anthem/Agua Fria Wastewater District as a
14 consolidated district on an interim basis and (ii) order the docket in the instant proceeding
15 to remain open for the limited purpose of designing and implementing stand-alone revenue
16 requirements and rate designs for the Anthem Wastewater District and Agua Fria
17 Wastewater District,²⁵ respectively, as soon as possible. In any event, such implementation
18 should be well in advance of AAWC's next rate case involving Anthem and Agua Fria
19 wastewater ratepayers.

20 **F. The Commission Should Adopt the Stand-Alone Water and Wastewater Rate**
21 **Design for Anthem Proposed by AAWC.**

22 Anthem does not support the rate design concepts for Anthem water and wastewater
23 customers recommended in the ROO. They are based upon Staff proposals that have been
24 heavily criticized by both the Company and Anthem, and rightfully so. More specifically,
25
26

27
28 ²⁵ Any amount of the Northwest Treatment Plant costs allocated to the Anthem/Agua Fria Wastewater District at the
time new stand-alone rate designs are established should be absorbed by the resulting Agua Fria Wastewater District
because Anthem residents are not served by the Northwest Treatment Plant and Agua Fria residents are.

1 the rate design concepts adopted in the ROO lack adequate foundation or support and
2 would adversely affect Anthem customers.

3 With respect to the Anthem Water District, there is no justification for the major
4 departures from AAWC's existing rate design which have been proposed by Staff and
5 adopted in the ROO. The proposed rate structure is heavily weighted as to
6 disproportionately allocate cost to the larger residential and commercial ratepayers, thereby
7 necessarily creating large intra and inter meter-size cross subsidies. In that regard, water
8 cost of service studies were not presented in this case to support Staff's rate design.
9 Further, the proposed rate design could create significant revenue stability problems for
10 AAWC. The magnitude of the intra class subsidy problem is readily discernable
11 comparing the proposed tier rates for residential meters with current rates. Staff
12 recommends a rate reduction of \$0.04 for the first 2,000 gallons – from \$1.54 to \$1.50 per
13 thousand gallons. However, Staff's top two tiers of \$7.00 (9,001 to 21,000 gallons) and
14 \$8.535 (over 21,000 gallons), are 227% and 277% greater, respectively, than the current
15 top tier rate of \$3.08 per thousand gallons. Similar rate distortions are prevalent in the
16 proposed rate designs for commercial meters, which also provide for a \$5.455 per thousand
17 gallon increase (277%) in the top tier with reductions in tier break-points. When coupled
18 with increased wastewater charges, the continued operation of many small businesses in
19 Anthem could be jeopardized. The ROO appears to accept this prospect with an assumed
20 hope that large reductions in water will offset poor economic consequences. However,
21 because the results are so speculative, this hoped-for trade-off is poorly conceived and
22 should be rejected.

23 With respect to the Anthem/Agua Fria Wastewater District, the recommended rate
24 design (\$9.5966 per thousand gallons for average January through March water usage),²⁶
25 which bases a residential customer's wastewater bill solely on water usage, is again an
26

27 ²⁶ For clarity with respect to how wastewater rates will be determined, Anthem has prepared Attachment 2 which is
28 intended to replace the existing Exhibit A (Anthem/Agua Fria Wastewater) currently attached to the ROO.

1 untested experiment in conservation-oriented rate design. Anthem customers who are
2 currently obligated by CC&R requirements to maintain winter lawns would pay, depending
3 on the usage, a combined water and wastewater rate of \$16.60 to \$18.13 per thousand
4 gallons to grow grass! None of this turf irrigation water usage, of course, is ever processed
5 by the wastewater treatment plant, and thus does not impose any wastewater transportation
6 or treatment costs. Staff is testing its conservation policies only on Anthem residents who
7 already pay among the highest water and wastewater rates of any of the Company's
8 customers. In contrast, Sun City residential customers in this case will continue to pay
9 wastewater rates on a fixed monthly charge basis and will therefore fortunately be immune
10 from Staff's unfair and unjustified wastewater rate proposals for Anthem.

11 For the reasons set forth above, the Commission should retain the current
12 fixed/commodity rate structure of the Anthem Water District and the Anthem/Agua Fria
13 Wastewater District and any allowed rate increases should be applied on an across-the-
14 board basis. However, if the Commission determines to adopt the rate structure
15 recommended in the ROO, then Anthem respectfully requests that the Commission delay
16 implementation of the new rate structure for an appropriate period of time (e.g., one year)
17 in order to provide Anthem ratepayers with the opportunity to alter usage requirements
18 (e.g., the winter lawn requirements) and actual usage. Concurrently, the Company should
19 offer a dual metering program for those Anthem customers that wish or are required to
20 maintain winter lawns. This would provide for the ability to measure both outdoor water
21 usage and indoor usage; and, wastewater bills would be based on only indoor usage,
22 thereby avoiding the requirement to pay for water that does not enter the sewage system.

23 IV. CONCLUSION

24 For the reasons discussed above and based upon the record in the instant proceeding,
25 Anthem respectfully requests the Commission to modify the ROO to provide for the
26 following:

- 27 (i) The permanent exclusion from AAWC's rate base and denial of any related
28 ratemaking recognition of the Disputed Pulte Refund payments;

- 1 (ii) Adoption of a ROR not to exceed 6.37%;
- 2 (iii) A reduction in the portion of the Northwest Treatment Plant cost to be
- 3 allocated to the Anthem/Agua Fria Wastewater District from the
- 4 recommended 28% to 16.5%, and the deconsolidation of the Anthem/Agua
- 5 Fria Wastewater District and the establishment of stand-alone rates for each
- 6 resulting district; and
- 7 (iv) Retention of the current fixed/commodity rate structure of the Anthem Water
- 8 District and the Anthem/Agua Fria Wastewater District, and applying any
- 9 rate increases on an across-the-board basis; but, if the rate structures
- 10 recommended by the ROO in this regard are adopted, then a one-year delay
- 11 in implementation of such rate structures to permit Anthem residents and
- 12 businesses to make necessary adjustments.

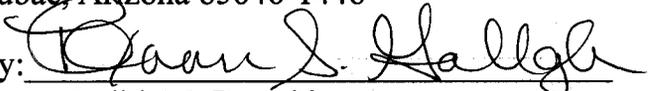
13 DATED this 9th day of December, 2010.

14 Respectfully submitted,

15 Judith M. Dworkin
16 Roxann S. Gallagher
17 Sacks Tierney PA
4250 North Drinkwater Blvd., 4th Floor
Scottsdale, Arizona 85251-3693

18 and

19 Lawrence V. Robertson, Jr.
20 P. O. Box 1448
Tubac, Arizona 85646-1448

21 By: 
22 Judith M. Dworkin
23 Roxann S. Gallagher
Attorneys for Anthem Community Council

24
25 ORIGINAL AND THIRTEEN (13) COPIES
of the foregoing filed this 9th day of December, 2010 to:

26 Docket Control
27 Arizona Corporation Commission
1200 W. Washington Street
28 Phoenix, AZ 85007

1 COPY of the foregoing mailed or e-mailed
2 this 9th day of December, 2010, to:

3 Teena Jibilian, Administrative Law Judge
4 Hearing Division
5 Arizona Corporation Commission
6 1200 W. Washington Street
7 Phoenix, AZ 85007

8 Thomas H. Campbell
9 TCampbell@LRLaw.com
10 Michael T. Hallam
11 MHallam@LRLaw.com
12 Lewis and Roca, LLP
13 40 N. Central Avenue
14 Phoenix, AZ 85004-4429

15 Daniel Pozefsky
16 DPozefsky@azruco.gov
17 RUCO
18 1110 W. Washington St., Suite 220
19 Phoenix, AZ 85007

20 Janice M. Alward, Chief Counsel
21 JAlward@azcc.gov
22 Legal Division
23 Arizona Corporation Commission
24 1200 W. Washington
25 Phoenix, AZ 85007-2927

26 Steve Olea, Director
27 SOlea@azcc.gov
28 Utilities Division
Arizona Corporation Commission
1200 W. Washington Street
Phoenix, AZ 85007

Lyn Farmer
Lfarmer@azcc.gov
Arizona Corporation Commission
1200 W. Washington Street
Phoenix, AZ 85007

Robert J. Metli
rmetli@swlaw.com
Jeffrey W. Crockett
jcrockett@swlaw.com
Snell & Wilmer LLP
400 E Van Buren
Phoenix, AZ 85004-2202
Attorneys for the Resorts

- 1 Michael Patten
mpatten@rdp-law.com
- 2 Roshka DeWulf & Patten PLC
400 E Van Buren Suite 800
- 3 Phoenix, AZ 85004-2262
- 4 Greg Patterson
gpatterson3@cox.net
- 5 916 W. Adams, Suite 3
Phoenix, AZ 85007
- 6 Attorneys for WUAA
- 7 W.R. Hansen
jpbillscwaz@aol.com
- 8 12302 W. Swallow Drive
Sun City West, AZ 85024
- 9
- 10 Bradley J. Herrema, Esq.
BHerrema@bhfs.com
- 11 Brownstein Hyatt Farber Schreck, LLP
21 E. Carrillo Street
Santa Barbara, CA 93101
- 12 Attorneys for Anthem Golf and Country Club
- 13 Norman D. James, Esq.
njames@fclaw.com
- 14 Fennemore Craig
3003 N. Central Avenue, Suite 2600
- 15 Phoenix, AZ 85012
Attorneys for DMB White Tank, LLC
- 16
- 17 Marshall Magruder, Esq.
mmagruder@earthlink.net
- 18 P.O. Box 1267
Tubac, AZ 85646-1267
- 19 Andrew M. Miller, Esq.
amiller@paradisevalleyaz.gov
- 20 Town Attorney
6401 E. Lincoln Drive
Paradise Valley, AZ 85253
- 21 Attorneys for Town of Paradise Valley
- 22
- 23 Joan S. Burke, Esq.
joan@jsburkelaw.com
- 24 Law Office of Joan S. Burke
1650 N. First Avenue
Phoenix, AZ 85003
- 25 Attorneys for Mashie, LLC, dba Corte Bella Golf Club
- 26 Larry D. Woods
15141 W. Horseman Lane
Sun City West, AZ 85375
- 27
- 28

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

Philip Cook
10122 W. Signal Butte Circle
Sun City, AZ 85373

Dan Neidlinger
Neidlinger & Associates, Ltd.
3020 N. 17th Drive
Phoenix, AZ 85012

Wendy Peterson

ATTACHMENT 1

ANTHEM PROPOSED AMENDMENTS NO. 1

TIME/DATE PREPARED: DECEMBER 9, 2010

COMPANY: Arizona-American Water Company

DOCKET NOS.: W-01303A-09-0343 and SW-01303A-09-0343

OPEN MEETING DATE: December 14, 2010

AGENDA ITEM NO.: 13

Page 19, Line 21 **INSERT** after "Staff's growth projections.":

"On December 3, 2010, the Company provided information to Anthem indicating that the Company served 2,975 wastewater customers in the Northeast Agua Fria area of the Anthem/Agua Fria Wastewater District as of October 2010.¹ Staff's projection of 4,224 wastewater customers, which provide the basis for its proposed 28% cost allocation, included 1,249 more customers than the actual October 2010 count, resulting in a forecast error of 41.98%. On the other hand, Mr. Neidlinger's projected customer count of 3,025 at the end of 2010 is only 50 more customers than the actual count. This is a forecast error of only 1.68%."

DELETE Page 20, Line 14 through 18:

AND REPLACE WITH:

"While the Commission agrees with Staff that projecting growth is not an exact science, Staff's projections result in an unreasonable forecasting error. Accordingly, Mr. Neidlinger's 16.5% allocation factor, which is supported by a known and measurable change, is significantly closer to reality and will be adopted by the Commission in this case."

MAKE CONFORMING CHANGES

Page 20, Line 22 **DELETE** "In 1997"

AND REPLACE WITH: "On September 29, 1997"

Page 25, Line 12 through Line 15 **DELETE:**

"Based on the fact that the Company did not obtain Commission approval pursuant to A.R.S. §§40-301 to 303 and A.A.C. R14-2-406, the Council requests that the Company's 2007 repayment of \$3,068,300.57 and 2008 repayment of \$20,2269,122 to Pulte for infrastructure costs pursuant to the Infrastructure Agreement be excluded from rate base and receive no ratemaking recognition."

¹ Anthem Exceptions at 16.

AND REPLACE WITH:

“Based on the fact that the Company did not obtain Commission approval required pursuant to A.R.S. §§40-301 to 303 and A.A.C. R14-2-406, the Council requests that the Company’s 2007 repayment of \$3,068,300.57 and 2008 repayment of \$20,2269,122 to Pulte for infrastructure costs pursuant to the Infrastructure Agreement (the “Pulte Refund Payments”) be excluded from rate base and receive no ratemaking recognition.”

DELETE Page 26, Line 18 through Line 23

AND REPLACE WITH:

“A.R.S. Section 40-301(B) states that before a public service corporation can issue stocks, stock certificates, bonds, notes and other evidences of indebtedness that are payable more than 12 months from the date of issuance, it must secure an order from the Commission authorizing the same. Any stock, stock certificate, bond, note and other evidence of indebtedness issued without a prior valid order of the Commission is void.² The Council alleges that the Infrastructure Agreement is a secured financing agreement with repayment terms extending beyond 12 months, and therefore is “evidence of indebtedness” within the plain meaning of A.R.S. §§ 40-301 *et seq.* There is no dispute that Pulte’s predecessor in interest neither sought nor received an order from the Commission authorizing the Infrastructure Agreement prior to its execution and delivery.³ The Council concludes, then, that pursuant to A.R.S. § 40-303(A), the Infrastructure Agreement is void as a matter of law. Similarly, the Company’s obligation to pay the Pulte Refund Payments under the Infrastructure Agreement was void from the outset, or “*ab initio.*” Therefore, the Council requests that the Commission permanently exclude the Pulte Refund Payments from the Company’s rate base and deny any associated ratemaking recognition of the Pulte Refund Payments.”

DELETE Page 27, Footnote 120

AND REPLACE WITH:

“Id. at 22, citing to In Re APS, Docket No. E-01345A-06-0779, Decision No. 69947 (October 30, 2007) at 10-13 (indicating that GAAP guides the determination as to whether an “evidence of indebtedness” exists), and at 11, fn 16 (“GAAP status is the determinant for compliance filings and how the condition test for issuance of debt or equity is calculated.”)”

Page 27, Line 17 through Page 28, Line **DELETE**:

“We disagree. The declaratory order APS sought in that case, and which the Commission declined to issue, would have allowed APS to exclude from treatment as debt two agreements which were classified as long-term debt per GAAP. Instead of issuing the requested declaratory order, Decision No. 69947 set out guidelines for the Company to follow in the event of changes in GAAP or changes in interpretation of GAAP.”

² A.R.S. § 40-303(A).

³ The Infrastructure Agreement is dated as of September 29, 1997. On October 29, 1997 Citizens filed an application requesting a CC&N and generally requesting Commission approval of the Infrastructure Agreement.

AND REPLACE WITH:

“In that case, APS sought a declaratory order confirming that only “traditional indebtedness for borrowed money” constituted “evidence of indebtedness” under A.R.S. §§ 40-301 *et seq.* and that other arrangements did not require prior Commission authorization and did not count against APS’ authorized debt capacity.⁴ The Commission declined to confine “evidence of indebtedness” to traditional indebtedness for borrowed money and stated that “the purpose of long-term debt limits would be frustrated if APS could structure the form of its debt to avoid those limits.” Instead, the Commission set out guidelines for APS to follow in the event that future changes to, or interpretations of, GAAP caused APS’ pre-existing agreements to exceed its authorized debt capacity. The Council points out that the Commission’s unwillingness to limit the definition of “evidence of indebtedness” to traditional forms of indebtedness allows the Commission to retain full regulatory control over various financing mechanisms like certificates of participation and interest rate swap agreements, which, while not technically considered “debt” under GAAP, have significant financial consequences on the parties thereto.⁵ The Commission recognizes the importance of regulating these types of financing activities to avoid the unintended consequence of providing a public service company with “a mechanism for circumventing [statutory debt] controls.”⁶

Page 28, Line 10 through Line 17 **DELETE:**

“The Council advances the argument that the Infrastructure Agreement constitutes a financing agreement whereby Pulte financed the construction of Anthem’s water and wastewater facilities through an interest-free loan, and that Arizona-American secured its indebtedness to Pulte through the issuance of two letters of credit. In regard to the Council’s reliance on *United States v. Austin*, the securities case cited by the Council in support of its position, the Company does not believe it provides relevant or persuasive authority, because it involves interpretation of the federal securities laws, which are of a different nature and purpose than a state law regulating a public utility’s debt and equity.”

AND REPLACE WITH:

“The Council responds that vehicle leases and trailer rental agreements are not intended to build up a public service corporation’s permanent capital structure, yet in Decision No. 69947 the Commission declined to exclude them from the scope of A.R.S. §§ 40-301 *et seq.*’s requirements. Moreover, the Council notes that like stocks, bonds, notes and other financing mechanisms, the Infrastructure Agreement was used to finance AAWC’s capital improvements and thus is a “financial instrument[s] used to build up the permanent capital structure of the utility.”⁷ The Council also noted certain instances where the Company and Staff classify AIAC, which occasion the Pulte Refund Payments, with proceeds from debt issuances.⁸ Finally, to dispute the Company’s claim that the Infrastructure Agreement was entered into for “the specific and limited purpose of placing the risks of development on the developer,” the Council provides evidence that the original parties to the Infrastructure Agreement understood it to be, among other things, a financing

⁴ Decision No. 69947, Docket No. E-01345A-06-0779 at 2.

⁵ Anthem’s Post-Hearing Reply Brief at 3-4.

⁶ Commission Decision No. 69947, Docket No. E-01345A-06-0779 at 2, 12 (stating “the purpose of long-term debt limits would be frustrated if [a public service corporation] could structure the form of its debt to avoid those limits.”).

⁷ Anthem’s Post-Hearing Reply Brief at 5 (quoting language from Post-Hearing Brief of Arizona-American Water Company at 23-24).

⁸ *See id.*

agreement requiring Commission approval.⁹ Given these considerations, the Council urges the Commission to properly recognize that infrastructure financing agreements that call for future repayment of loans and advances by public utilities are evidence of indebtedness and to claim regulatory jurisdiction of them under A.R.S. §§ 40-301 *et seq.*”

DELETE Page 29, Line 7 through 14.

Page 30, Line 4 **INSERT** after “would be inequitable.”:

“However, the Council asserts that retroactive efforts by the Company and its predecessors to have the Infrastructure Agreement approved by the Commission are irrelevant because (i) Commission approval prior to the effective date of the Infrastructure Agreement, as explicitly required by A.R.S. §§ 40-301 *et seq.*, was neither sought nor obtained, and (ii) Arizona case law does not permit retroactive regulatory approval.¹⁰ Similarly, the Council points out that because want of Commission approval made the Infrastructure Agreement void from inception, any claim of unfairness to the Company due to its reliance on the Commission’s repeated refusals to approve the Infrastructure Agreement in and after 1998 lacks merit.”

Page 30, Line 12 **INSERT** after “as well as refund obligations.”:

“However, in fairness, the Commission observes that vehicle leases, trailer rental agreements and other agreements which may be included within the scope of A.R.S. §§ 40-301 *et seq.* pursuant to Decision No. 69947 are also not stocks, bonds, notes or any other form of financing agreement. Nevertheless,”

Page 30, Line 13 through Line 17 **DELETE**:

“Staff also points out that while the Council would use the Company’s failure to obtain Commission approval under A.R.S. §§ 40-301 to 303 to permanently exclude the full amount of the refund payments from rate base, the Council fails to explain how it reconciles this position with the fact that the Company sought Commission approval on several occasions but was unsuccessful in obtaining it.”

Page 31, Line 2 **INSERT** after “of indebtedness.”:

“In that regard, the Council notes that all existing main extension agreements which have been reviewed and approved by the Commission under A.A.C. R14-2-406 have satisfied the prior approval requirement of A.R.S. §§ 40-301 *et seq.* Further, the Council asserts that the Commission’s determination in Decision No. 69947 that contracts classified as “debt” under GAAP are subject to A.R.S. §§ 40-301 *et seq.* means that many routine contractual arrangements which might not be characterized as “traditional” forms of indebtedness are already subject to Commission review.”¹¹ The Council submits that it is disingenuous and indefensible to argue or conclude that a secured private financing arrangement on the order of \$100,000,000, with

⁹ See Anthem’s Exceptions at 7-8.

¹⁰ See Anthem’s Post-Hearing Reply Brief at 5-6 (citing *George v. Arizona Corp. Commission*, 83 Ariz. 387, 322 P.2d 369 (1958) which in addition to prohibiting retroactive approval where prior approval is required, states that “where the public interest is involved neither estoppel nor laches can be permitted to override that interest”). 83 Ariz. at 391, 322 P.2d at 371.

¹¹ Anthem’s Exceptions at 5 fn. 4.

concomitant future ratemaking consequences for a public service corporation party thereto, should not be subject to the Commission's "supervision" and "control," particularly where the Commission has elected to retain supervision and control over routine contracts.¹²

Page 31, Line 6 **INSERT** after "refunds it made.":

"Finally, in response to other arguments put forth by the Company, Staff or RUCO, the Council correctly observes that A.R.S. §§ 40-301 *et seq.*, does not contain any provision (i) exempting "private agreements," (ii) waiving the prior approval requirement where a public utility has previously tried but failed to obtain the required approval, (iii) allowing the Commission to ignore the application of the law if it would be unfair to the public service corporation in question, or (iv) allowing the Commission to ignore the law if following it would be administratively burdensome for the Commission."¹³

DELETE Page 31, Line 6 through Line 20

AND REPLACE WITH:

"Given the above considerations, we conclude that the Infrastructure Agreement is "evidence of indebtedness" within the meaning of A.R.S. §§ 40-301 *et seq.*, which required prior Commission approval. Pulte's predecessor in interest neither sought nor received an order from the Commission authorizing the Infrastructure Agreement prior to its execution and delivery. Therefore, pursuant to A.R.S. § 40-303(A), the Infrastructure Agreement and the Company's obligation to pay the Pulte Refund Payments pursuant to the Infrastructure Agreement were void from the outset, or "*ab initio*." In recognition of these circumstances, we find that the Pulte Refund Payments should be permanently excluded from the Company's rate base and denied any associated ratemaking recognition. In doing so, the Commission will avoid the unintended consequence of public utility customers being saddled with exorbitant rate increases originating from an allegedly "private agreement," where the parties thereto had no public accountability to the substantial detriment of unprotected third-party ratepayers."

MAKE CONFORMING CHANGES

Page 33, Line 17 through Line 19 **DELETE:**

"We find that the fact that the Company did not obtain approval of the Infrastructure Agreement pursuant to A.A.C. R14-2-406 does not provide a valid basis for excluding the refund payments from rate base."

AND REPLACE WITH:

"However, this perceived "remedy" does not in fact fully address and compensate for the situation now before the Commission. More specifically, the purpose of the approval requirement prescribed in A.A.C. R14-2-406 is to provide the Commission with an opportunity to examine all

¹² Anthem Exceptions at 6-7.

¹³ Anthem Exceptions at 5.

aspects of a proposed main extension agreement (including the proposed refund formula) in order that the Commission may insure that all aspects of the proposed agreement are consistent with the "public interest." In that regard, the immediate refund "remedy" set forth in A.A.C. R14-2-406(M) would appear to address the concerns of the person or entity providing the AIAC in question. However, this perceived "remedy" does not in any manner address those aspects of a proposed main extension agreement which could adversely impact the ratepayers of the public service corporation in question at some future date. That is precisely the situation now before the Commission, where the Company is seeking rate base inclusion and ratemaking recognition of refund payments made by the Company pursuant to an Infrastructure Agreement (and refund formula) never approved by the Commission. Therefore, the only effective "remedy" for the failure of the Company (and its predecessor in interest) to obtain Commission approval of the Infrastructure Agreement required by A.A.C. R14-2-406(A) and (M) is for the Commission to deny the Company's request for rate base inclusion and ratemaking recognition of the Pulte Refund Payments."

MAKE CONFORMING CHANGES

Page 35, Line 21 after "future rate cases." **INSERT:**

"This situation is further compounded by recently discovered information, jointly filed in this proceeding by RUCO and the Council on November 9, 2010, in which Del Webb, Pulte's predecessor in interest, disclosed to the Arizona Department of Real Estate (the "Department") that the estimated costs of the Anthem water and wastewater infrastructure were to be included in the purchase prices of homes to be sold by Del Webb to Anthem residents, who thereafter became water and wastewater ratepayers of the Company.¹⁴"

Page 36, Line 16 after "matter of equity." **INSERT:**

"However, RUCO's recent Joint Filing with the Council appears to suggest that RUCO believes it would be unconscionable for the Commission to require Anthem residents to pay through rates what they have already paid through home prices, regardless of the use and usefulness of the facilities."

Page 60, Line 17 after "its capital structure." **INSERT:**

"In its July 16, 2010 Closing Brief, RUCO's revised computations suggest that a 6.37% ROR is also reasonable and appropriate, based on American Capital's lower cost of short-term debt, as reported in American Water's most recent 10-K filing with the SEC. Further, the Council points to investment expert Steven Puhr's written public comment in the instant proceeding which demonstrates that a 5.23% ROR is also reasonable and appropriate.¹⁵ The Council argues that because American Water is the sole shareholder of AAWC and AAWC's stock is not publicly sold, any claim by the Company that a higher return on equity and, correspondingly, a higher ROR is needed in order to attract independent equity capital does not account for the real-world phenomena in this instance.¹⁶"

¹⁴ See "Notice of Supplemental Information" jointly docketed by RUCO and the Council on November 9, 2010.

¹⁵ See Opinion and supporting materials filed by Stephen P. Puhr as public comment with the Commission's Docket Control on April 28, 2010 in the instant proceeding.

¹⁶ Anthem's Post-Hearing Reply Brief at 15-16.

DELETE Page 61 Line 15 through Line 18

AND REPLACE WITH:

“Based on the entire record in this proceeding, the adoption of a ROR [not to exceed 6.37%] for the Company, which in this instance results in a fair and reasonable ROR that (i) accounts for the Company’s capital requirement, and (ii) at the same time mitigates, to some extent, the significant rate increases to be experienced by Anthem residents. In our opinion, such determination is consistent with our responsibility to establish “just and reasonable rates and charges” pursuant to Article 15, Section 3 of the Arizona Constitution.”

MAKE CONFORMING CHANGES

DELETE Page 81, Line 9 through Page 82, Line 2

AND REPLACE WITH:

“Good public policy requires the Commission to correctly assign cost responsibility for all ratemaking components in as expeditious manner as possible, and deconsolidation of Anthem/Agua Fria Wastewater District is consistent with such action. However, the record does not include adequate rate base or operating income information to immediately implement stand-alone rate designs for the resulting Anthem Wastewater District and Agua Fria Wastewater District at this time. Therefore, we will (i) order a rate design for the Anthem/Agua Fria Wastewater District as a consolidated district on an interim basis utilizing the Company’s existing rate structure, and (ii) order the docket in the instant proceeding to remain open for the limited purpose of designing and implementing stand-alone revenue requirements and rate designs for the Anthem Wastewater District and Agua Fria Wastewater District, respectively, as soon as possible. In any event, such implementation should be well in advance of AAWC’s next rate case involving Anthem and Agua Fria wastewater ratepayers.”

MAKE CONFORMING CHANGES

Page 79, Line 21 after “service principles.” **INSERT:**

“The Council has requested that if the Commission determines to adopt Staff’s rate structure, then the Commission delay implementation of the new rate structure for an appropriate period of time (e.g., one year) in order to provide Anthem ratepayers with the opportunity to alter usage requirements (e.g., the winter lawn requirements) and actual usage.¹⁷ Concurrently, the Company should offer a dual metering program for those Anthem customers that wish or are required to continue to maintain winter lawns. The Council asserts that this would provide all interested persons with the ability to measure both outdoor water usage and indoor usage; and, wastewater bills would be based on only indoor usage, thereby avoiding the requirement to pay for water that does not enter the sewage system.”

¹⁷ See Anthem’s Exceptions at 19.

[OPTION 1]

DELETE Page 82, Line 16 through Page 83, Line 13

AND REPLACE WITH:

“Of the stand-alone rate design proposals presented, we find the Company’s proposal to be the most appropriate and reasonable, and will adopt it, as set forth in Exhibit A, attached hereto and incorporated herein.”

[OR OPTION 2]

Page 83, Line 13 after “will be adopted.” **INSERT:**

“However, implementation of the new rate structures for Anthem Water District and the Anthem/Agua Fria Wastewater District will be delayed until [January 1, 2012] to provide Anthem ratepayers with the opportunity to alter usage requirements and actual usage. Concurrently, the Company will offer a dual metering program for those Anthem customers that wish or are required to continue to maintain winter lawns.”

MAKE CONFORMING CHANGES

ATTACHMENT 2

DOCKET NO. W-01303A-09-0343 ET AL.

EXHIBIT A

ANTHEM/AGUA FRIA WASTEWATER

Monthly Usage Charge:

Residential	
Commercial 5/8"	\$ 44.48
Commercial 3/4"	66.72
Commercial 1"	89.06
Commercial LG	178.05

Commodity Charge (Per 1,000 gallons water usage)*

Residential	\$9.5968**
Commercial 5/8"	5.5760
Commercial 3/4"	5.5760
Commercial 1"	5.5760
Commercial LG	5.5760
Wholesale Phoenix	5.5760

Effluent Charge:

All gallons (Per Acre-foot)	\$250.00
All gallons (Per 1,000 gallons)	0.77

Annual Fee for Industrial Discharge Service

<=50,000 gallons water per month	\$ 500.00
> 50,000 gallons water per month	1,000.00

Sewer Facilities Hook-Up Fees

Fee per Equivalent Residential Unit (" ERU")	\$ 765.00
ERU Schedule:	
Single Family Home	1.00
Apartment Units	0.50
Commercial Units (per acre)	4.00
Resorts (per room)	0.50

SERVICE CHARGES:

Establishment during business hours	\$30.00
Establishment after business hours	45.00
Reconnection (delinquent)	40.00
Reconnection after hours	55.00
NSF Check	15.00
Late Fee (Per Month)	1.50%

*Note: Each residential customer will be billed based on that customer's average water usage for the months of January, February and March in a given year. The customer's billing would be reset every year based upon the customer's water usage for this preceding three month period at a rate of \$9.5966 per 1,000 gallons. ROO at p.790, lines 3-9.

** Note: \$9.5966. ROO at p.79, line 7.