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AZ CORP COMMISSION
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Arizona Corporation Commission

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BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION OF ARIZONA WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY, AND FOR ADJUSTMENTS TO ITS RATES AND CHARGES FOR UTILITY SERVICE FURNISHED BY ITS WESTERN GROUP AND FOR CERTAIN RELATED APPROVALS.

DOCKET NO. W-01445A-10-0517

ARIZONA WATER COMPANY'S MOTION FOR PROCEDURAL ORDER REGARDING SUFFICIENCY OF APPLICATION

(Expedited Consideration Requested)

(Oral Argument Requested)

Arizona Water Company ("Arizona Water Company" or the "Company") requests an Order (1) addressing the sufficiency of Arizona Water Company's December 29, 2010 Application for a Determination of the Fair Value of its Utility Plant and Property, and for Adjustments to its Rates and Charges for Utility Service Furnished by its Western Group ("Application") in this docket, (2) confirming the time limitations related to sufficiency determinations as set out in the Rate Case Management Rule, A.A.C. R14-2-103 ("Rule 103"), (3) denying any request to administratively close the present proceeding, and (4) directing the Utilities Division ("Staff") of the Arizona Corporation Commission ("Commission") to complete its review of Arizona Water Company's pending Application to ascertain whether it complies with the sufficiency requirements of Rule 103.

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1 Arizona Water Company further requests that a procedural conference be set at the
2 earliest opportunity to address the compelling procedural issues set forth below. The Rule
3 103 sufficiency period expires on January 28, 2011. Accordingly, Arizona Water Company
4 believes that a telephonic conference should be scheduled as soon as practicable to set the
5 requested procedural conference.

6 **I. INTRODUCTION.**

7 After receiving a complete rate case application that complies with the sufficiency
8 requirements of Rule 103 and its Appendices, may Staff choose to cease work on the
9 Application at the sufficiency stage and thwart the time limitations established by the
10 Commission by unilaterally imposing its own unsupported interpretations of what is an
11 appropriate "one-year historical period" and "the most recent practical date available prior
12 to filing" utilized by the Company for its test year?

13 That is the question presented by the exchange of letters that has occurred between
14 Staff and Arizona Water Company at the onset of Arizona Water Company's 2010 Western
15 Group rate case filing. As a result, the parties need the Administrative Law Judge's
16 intervention to move the case forward.

17 Staff asserts that Arizona Water Company's test year is stale and that it must
18 withdraw its Application and wait until it has at least 12 full months of actual experience
19 with rates the Commission adopted last year (Decision No. 71845, August 25, 2010) before
20 it can apply for a new rate determination. But instead of addressing the substantive issues of
21 normalizing revenues, expenses and rate base through pro forma adjustments in evidentiary
22 proceedings, Staff is attempting to circumvent the rules and threatens to seek administrative
23 closure of this matter, which would cause Arizona Water Company to waste many hundreds
24 of hours of its employees' time and significant expert witness costs and legal expenses, just
25 to start the process over again later this year in order to satisfy Staff's arbitrary demands.
26 Arizona Water Company seeks a final sufficiency determination under Section (B)(7) of
27 Rule 103, which it is entitled to by January 28, 2011, and for the case to proceed forward as
28 filed under the time deadlines established in Commission rules.

1 **II. PROCEDURAL HISTORY.**

2 Arizona Water Company's Application was filed on December 29, 2010. The
3 Application seeks adjustments to the Company's rates and charges for utility service
4 furnished to approximately 30,400 customers by its Western Group, which includes five
5 water systems, three of which have been consolidated.

6 Arizona Water Company utilized a test year ending December 31, 2009 in its
7 Application, with appropriate pro forma adjustments made to the test year data to reflect
8 certain changed conditions, including the new rates and charges the Commission adopted in
9 Decision No. 71845, effective July 1, 2010. In submitting its Application, Arizona Water
10 Company carefully followed the requirements of Rule 103, and prepared and docketed
11 thousands of pages of pre-filed testimony (including expert testimony), detailed schedules,
12 exhibits, studies and reports.

13 On January 7, 2011, Staff sent a letter to Arizona Water Company directing the
14 Company to withdraw its pending Application or face administrative closure of the
15 Application (the "January 7 Staff Letter", attached as Exhibit "A"). Arizona Water
16 Company responded by letter on January 14, 2011 (attached as Exhibit "B"), presenting
17 compelling reasons why Staff should withdraw the January 7 Staff Letter, and requesting
18 Staff to do so by January 19, 2011. Staff has refused, and persists with its refusal to process
19 the Application and its threat to seek administrative closure of this Docket. In taking this
20 position, Staff is grafting unsupported requirements onto Rule 103 that deny Arizona Water
21 Company the right to present its rate case to the Commission for determination. In addition,
22 Staff's position essentially adopts and imposes new rules and guidelines on the Company in
23 contravention of the Arizona Administrative Procedures Act ("APA") and the
24 Commission's own rulemaking procedures. Accordingly, Arizona Water Company requests
25 entry of an Order directing Staff to proceed with timely processing of the Application as
26 filed.

27 **III. ARGUMENT.**

28 In the January 7 Staff letter, Staff has taken the position that Arizona Water

1 Company is required to withdraw its current application and resubmit a “new application
2 using a test year that provides at least twelve months of actual data under the most current
3 rates approved by the Commission,” and is requiring the Company to use an historical test
4 year more recent than December 31, 2009. [Ex. A at 2.] Essentially, Staff’s position is that
5 Arizona Water Company is prohibited from filing a rate application utilizing an historical
6 test year ending earlier than July 1, 2011, twelve months following the date Arizona Water
7 Company’s current rates became effective. Staff’s position is unsupported by and contrary
8 to the plain language of Rule 103, contrary to Arizona law and Commission practice, which
9 permits consideration of testimony and evidence about events subsequent to the historical
10 test year during a rate case. Also, Staff’s position would unilaterally impose sweeping new
11 rules and regulations on utilities without appropriate notice or legal basis, depriving Arizona
12 Water Company of its right to a fair consideration of its Application and an opportunity to
13 earn a fair and reasonable rate of return on its utility plant and property. *See* Ariz. Const.
14 art. 15, § 3; *Arizona Corporation Comm’n v. Arizona Public Service Co.*, 113 Ariz. 368,
15 370, 555 P.2d 326, 328 (1976).

16 **A. Staff’s Position Contravenes the Plain Language of Rule 103, and**
17 **Confuses Sufficiency With Its Disagreement over Substantive Issues to be**
18 **Determined Later In the Case.**

19 Under Rule 103, Arizona Water Company is entitled to apply for a change in its rates
20 and charges. So long as that application complies with the requirements of Rule 103, Staff
21 must consider that application sufficient, and the Commission must then provide Arizona
22 Water Company and the other parties the opportunity to present evidence and testimony on
23 the merits of the issues in the case. *See Clay v. Ariz. Interscholastic Ass’n, Inc.*, 161 Ariz.
24 474, 476, 779 P.2d 349, 351 (1989) (“an agency must follow its own rules and regulations;
25 to do otherwise is unlawful”). Staff’s sweeping assertions that the historical test year
26 utilized by Arizona Water Company renders the entire Application “deficient” and all
27 associated schedules “invalid” is unsupportable, as is Staff’s unilateral decision to halt all
28 further work on the Application. Staff points to no provision of Rule 103 or other

1 Commission Rule or statutory authority for its position, and none exists. More importantly,
2 Rule 103 itself compels the opposite result. Under Rule 103, Section (B)(7), Staff has 30
3 days from the filing of a rate application to review each such filing and provide notice to the
4 utility that its filing is or is not in compliance with the Commission's requirements. If Staff
5 fails to file such notice, the application is deemed sufficient. If Staff unilaterally ceases
6 work on the Application without statutory or other authority, the Application must be
7 deemed sufficient as of January 28, 2011.

8 Stated succinctly, the Rule calls on Staff to review the rate filing to make sure it is
9 sufficient in form and content, but it does not authorize Staff to summarily disqualify a
10 filing based on Staff's disagreement with substantive issues and pro forma adjustments,
11 which must be the subject of later evidentiary hearings on the merits of those issues.

12 Also contrary to Staff's position, Rule 103 does not contain any requirement that the
13 historical test year utilized by Arizona Water Company must include twelve months of
14 actual experience under the most current rates approved by the Commission. Historically,
15 the Commission has deemed applications sufficient that utilized test years with far less than
16 twelve months' worth of actual data under then-existing rates. *See* Decision No. 54247
17 (November 28, 1984) (no new rates in test year); Decision No. 67744 (December 6, 1991)
18 (same); Decision No. 55118 (July 24, 1986) (original sufficiency finding had no new rates
19 in test year; later updated to include one month of new rates); Decision No. 55228 (October
20 9, 1986) (same).

21 More importantly, Section (B)(11)(g) of Rule 103 specifically allows a utility to file a
22 second rate application prior to the conclusion of a pending rate case (recognizing that the
23 time frames for a procedural conference and hearing "shall not be applicable to any filing
24 submitted by a utility which has more than one rate application before the Commission at
25 the same time"). Rule 103 does not, therefore, require a utility to wait for *any* actual
26 experience under new rates before filing a rate case. Staff is required by Rule 103 to
27 consider the second rate application even though the filing utility's rates may not have yet
28 changed. *See* Decision No. 55228 (October 9, 1986) (noting filing and sufficiency of

1 second rate application during pendency of first rate case). Section (B)(11)(g) of Rule 103
2 would never apply and would be rendered meaningless and unnecessary if, as Staff asserts
3 here, a utility is required to wait a full twelve months (or for any additional time period)
4 following one rate change before it was permitted to file a second application. Under
5 Arizona law, a regulation, like a statute, must be read to give meaning to all parts of the
6 regulation. *See Stapert v. Ariz. Bd. of Psychologist Exam'rs*, 210 Ariz. 177, 179, 108 P.3d
7 956, 958 (App. 2005) (rules of statutory construction apply to regulations); *Kimble v. City of*
8 *Page*, 199 Ariz. 562, 565, 20 P.3d 605, 608 (App. 2001) (court should avoid interpretation
9 that would render rule invalid). Accordingly, Staff's reading of Rule 103, which would
10 render one or more sections of that rule meaningless, must be rejected.

11 With respect to the allegedly "stale" nature of the historic test year utilized by
12 Arizona Water Company, Rule 103 expressly provides that a utility utilize "the most recent
13 *practical* date available prior to filing" for its historical data. A.A.C. R14-2-103(B)(1)
14 (emphasis supplied). Rule 103 does not further define the "most recent practical date
15 available," and certainly does not compel any minimum waiting period before filing. The
16 January 7 Staff Letter cites no authority demonstrating that a calendar 2009 test year is not
17 the most recent practical date available to Arizona Water Company for purposes of the
18 Application less than twelve months after the end of the test year. Notably, in Decision No.
19 71845, the Commission ordered Arizona Water Company not to file a general rate case
20 application earlier than ninety days after it docketed a Commission-ordered Consolidation
21 Study. The Consolidation Study was filed with the Commission on September 30, 2010,
22 ninety days prior to the filing of the Application. *See* Docket No. W-01445A-08-0440,
23 Certificate of Compliance Filing. Without that requirement, the Application would have been
24 filed earlier. The 2009 test year utilized by Arizona Water Company was the most recent
25 recorded calendar year available at the time the Application was filed, and the most practical
26 year available for providing the data and information required by Rule 103. Accordingly,
27 Arizona Water Company's use of that test year complies with Rule 103 and is entirely
28 appropriate.

1 Moreover, the Commission has repeatedly allowed the use of historical test years
2 within similar time frames as the one that was most practical in this case. For example, in
3 Docket No. W-2351A-07-0686, Picacho Peak Water Company filed a rate application on
4 December 13, 2007 utilizing a test year ending December 31, 2006. That application was
5 deemed sufficient by Staff with no requirement to change the test year. Similarly, in Docket
6 No. W-01303A-02-0908, Arizona American Water Company filed a rate application on
7 December 13, 2002, which utilized a test year ending December 31, 2001. That application
8 was also deemed sufficient with no change to the proposed test year. *See also* Docket No.
9 W-02168A-00-1000 (test year ending 11+ months before application deemed sufficient);
10 Docket No. W-01445A-00-0962 (test year ending 11 ¾ months before application deemed
11 sufficient); Docket No. W-02113A-07-0551 (test year ending 9 months before filing of
12 application sufficient). There is no support in the governing Rule or Commission policy and
13 procedure for Staff's assertion that the test year utilized by Arizona Water Company must
14 be updated before Staff considers the Application.

15 In Arizona Water Company's last Western Group rate filing, Docket No. W-01445A-
16 04-0650, Staff took the position that the Company was required to submit an inverted tiered
17 rate design as a condition of sufficiency under the Rule (*See* Motion to Require
18 Supplemental Sufficiency Information docketed September 24, 2004). After briefing and
19 argument before Administrative Law Judge Teena Wolfe, including her analysis of many of
20 the issues applicable here, Staff's motion was summarily denied. *See* Rate Case Procedural
21 Order Docketed November 15, 2004. In that case, as in this case, Staff argued that a
22 substantive issue was a condition of sufficiency, while the ALJ ruled it was actually an issue
23 of fact to be decided by the Commission after evidentiary hearings. The same result should
24 occur here.

25 **B. Arizona Law and Commission Practice Permits Consideration of Post**
26 **Test Year Evidence and Pro Forma Adjustments to Historical Test Year**
27 **Data.**

28 As acknowledged in the January 7 Staff Letter, the Commission routinely utilizes pro

1 forma adjustments. These adjustments are properly used to account for the effect of
2 recently-approved rates on historical test years. In fact, Rule 103 specifically provides for
3 pro forma adjustments to be made to actual test year results and balances to obtain a more
4 realistic relationship between revenues, expenses and rate base. See A.A.C. R14-2-103,
5 Schedule C-2 (Income Statement Pro forma Adjustments). The Rule also requires
6 projections of income as part of the ratemaking process. See Schedule F-1 (Projected
7 Income Statements – Present and Proposed Rate).

8 Similarly, Arizona law does not support Staff's position. In *Arizona Corporation*
9 *Comm'n v. Arizona Public Service Co.*, 113 Ariz. 368, 555 P.2d 326, the Arizona Supreme
10 Court recognized that certain future costs were relevant to Commission consideration in its
11 rate setting. Specifically, the Supreme Court recognized that pro forma adjustments or
12 adjustments to historical test year figures were consistent with the Commission's
13 constitutional obligation to set reasonable rates and charges for public service corporations.
14 *Id.* at 371, 555 P.2d at 329 ("it is obvious that the Commission in its discretion can consider
15 matters subsequent to the historic year, bearing in mind that all parties are entitled to a
16 reasonable opportunity to rebut evidence presented"). In making that determination, the
17 Supreme Court recognized that the Commission is obligated to establish the "fair value" of
18 the utility's rate base in order to ensure that the utility is provided the opportunity to earn a
19 reasonable return on its utility property. *Id.*, 555 P.2d at 329 (citing *Simms v. Round Valley*
20 *Light & Power Co.*, 80 Ariz. 145, 151, 294 P.2d 378, 383 (1956)). To the extent that
21 inquiry requires adjustments to reflect post-test year developments or to reflect the impact of
22 approved rate changes, the Commission must consider evidence and testimony about those
23 factors. *Id.*, 555 P.2d at 327; see also, e.g., *Arizona Corporation Comm'n v. Citizens*
24 *Utilities Co.*, 120 Ariz. 184, 189, 584 P.2d 1175, 1180 (App. 1978) (recognizing that the
25 Commission "enters the misty area of prognostication" in its rate setting and that when it
26 does so "it must be prepared to accept what the sunshine of experience reveals as to the
27 validity of those forecasts" in subsequent challenges). In other words, those issues of fact
28 must be dealt with by the Commission after evidentiary hearings, and not by Staff using the

1 sufficiency review process to reject the Application because it disagrees with Arizona Water
2 Company's positions on the issues in the case.

3 **C. Staff's Position Violates the Arizona Administrative Procedures Act and**
4 **the Commission's Own Rulemaking Practices.**

5 As a state agency, the Commission is subject to the requirements set forth in the
6 APA. In the case of the Commission, those requirements have been established pursuant to
7 the Legislature's constitutional power to "prescribe rules and regulations to govern
8 proceedings instituted by and before" the Commission. Ariz. Const. art. 15, § 6; *Cf., State*
9 *ex rel. Corbin v. Arizona Corporation Comm'n*, 174 Ariz. 216, 218-19, 848 P.2d 301, 303-
10 04 (App. 1992) (holding that the Legislature has the power to enact rules of practice and
11 procedure governing proceedings before the Commission, although it may not enact laws
12 giving the executive branch the power to review the substance of rules that relate to
13 ratemaking). Under the APA, a "rule" is defined as "an agency statement of general
14 applicability that implements, interprets or prescribes law or policy, or describes the
15 procedure or practice requirements of an agency." A.R.S. § 41-1001(18). Under this
16 definition, any requirement imposed by the Staff that a utility utilize at least twelve months
17 of actual experience under approved rates or changing the definition of the appropriate test
18 year constitutes a proposed rule under the APA.¹

19 Article 3 of the APA, A.R.S. §§ 41-1021 through 41-1037, contains a number of
20 mandatory procedural requirements applicable to state agencies, including the Commission.
21 Among other requirements, each agency must establish and maintain a public rulemaking
22 docket that allows the public, including the regulated community, to be aware of the subject
23 matter of all proposed rules and their current status. A.R.S. § 41-1021. Prior to adopting
24 any new rule or amending or repealing an existing rule, each agency must file a notice of the
25

26
27 ¹ To the extent that the Staff "purports to exercise authority subject to this chapter"
28 (*i.e.*, to implement a new policy or practice requirement), the APA applies to that action.
A.R.S. § 41-1001(1).

1 proposed action with the Arizona Secretary of State for publication in the Arizona
2 Administrative Register. A.R.S. § 41-1022(A), (B). The agency must also afford persons
3 the opportunity to submit written statements, arguments, data and views on any proposed
4 rule prior to its adoption or amendment. A.R.S. § 41-1023. Each agency is then required to
5 consider the impact its proposed rulemaking will have on small businesses. A.R.S. § 41-
6 1035. A new rule, absent certain limited circumstances not present here, only becomes
7 effective 60 days after a certified original and two copies of the rule have been filed in the
8 Secretary of State's office. A.R.S. §§ 41-1031, 1032. If an agency does not substantially
9 comply with these procedural requirements, that new rule cannot be valid. A.R.S. § 41-
10 1030(A).

11 Here, Staff has not complied with any of the requirements of the APA in its attempt
12 to impose new application processing requirements on Arizona Water Company. If the
13 Commission actually imposes the additional requirements set out in the January 7 Staff
14 Letter on utilities, the Commission would be violating numerous Arizona statutes governing
15 agency rulemaking, rendering the new policy invalid as a matter of law. A.R.S. § 41-
16 1030(A). The Commission would also be disregarding its own rulemaking processes.
17 Accordingly, the positions stated in the January 7 Staff Letter are legally deficient, and Staff
18 should be directed to timely proceed with its required sufficiency review of the Application.

19 **IV. CONCLUSION.**

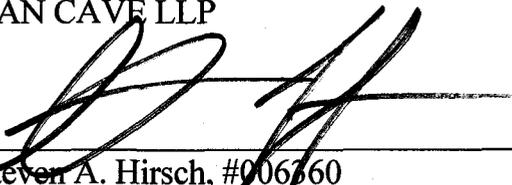
20 There is no legal basis for Staff's demand that Arizona Water Company withdraw its
21 application and resubmit an application utilizing a test year ending no earlier than July 1,
22 2011, especially under penalty of administrative closure of an Application that took
23 hundreds of hours and a great deal of cost to prepare. The filing requirements that must be
24 met by a utility's application for changes to its rates and charges for service are set forth in
25 Rule 103. Staff cannot summarily graft additional requirements onto Rule 103 and
26 announce them to the utility after its application has been filed, as Staff has done here. Nor
27 can Staff use the sufficiency review process to declare an application deficient based on
28 Staff's differences of opinion on factual and substantive matters without those matters being

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1 presented in evidentiary hearings. Given the Commission's long-standing practice of
2 accepting historical test years comparable to that utilized by Arizona Water Company in the
3 present case, and the routine use of pro forma adjustments to account for necessary
4 adjustments to the test year data (including rate changes the Commission adopts), Staff's
5 positions must be rejected and an Order entered confirming that this matter will not be
6 administratively closed, and directing Staff to timely review the Application in accordance
7 with Rule 103 and proper Commission procedure.

8
9 RESPECTFULLY SUBMITTED this 20th day of January, 2011.

10 BRYAN CAVE LLP

11
12 By 

13 Steven A. Hirsch, #006760

14 Stanley B. Lutz, #021195

15 Two N. Central Avenue, Suite 2200

16 Phoenix, AZ 85004-4406

17 Attorneys for Arizona Water Company

18 **ORIGINAL** and 13 copies of the foregoing
19 filed this 20th day of January, 2011 with:

20 Docket Control Division
21 Arizona Corporation Commission
22 1200 W. Washington Street
23 Phoenix, AZ 85007

24 **COPIES** of the foregoing hand-delivered
25 this 20th day of January, 2011, to:

26 Lyn A. Farmer, Esq.
27 Chief Administrative Law Judge
28 Hearing Division
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Exhibit A

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January 14, 2011

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Re: IN THE MATTER OF THE APPLICATION OF ARIZONA WATER
COMPANY FOR APPROVAL OF A RATE INCREASE (DOCKET NO.
W-01445A-10-0517)

Dear Mr. Olea:

This letter responds to your letter dated January 7, 2011 to Mr. Robert W. Geake,
Vice President and General Counsel of Arizona Water Company, regarding this case.

As detailed below, Arizona Water Company firmly believes that its December 29,
2010 Western Group Water Systems rate filing (the "Application") fully complies
with the sufficiency requirements set forth in the Rate Case Management Rule,
A.A.C. R14-2-103 (the "Rule"), and that the assertions and conclusions in your letter
and actions taken by Staff are unwarranted under Commission Rules and Regulations
and its historical practices and procedures.

Initially, it is important to note that there is no support in the Rule for Staff's position
that Arizona Water Company's pro forma adjustments of the historical Test Year to
reflect current rates is inappropriate. Nor is there any support in the Rule for Staff's
position that the 2009 historical Test Year used by the Company in the Application
employs "stale data" or otherwise fails to meet the requirements of the Rule. The
Commission authorized the current rates in Decision No. 71845 as of July 1, 2010¹
For these reasons, your unilateral declaration that the Application is "deficient," that
"all associated schedules" are "invalid," and that the Staff may simply choose not to
work further on the Application at this time are not only unjustified, but violate the
expressly-stated time clock provisions of the Rule.

¹ The Commission determined the current rates based on a test year ending December 31,
2007, not December 31, 2008 as stated in the January 7 letter

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Contrary to the observations in your January 7 letter, the Rule does not contain a definition of "the most recent practical date available prior to the filing," and your letter provides no authority to support Staff's conclusion that the December 31, 2009 test year employed by the Company is not "the most practical date available." In fact, December 31, 2009 was the most recent recorded calendar year at the time the Application was filed. As Staff and the Commission are well aware, there are many prior rate cases for which sufficiency has been found that were filed near or beyond one year from the chosen test year.²

Moreover, the Rule contains no requirement, and Staff does not cite any authority for its conclusion, that the one-year historical test period must include 12 months' experience of actual data under the most current rates approved by the Commission. As Staff must be aware, there are dozens and dozens of rate cases in which applications have been deemed sufficient despite containing test years with far less than 12 months' worth of actual data under the most current rates.³ In fact, in the December 22, 2010 meeting that you held with Arizona Water Company's officials before the Application was filed, you stated that the Staff would prefer to see a test year with six months of actual data under the most current rates, not 12 months. Again, the Rule does not provide for either time frame, or any specified time frame, to be controlling. As you acknowledge in your letter, pro forma adjustments are routine. The Rule provides for pro forma adjustments to be made to actual test year results and balances to obtain a more realistic relationship between revenues, expenses and rate base.

Section (B)(11)(g) of the Rule specifically contemplates a situation where a utility may file a second rate application even prior to the conclusion of a pending rate request, underscoring that the Staff is directed by the Rule to consider rate applications under rates that are not yet changed. Because the Rule allows for more than one rate filing (which obviously would not contain any rate experience under newly approved rates, let alone 12 months of experience), this section of the Rule would be rendered meaningless and unnecessary if a utility was required to wait a full 12 months following one rate change before it was permitted to file a second application.

In addition, case law does not support the conclusions in your January 7 letter. Not only is there no Arizona case of which we are aware that supports Staff's positions, many Arizona opinions actually support pro forma adjustments and the use of adjustments to historical test year figures to give effect to Commission-authorized rates as part of the Commission's obligation to set reasonable rates

² See, e.g., *Picacho Peak Water Company*, Docket No. W-02351A-07-0686 (test year ending 11 1/2 months before application filing accepted as sufficient); *Chaparral City Water Company*, Docket No. W-02113A-07-0551 (test year ending 9 months earlier accepted as sufficient); *Arizona American Water Company*, Docket No. W-01303A-02-0908 (test year ending 11 1/2 months before application filing accepted as sufficient); *Arizona Water Company*, Docket No. W-01445A-00-0962 (test year ending 11 3/4 months earlier accepted as sufficient).

³ See, e.g., *Arizona Public Service Company Rate Cases*, Decision No. 54247 (November 28, 1984)(no new rates in accepted test year); Decision No. 67744 (December 6, 1991)(same); Decision No. 55118 (July 24, 1986)(same as to original sufficiency finding; later updated to include only one month of new rates); Decision No. 55228 (October 9, 1986)(same).

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and charges for public service corporations. *See, e.g., Arizona Corporation Commission v. Arizona Public Service Co.*, 113 Ariz. 368, 371, 555 P.2d 326, 329 (“it is obvious that the Commission in its discretion can consider matters subsequent to the historic year, bearing in mind that all parties are entitled to a reasonable opportunity to rebut evidence presented”); *Arizona Corporation Commission v. Citizens Utilities Co.*, 120 Ariz. 184, 189, 584 P.2d 1175, 1180 (1978) (“when the Commission itself, in defense of its rate making, enters the misty area of prognostication, it must be prepared to accept what the sunshine of experience reveals as to the validity of those forecasts. We find no error in the trial court’s admission of post-Test Year or post-Commission date of hearing evidence in this area”).

The sweeping conclusions in the January 7 letter that the test year issues render the entire Application deficient and all associated schedules invalid, and justify the Staff unilaterally ceasing any work whatsoever on the Application, are clearly not supportable. Not only is there no Rule or law permitting the Staff to do so, the terms of the Rule itself compel the Staff to file a notice of deficiency, including an explanation of any of the defects Staff finds in the materials filed with the Application, within 30 days of the utility’s filing. *See* Section (B)(7) of the Rule. Clearly the Rule calls on Staff to review the filing to make sure it is sufficient in form and content, but it does not authorize Staff to summarily disqualify a filing based on Staff’s disagreement with substantive issues and pro forma adjustments, which must be the subject of evidentiary hearings on the merits of those issues.

As I am sure you can appreciate, Arizona Water Company undertook many hundreds of man hours and incurred significant expense in preparing its Application, which in the interest of avoiding a stale test year, the Company filed as early as it was permitted to do so. As you know, the Application included several additional items, including a DSIC study and a report addressing water losses in the Pinal Valley Water System, as had been ordered by the Commission in the last rate case. Significantly, the Commission also directed Arizona Water Company not to file a general rate case application sooner than ninety days after it docketed the Commission-ordered Consolidation Study. That study was filed with the Commission on September 30, 2010, ninety days before this Application was filed. The Company worked diligently to complete all of the filings, and the Application complies in every respect with the Rule and the Appendices to the Rule. Arizona Water Company is entitled to have its Application for just and reasonable rates be processed, heard and decided by the Commission. It is completely unjustified and unreasonable for Staff to unilaterally conclude, without any support in the law or the record, that it simply “is unable to progress any further with regard to the sufficiency of your rate application.”

The Staff’s position also implicates other legal issues. If Staff’s argument were accepted by the Commission, the Commission’s actions would conflict with the Arizona Administrative Procedure Act (“APA”), A.R.S. §§ 41-1001 *et seq.*, by formulating and adopting a rule that implements agency policy without any required prior notice or public participation. Also, in Arizona Water Company’s last Western Group rate filing, you may recall that Staff took the position that the Company was required to submit an inverted tiered rate design as a condition of sufficiency under the Rule (Docket No. W-01445A-04-0650; *see* Motion to Require Supplemental Sufficiency Information docketed September 24, 2004). After briefing and argument before ALJ Teena Wolfe, including her analysis of many of the

Mr. Steven M. Olea
January 14, 2011
Page 4

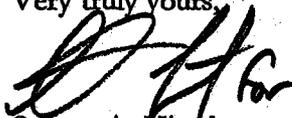
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issues set forth in this response letter, Staff's motion was summarily denied. *See* Rate Case Procedural Order Docketed November 15, 2004 in Docket No. W-01445A-04-0650. In that case, as in this case, the Staff argued that a substantive issue was a condition of sufficiency while the ALJ ruled it was actually an issue of fact to be decided by the Commission after evidentiary hearings.

By taking the position in your January 7 letter that the Company must withdraw its case by January 28 or the Staff will request that the docket be administratively closed, you have left the Company with no choice but to seek relief before ALJ Sarah Harpring unless the Staff reconsiders and withdraws its position. Under Section (B)(7) of the Rule, Staff has until January 28, 2011 to note deficiencies in Arizona Water Company's Application. If no such deficiencies are noted, Arizona Water Company will take the position that no such deficiencies in its filing exist.

For the reasons stated above, Arizona Water Company requests that the Staff proceed to complete its review within the Commission-required timelines under the Rule. Arizona Water Company further requests that you withdraw your January 7 letter. Please respond to the undersigned by the close of business on Wednesday, January 19, 2011 as to whether Staff will do so. Otherwise, Arizona Water Company will have no choice but to seek appropriate relief.

Very truly yours,



Steven A. Hirsch

SAH:car/ct

c: Docket Control Center
Lyn Farmer, Hearing Division
Delbert Smith, Engineering
Connie Walczak, Consumer Services
Janice Alward, Legal Division
Elijah Abinah, Utilities Division
Nancy Scott, Utilities Division
William M. Garfield, Arizona Water Company
Robert Geake, Arizona Water Company

Exhibit B

1 ARIZONA WATER COMPANY
Robert W. Geake (No. 009695)
2 Vice President and General Counsel
3805 N. Black Canyon Highway
3 Phoenix, Arizona 85015-5351
Telephone: (602) 240-6860
4
5 Steven A. Hirsch (No. 006360)
Stanley B. Lutz (No. 021195)
BRYAN CAVE, LLP
6 Two North Central Avenue, Suite 2200
Phoenix, AZ 85004
7 Telephone: (602) 364-7000
Attorneys for Arizona Water Company
8

9 **BEFORE THE ARIZONA CORPORATION COMMISSION**

10
11 IN THE MATTER OF THE APPLICATION
OF ARIZONA WATER COMPANY, AN
12 ARIZONA CORPORATION, FOR A
DETERMINATION OF THE FAIR VALUE
13 OF ITS UTILITY PLANT AND PROPERTY,
AND FOR ADJUSTMENTS TO ITS RATES
14 AND CHARGES FOR UTILITY SERVICE
FURNISHED BY ITS WESTERN GROUP
15 AND FOR CERTAIN RELATED
16 APPROVALS.

DOCKET NO. W-01445A-10-0517

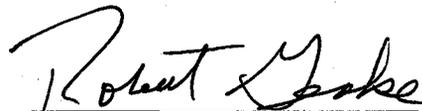
**ARIZONA WATER COMPANY'S
RESPONSE TO STAFF'S LETTER OF
DEFICIENCY**

17
18 Arizona Water Company, an Arizona corporation, hereby submits its response to the
19 Utility Division Staff's January 7, 2011 letter of deficiency to Arizona Water Company (see
20 Exhibit A attached hereto).

21 RESPECTFULLY SUBMITTED this 14th day of January, 2011.

22 ARIZONA WATER COMPANY

23
24 By:



25 Robert W. Geake
26 Vice President and General Counsel
ARIZONA WATER COMPANY
27 Post Office Box 29006
Phoenix, Arizona 85038-9006
28

1 Steven A. Hirsch
2 Stanley B. Lutz
3 BRYAN CAVE, LLP
4 Two North Central Avenue, Suite 2200
5 Phoenix, AZ 85004
6 Attorneys for Applicant
7 Arizona Water Company

8 An original and thirteen (13) copies of this Response was delivered this 14th day of January, 2011
9 to:

10 Docketing Supervisor
11 Docket Control Division
12 Arizona Corporation Commission
13 1200 West Washington Street
14 Phoenix, Arizona 85007

15 A copy of this Response was delivered this 14th day of January, 2011 to:

16 Ms. Lyn Farmer
17 Chief Administrative Law Judge
18 Hearing Division
19 Arizona Corporation Commission
20 1200 West Washington Street
21 Phoenix, Arizona 85007

22 Mr. Steve Olea, Director
23 Utilities Division
24 Arizona Corporation Commission
25 1200 West Washington Street
26 Phoenix, Arizona 85007

27 Ms. Janice Alward, Chief Counsel
28 Legal Division
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

By: 

EXHIBIT A



Steven A. Hirsch
Certified Real Estate Specialist
Partner
Direct: (602) 364-7319
Fax: (602) 716-8319
sahirsch@bryancave.com

January 14, 2011

Mr. Steven M. Olea
Director of Utilities Division
Arizona Corporation Commission
1200 W. Washington Street
Phoenix, AZ 85007-2927

Re: IN THE MATTER OF THE APPLICATION OF ARIZONA WATER
COMPANY FOR APPROVAL OF A RATE INCREASE (DOCKET NO.
W-01445A-10-0517)

Dear Mr. Olea:

This letter responds to your letter dated January 7, 2011 to Mr. Robert W. Geake,
Vice President and General Counsel of Arizona Water Company, regarding this case.

As detailed below, Arizona Water Company firmly believes that its December 29,
2010 Western Group Water Systems rate filing (the "Application") fully complies
with the sufficiency requirements set forth in the Rate Case Management Rule,
A.A.C. R14-2-103 (the "Rule"), and that the assertions and conclusions in your letter
and actions taken by Staff are unwarranted under Commission Rules and Regulations
and its historical practices and procedures.

Initially, it is important to note that there is no support in the Rule for Staff's position
that Arizona Water Company's pro forma adjustments of the historical Test Year to
reflect current rates is inappropriate. Nor is there any support in the Rule for Staff's
position that the 2009 historical Test Year used by the Company in the Application
employs "stale data" or otherwise fails to meet the requirements of the Rule. The
Commission authorized the current rates in Decision No. 71845 as of July 1, 2010¹
For these reasons, your unilateral declaration that the Application is "deficient," that
"all associated schedules" are "invalid," and that the Staff may simply choose not to
work further on the Application at this time are not only unjustified, but violate the
expressly-stated time clock provisions of the Rule.

¹ The Commission determined the current rates based on a test year ending December 31,
2007, not December 31, 2008 as stated in the January 7 letter

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And Bryan Cave,
A Multinational Partnership,
London

Mr. Steven M. Olea
January 14, 2011
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Contrary to the observations in your January 7 letter, the Rule does not contain a definition of "the most recent practical date available prior to the filing," and your letter provides no authority to support Staff's conclusion that the December 31, 2009 test year employed by the Company is not "the most practical date available." In fact, December 31, 2009 was the most recent recorded calendar year at the time the Application was filed. As Staff and the Commission are well aware, there are many prior rate cases for which sufficiency has been found that were filed near or beyond one year from the chosen test year.²

Moreover, the Rule contains no requirement, and Staff does not cite any authority for its conclusion, that the one-year historical test period must include 12 months' experience of actual data under the most current rates approved by the Commission. As Staff must be aware, there are dozens and dozens of rate cases in which applications have been deemed sufficient despite containing test years with far less than 12 months' worth of actual data under the most current rates.³ In fact, in the December 22, 2010 meeting that you held with Arizona Water Company's officials before the Application was filed, you stated that the Staff would prefer to see a test year with six months of actual data under the most current rates, not 12 months. Again, the Rule does not provide for either time frame, or any specified time frame, to be controlling. As you acknowledge in your letter, pro forma adjustments are routine. The Rule provides for pro forma adjustments to be made to actual test year results and balances to obtain a more realistic relationship between revenues, expenses and rate base.

Section (B)(11)(g) of the Rule specifically contemplates a situation where a utility may file a second rate application even prior to the conclusion of a pending rate request, underscoring that the Staff is directed by the Rule to consider rate applications under rates that are not yet changed. Because the Rule allows for more than one rate filing (which obviously would not contain any rate experience under newly approved rates, let alone 12 months of experience), this section of the Rule would be rendered meaningless and unnecessary if a utility was required to wait a full 12 months following one rate change before it was permitted to file a second application.

In addition, case law does not support the conclusions in your January 7 letter. Not only is there no Arizona case of which we are aware that supports Staff's positions, many Arizona opinions actually support pro forma adjustments and the use of adjustments to historical test year figures to give effect to Commission-authorized rates as part of the Commission's obligation to set reasonable rates

² See, e.g., *Picacho Peak Water Company*, Docket No. W-02351A-07-0686 (test year ending 11 1/2 months before application filing accepted as sufficient); *Chaparral City Water Company*, Docket No. W-02113A-07-0551 (test year ending 9 months earlier accepted as sufficient); *Arizona American Water Company*, Docket No. W-01303A-02-0908 (test year ending 11 1/2 months before application filing accepted as sufficient); *Arizona Water Company*, Docket No. W-01445A-00-0962 (test year ending 11 3/4 months earlier accepted as sufficient).

³ See, e.g. *Arizona Public Service Company Rate Cases*, Decision No. 54247 (November 28, 1984)(no new rates in accepted test year); Decision No. 67744 (December 6, 1991)(same); Decision No. 55118 (July 24, 1986)(same as to original sufficiency finding; later updated to include only one month of new rates); Decision No. 55228 (October 9, 1986)(same).

and charges for public service corporations. *See, e.g., Arizona Corporation Commission v. Arizona Public Service Co.*, 113 Ariz. 368, 371, 555 P.2d 326, 329 (“it is obvious that the Commission in its discretion can consider matters subsequent to the historic year, bearing in mind that all parties are entitled to a reasonable opportunity to rebut evidence presented”); *Arizona Corporation Commission v. Citizens Utilities Co.*, 120 Ariz. 184, 189, 584 P.2d 1175, 1180 (1978) (“when the Commission itself, in defense of its rate making, enters the misty area of prognostication, it must be prepared to accept what the sunshine of experience reveals as to the validity of those forecasts. We find no error in the trial court’s admission of post-Test Year or post-Commission date of hearing evidence in this area”).

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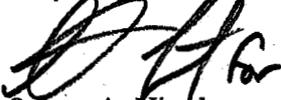
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Very truly yours,



Steven A. Hirsch

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