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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission
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COMMISSIONERS

GARY PIERCE - Chairman
BOB STUMP
SANDRA D. KENNEDY
PAUL NEWMAN
BRENDA BURNS

IN THE MATTER OF THE APPLICATION OF BELLA VISTA WATER CO., INC. AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANTS AND PROPERTY AND FOR INCREASES IN ITS WATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.	DOCKET NO. W-02465A-09-0411
IN THE MATTER OF THE APPLICATION OF NORTHERN SUNRISE WATER COMPANY, INC., AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANTS AND PROPERTY AND FOR INCREASES IN ITS WATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.	DOCKET NO. W-20453A-09-0412
IN THE MATTER OF THE APPLICATION OF SOUTHERN SUNRISE WATER COMPANY, INC., AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE FAIR VALUE OF ITS UTILITY PLANTS AND PROPERTY AND FOR INCREASES IN ITS WATER RATES AND CHARGES FOR UTILITY SERVICE BASED THEREON.	DOCKET NO. W-20454A-09-0413
IN THE MATTER OF THE JOINT APPLICATION OF BELLA VISTA WATER CO., INC., NORTHERN SUNRISE WATER COMPANY, INC. AND SOUTHERN SUNRISE WATER COMPANY, INC. FOR APPROVAL OF AUTHORITY TO CONSOLIDATE OPERATIONS, AND FOR THE TRANSFER OF UTILITY ASSETS TO BELLA VISTA WATER CO., INC. PURSUANT TO ARIZONA REVISED STATUTES § 40-285.	DOCKET NO. W-02465A-09-0414 DOCKET NO. W-20453A-09-0414 DOCKET NO. W-20454A-09-0414 DECISION NO. 72251 **OPINION AND ORDER**

DATES OF HEARING: July 21 & 22, 2010 and August 16-19, 2010

PLACES OF HEARING: Tucson and Phoenix, Arizona

ADMINISTRATIVE LAW JUDGE: Jane L. Rodda

APPEARANCES:

Mr. Jay Shapiro and Mr. Todd Wiley, FENNEMORE CRAIG, PC, on behalf of the Applicants;

Ms. Michelle L. Wood, Staff Counsel Residential Utility Consumer Office; and

Ms. Robin Mitchell, Ms. Bridget A. Humphrey and Ms. Kimberly A. Ruht, Staff Attorneys, Legal Division, on behalf of the Arizona Corporation Commission Utilities Division Staff.

BY THE COMMISSION:

I. BACKGROUND AND REQUESTED RELIEF

A. Introduction

Bella Vista Water Company, Inc. ("Bella Vista"), Northern Sunrise Water Company, Inc. ("NSWC") and Southern Sunrise Water Company, Inc. ("SSWC") (collectively the "Companies" or "Applicants") are certificated Arizona public service corporations that provide water utility service in Cochise County, Arizona. Bella Vista, NSWC and SSWC are all owned by Liberty Water, Inc. ("Liberty Water"), which is a wholly-owned subsidiary of Algonquin Power & Utilities Corporation ("APUC"), a publicly-traded corporation on the Toronto Stock Exchange ("TSX").

The Applicants each filed applications for rate increases, and also jointly filed an application to consolidate rates and operations. If consolidation is granted, operations will be consolidated under the aegis of Bella Vista, and all customers of the consolidated entity would pay uniform rates.[1] All of these dockets were consolidated for judicial efficiency.

The Residential Utility Consumer Office ("RUCO") was granted intervention.

The Commission received written comments from ratepayers who were primarily concerned about the magnitude of the requested increase, and who question whether Bella Vista ratepayers would be subsidizing the operations of the two smaller utilities.

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[1] In this Order the stand-alone Bella Vista Water Co., is called "Bella Vista" and the proposed consolidated utility is referred to as "BVWC" or "Company."

B. Bella Vista

Bella Vista started as Newman Water Company, and received a Certificate of Convenience and Necessity ("CC&N") in 1955 to serve an area around Sierra Vista, Arizona.[2] Bella Vista took its current name in 1981.[3] Bella Vista acquired and consolidated the operations of Nicksville Water Company in 1999.[4] Algonquin Water Resources of America, Inc. ("AWR"), the predecessor to Liberty Water, acquired Bella Vista in 2002.[5]

Bella Vista currently operates two major water systems, the City System and the South System. The systems are not located within an Active Management Area ("AMA"), but according to the Applicants, Cochise County has implemented rules requiring proof of adequate water supply for new construction/subdivisions which are intended to help control growth and ensure adequate water supply for the county's citizens.[6] Bella Vista states that it promotes water conservation in its service area and voluntarily implements Best Management Practices ("BMPs").

Currently, Bella Vista serves approximately 7,500 residential customers and over 1,000 commercial/industrial customers. Bella Vista has more than 30 wells and about 7.5 million gallons of water storage.[7] Bella Vista states, however, that water supply is a significant challenge in its South System because the geology of the area detrimentally impacts the yield from groundwater pumping.[8]

C. NSWC and SSWC

NSWC's and SSWC's service areas are located in and around Huachuca City and the Whetstone and Hereford townships in Cochise County, Arizona. NSWC and SSWC provide service to approximately 349 and 789 customers, respectively, nearly all of whom are residential. NSWC has 4 subsystems, two pairs of which are interconnected, and SSWC has three subsystems, 2 of which are interconnected. Between the two companies, there are a total of ten wells and approximately 500,000 gallons of combined storage.

NSWC and SSWC were formed by consolidating seven small water systems into two new

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[2] Decision No. 28866 (April 18, 1955).
[3] Decision No. 52033 (April 10, 1981).
[4] Decision No. 61730 (June 4, 1999).
[5] Applicants Initial Closing Brief at 2.
[6] *Id.* at 1.
[7] Ex S-3, Scott Dir. at MSJ at 8.
[8] Ex A-1, Sorenson Bella Vista Dir. at 5-6.

water utilities. Each of the water systems had been owned and operated by Johnny McLain and suffered from many physical inadequacies due to lack of capital investment and inattention to repair and maintenance. In 2003, the Commission issued an Order to Show Cause against the McLain systems, and during the course of that proceeding, the McLains filed bankruptcy.[9] In 2004, the Commission obtained relief from the automatic stay in the bankruptcy proceeding, and approved the appointment of the first interim manager, Arizona Small Utility Association of Arizona ("ASUA"), for the McLain systems.[10] In 2005, because the McLain systems were in severe disrepair, the Commission ordered a moratorium on new hook-ups.[11] The Commission approved the consolidation of the seven McLain systems into two utilities and approved rates and charges for NSWC and SSWC in 2006.[12] In September 2006, AWR replaced ASUA as the interim operator. AWR operated the McLain systems as interim operator until it was the successful bidder in the bankruptcy proceeding and acquired the systems in March 2007.

Liberty Water, the successor to AWR, made new capital investments in NSWC and SSWC including the installation of new meters, several new storage tanks and a number of pressure facilities, in addition to replacing pumps, electrical equipment and treatment facilities. Liberty Water states that it invested more than $1.66 million in NSWC and SSWC to bring them into conformance with applicable regulations and to provide safe and reliable service to their ratepayers.

D. APUC and Liberty Water

APUC owns 46 electric facilities and 17 water and wastewater facilities in Canada and the United States. Applicants state that similar to publicly traded companies in the United States, APUC is subject to various public reporting, financial, audit and other rules and requirements of the TSX and Canadian securities laws.[13] Algonquin Power Trust ("APT") provides financial, management, compliance, administrative and support services to APUC and its subsidiaries. APT charges APUC for its services and APUC allocates those costs to its regulated and unregulated facilities, as discussed later in this Order.

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[9] Decision No. 66241 (September 16, 2003); *see also* Decision No. 68667 (April 20, 2006) at 3.
[10] Decision No. 66241 (September 16, 2003).
[11] Decision No. 68272 (November 8, 2005).
[12] Decision No. 68826 (June 29, 2006).
[13] Ex A-18, Eichler Reb at 3; Tr. at 413-15.

Liberty Water provides all day-to-day administration and operations personnel for APUC's regulated utilities in Arizona, Texas, Missouri and Illinois. In Arizona, in addition to the Applicants, Liberty Water operates Gold Canyon Sewer Co., Black Mountain Sewer Co., Litchfield Park Service Co. ("LPSCO"), Entrada Del Oro Sewer Co. and Rio Rico Utilities, Inc. ("RRUI").

E. The Rate Requests

In Decision No. 68826, the Commission set NSWC's and SSWC's current rates and required that the companies file for new rates after system improvements were completed. NSWC and SSWC filed applications for rate increases on August 31, 2009, using a March 31, 2009, test year. According to the Applicants' Final Schedules, in the test year, NSWC had an operating loss of $78,045, on gross revenues of $191,966, and SSWC had operating income of $23,856, on gross revenues of $444,136, a 1.8 percent return on SSWC's rate base.[14]

The Commission approved Bella Vista's current rates in Decision No. 65350 (November 1, 2002). Bella Vista filed its current rate application on August 31, 2009, and reported adjusted operating income of $138,435, on adjusted gross revenues of $3,526,033, a 2.4 percent rate of return on Bella Vista's rate base, for the test year ended March 31, 2009.

On a stand-alone basis, the Applicants request revenue requirements as follows:[15]

Utility	Final Rate Base	Required Operating Income	WACC[16]	Total Revenue Requirement	Total Increase in Revenue Requirement	% Increase
Bella Vista	$5,914,586	$562,475	9.51%	$4,216,640	$690,607	19.6%
NSWC	$660,315	$73,295	11.10%	$398,939	$206,973	107.8%
SSWC	$1,320,713	$146,599	11.10%	$635,713	$191,577	43.1%

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[14] NSWC Final Schedule A-1; SSWC Final Schedule A-1.
[15] Applicants' Final Schedules A-1 for Bella Vista, NSWC and SSWC.
[16] Weighted Average Cost of Capital.

On a consolidated basis, BVWC seeks the following revenue requirement:[17]

Utility	Final Rate Base	Required Operating Income	WACC	Total Revenue Requirement	Total Increase in Revenue Requirement	% Increase
BVWC	$7,857,799	$773,993	9.85%	$5,267,035	$1,104,899	26.5%

RUCO recommends:[18]

Utility	Final Rate Base	Required Operating Income	WACC	Total Revenue Requirement	Total Increase in Revenue Requirement	% Increase
Bella Vista	$5,915,662	$487,742	8.24%	$3,932,619	$406,586	11.5%
NSWC	$660,314	$52,191	7.9%	$352,426	$160,460	83.5%
SSWC	$1,320,711	$104,389	7.9%	$504,671	$60,535	13.6%
BVWC	$7,858,889	$662,000	8.42%	$4,880,352	$718,216	17.26%

Staff recommends:[19]

Utility	Final Rate Base	Required Operating Income	WACC	Total Revenue Requirement	Total Increase in Revenue Requirement	% Increase
Bella Vista	$5,997,538	$527,783	8.8%	$2,758,987	$232,954	6.6%
NSWC	$649,345	$57,142	8.8%	$380,468	$188,502	98.2%
SSWC	$1,295,446	$113,999	8.8%	$563,118	$118,982	26.79%
BVWC	$7,942,329	$698,925	8.8%	$4,641,716	$479,580	11.52%

F. The Requested Consolidation

The Applicants propose to consolidate the operations of the three utilities, with Bella Vista becoming the sole surviving public service corporation. Applicants filed their Application to Consolidate on August 31, 2009, and request that the Commission transfer NSWC's and SSWC's CC&Ns to Bella Vista pursuant to A.R.S. §40-285. The resultant utility would have approximately 9,600 total customers and provide service under a single set of tariffs. Applicants assert that they operate multiple water systems in the same general area around Sierra Vista, and that consolidation is

[17] Applicants' Final Schedules BVWC A-1.
[18] RUCO's Final Schedules RLM-1 for BVWC, Bella Vista, NSWC and SSWC.
[19] Staff's October 5, 2010 Final Schedules ("Staff's Final Schedules") at CSB-1 for BVWC, Bella Vista, NSWC and SSWC.

the next logical step in "a small-region regionalization" that could promote economic development in the area by creating "regional ratepayer equity."[20]

Applicants argue that consolidation and regionalization can help ensure that more customers receive quality water service by creating a larger customer base which leads to a lower cost per connection.[21] Applicants claim that consolidation will lead to regulatory and administrative efficiencies, as the Commission will be regulating one utility with almost 10,000 customers, instead of three utilities, two of which would have fewer than 1,000 customers. Applicants believe that consolidation can increase operational efficiencies, by reducing costs associated with record-keeping, implementing the BMPs, and water sampling. Applicants argue that all of the customers would benefit from any future cost-savings because they would be sharing the total cost of service in a fair and equitable manner.[22]

In this case, based on the Applicants' proposed revenues and rates, on a stand-alone basis, the average NSWC customer would see an increase of $50.08, or 116.25 percent, per month and the average SSWC customer would see an increase of $20.36, or 47.80 percent, per month.[23] Under the Companies' proposed consolidated rates, the average NSWC residential customer would see a monthly <u>decrease</u> of $14.71 and the average residential SSWC customer would see a <u>decrease</u> of $14.64, while an average Bella Vista residential customer would see an increase of approximately $4.07 more per month than on a stand-alone basis.

Applicants assert that with consolidation the Bella Vista ratepayers will receive the benefit of a greater access to a reliable water supply and that the ability to share water between the SSWC and Bella Vista systems is a significant factor that favors consolidation. Applicants note that the Bella Vista South System is already physically connected to the SSWC Horseshoe subsystem and water can flow in either direction. Because Bella Vista's South System needs the water that SSWC can provide, Applicants believe that Bella Vista's customers will benefit from reduced future capital expenditures for well and storage facilities.

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[20] Applicants Initial Closing Brief at 7.
[21] *Id.*
[22] *Id.* at 8.
[23] Applicants' Final Schedule H-2, page 1; NSWC Final Schedule H-2, page 1; SSWC Final Schedule H-2, page 1.

RUCO does not object to the consolidation of the BVWC systems, finding that the following factors favor consolidation:

1. All three systems have similar water consumption patterns so a consolidated rate design would not distort price signals or contradict the Commission's goal of water conservation.
2. The three systems draw from the same water source.
3. Two of the three systems (Bella Vista and SSWC) are physically interconnected and NSWC is only six miles from Bella Vista, making Liberty Water in essence a "regional" water provider.
4. Applicants have a history of acquiring small water utilities and rate consolidation, with Bella Vista acquiring Nicksville Water, and Liberty Water acquiring the seven McLain systems and consolidating them into two entities.

RUCO also believes that consolidation will mitigate rate shock for the customers of the small NSWC and SSWC systems immediately, and by spreading costs over a larger customer base would reduce the severity of rate increases for all customers in future rate cases.[24] RUCO recognizes that consolidation may allow BVWC to better meet the capital needs of the smaller systems as they would not be constrained by their modest operating incomes, and believes that allowing consolidation might put BVWC in a position to consider acquiring other small and struggling water systems in the area.[25]

Staff supports consolidation and notes that rates would be higher on a stand-alone basis because the Applicants could not take advantage of economies of scale.[26] Staff believes that where and when it is technically and financially feasible, the Commission should seriously consider rate consolidation or system interconnection.[27] Staff believes that consolidation is favored when it promotes public health and safety; when systems are in close proximity such that they can be interconnected or allow customers to recognize a logical connection; and when it would result in economies of scale, minimize rate case expense, and mitigate price shock.[28]

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[24] RUCO Closing Brief at 30.
[25] *Id.*
[26] Staff's Opening Brief at 3.
[27] Ex S-8, Brown Consolidation/Rate Design Dir. at 1.
[28] *Id.* at 2-3.

All parties in this case recommend consolidation of operations and uniform tariffs for the three utilities. The systems are already owned by the same parent and utilize the same Liberty Water personnel for day-to-day operations. The systems are in the same general area near Sierra Vista, Arizona, and Bella Vista and SSWC are already physically interconnected.

The benefits of consolidation for the two smaller systems, NSWC and SSWC, are clear. These systems had a troubled past when they were part of the McLain systems, and they required significant system upgrades to come into compliance with Arizona Department of Environmental Quality ("ADEQ") and Commission standards. Under consolidation, because the investment in plant is spread over a larger customer base, the NSWC and SSWC ratepayers would receive substantial rate decreases under each of the different parties' recommendations in this case, as illustrated below:

			Applicants[29]		RUCO[30]		Staff[31]	
	Ave Gal. Used	Current Ave. Bill	Stand Alone	Consol.	Stand Alone	Consol.	Stand Alone	Consol.
NSWC	5755	$43.08	$93.15	$28.37	$82.53	$29.93	$86.80	$19.11
SSWC	5581	$42.60	$62.96	$27.95	$50.11	$26.48	$54.37	$18.67

Even the larger Bella Vista System will benefit from consolidation, as it gains access to a much needed additional water source, and because it will have approximately 1,000 additional connections over which to spread the costs of capital improvements and increasing operational costs in the future. The rate impact on the Bella Vista ratepayers under each of the parties' positions is illustrated below:

			Applicants		RUCO		Staff	
	Ave Gal.	Current Ave. Bill	Stand Alone	Consol.	Stand Alone	Consol.	Stand Alone	Consol.
Bella Vista	6612	$22.90	$26.34	$30.42	$26.60	$29.15	$27.38	$20.82

Under Staff's recommendations, the current average residential Bella Vista ratepayer would see a monthly decrease of $2.08 under consolidation versus an increase of $4.48 on a stand-alone basis. Under the Applicants' proposed rates, the average Bella Vista residential ratepayer would see

[29] Applicants' Final Schedules at H-2.
[30] RUCO's Final Schedules at RUM-RD2.
[31] Staff's Final Schedules at CSB-4 RD, CSB-6 RD and CSB-8 RD.

an increase of $3.44 on a stand-alone basis, and an increase of $7.50 on a consolidated basis. Thus, under the Companies' proposed rates, the "cost of consolidation" for the residential Bella Vista ratepayer is $4.06 per month, (i.e., the difference between the consolidated rates and the stand-alone rates). Under RUCO's proposed rates, the average residential Bella Vista ratepayer would pay $2.55 per month more under the consolidated rates than under stand-alone rates. The immediate cost of consolidation to the ratepayers is relatively small compared to the significant benefits to all of the companies and the region.[32] Having a regional provider benefits the entire area as issues of water management and conservation will be easier to administer.

We agree with the parties, that if ever there was a case that supported consolidation of operations and rates, this is the case, and we approve the transfer of assets and CC&N from NSWC and SSWC to Bella Vista and the consolidation of operations and rates.

Staff recommends that although Bella Vista, NSWC and SSWC are consolidated, the Company should continue "to report the data and information separately for each of its individual systems by ADEQ Public Water System, including, but not limited to plant description, water use data, future Annual Reports and rate case filings."[33]

To the extent Staff's recommendation means that the Company should continue to track and account for plant improvements, and water use data for each of its water systems separately for use in annual reports and rate case filings, Staff recommendation is reasonable, and we concur with Staff's request. However, Staff's recommendation should not be interpreted as requiring or permitting separate rate case filings for individual systems now that the systems will be consolidated.

II. RATE BASE ISSUES

The parties recommend the following Original Cost Rate Base ("OCRB") balances:

	Bella Vista	NSWC	SSWC	Consolidated BVWC
Applicants[34]	$5,914,568	$660,315	$1,320,713	$7,857,799
RUCO[35]	$5,915,662	$660,314	$1,320,711	$7,858,889

[32] As discussed under the Rate Design section of this Order, under the authorized rates approved herein, the average Bella Vista ratepayer using 6,612 gallons per month would see an increase of $3.68 per month.
[33] Staff Closing Brief at 23.
[34] Applicants' Final Schedules filed September 16, 2010 at Ex 1 A-1; Ex, Ex 2, A-1, Ex -3, A-1 and Ex 4 A-1.
[35] RUCO's Final Schedules filed September 10, 2010 at RLM-1.

Staff[36]	$5,991,538	$649,345	$1,295,445	$7,942,328

Applicants did not request a Reconstruction Cost New Rate Base and thus, their Fair Value Rate Base ("FVRB") is the equivalent of their OCRB.

A. "Inadequately Supported" Plant Balances

Staff recommends disallowing $180,038 from Plant in Service because Staff claims the Applicants failed to provide adequate documentation of asset values. Staff argues that it is the utility's duty to maintain appropriate accounting records that reflect the cost of its plant, and that in the absence of documents verifying costs, the potential exists for ratepayers to pay for "non-existent plant."[37] Staff claims that its recommendation is consistent with other dockets in which the Commission has approved the same disallowance for failing to support plant values. Staff agrees that the Applicants' books reflect the plant balances that they are claiming, but states that they were not able to provide supporting invoices for all of the costs on the books.[38]

Applicants state that they don't disagree with Staff about the burden of proof concerning plant balances, but assert that they provided source documentation for the majority of plant costs for which Staff requested documentation. They state that they were unable to locate some of the original invoices dating back to the prior owners.[39] Applicants argue that they met their burden of proof, and thus the burden shifts to Staff to show that the amount being claimed is not reasonable, and that Staff must present substantial evidence in order to prevail. Applicants argue that there is no evidence of risk to ratepayers, as Staff's engineers did not claim that plant was missing.[40]

RUCO did not take issue with the Applicants' final plant values.[41]

Staff disallowed $145,870 for Bella Vista dating back to 2003, and $13,740 for NSWC and $25,428 for SSWC dating back to 2006 on the grounds of lack of documentation for plant values. The Company does not claim that it provided documentation, (other than ledger amounts), but rather claims that some of the records could not be located.[42] In his rejoinder testimony, Mr. Bourassa

[36] Staff's Final Schedules at CSB-1.
[37] Staff Opening Brief at 4.
[38] Staff Reply Brief at 4.
[39] Ex A-14, Bourassa Reb at 9; Ex A-16, Bourassa Rj at 5.
[40] Applicants Reply Closing Brief at 3-4.
[41] RUCO Closing Brief at 5.
[42] Ex A-14 at 9.

testified that with respect to the plant balances as reflected in its books and records: "[t]o disregard this evidence of cost, we have to assume that the Company either recorded the plant incorrectly or just made-up its plant costs out of thin air."[43]

The Commission must consider the fair value of the plant a utility uses to provide service. In doing so, the Commission must ensure that the plant that the Company claims to be using to provide service is actually in use, and also must verify that the value of that plant is accurately recorded. It is the value of plant in service that forms the basis on which rates are set. It is the Company's burden to demonstrate that its books and records accurately reflect plant values. It can do this in a number of ways, but having invoices that support the recorded values is one of the best. In this case, the Company could not find certain records, and besides the values recorded on its books, the Company did not offer other evidence of the plant value. The Company's suggestion that Staff has the burden of showing the Company's records are incorrect would be a complete reversal of the burden of proof. It is not unreasonable to request records, i.e. invoices, for plant additions, and the Company failed to provide sufficient evidence to support its plant values. Consequently, we adopt Staff's adjustment to Plant in Service.

B. Plant Retirements

In this proceeding, Staff raised the issue that Applicants were not appropriately recording retired plant.[44] Subsequently, the parties worked together to arrive at the amount of plant retirements.[45] Thus, the value of retired plant is no longer at issue. Furthermore, on July 29, 2010, Applicants filed Liberty Water's Asset Retirement Policy.[46] Staff reviewed the policy and provided its comments in Staff's Opening Brief.[47]

Staff notes that the Liberty Water policy addresses plant retirements only for plant that originally cost $5,000 or more, while the National Association of Regulatory Utility Commission ("NARUC") guidelines recommend recording all plant retirements, regardless of cost.[48] In addition,

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[43] Ex A-16 at 5.
[44] Ex S-6, Brown Dir. at 6-8.
[45] Staff Opening Brief at 5.
[46] Ex A-31.
[47] Tr. at 874; Staff Opening Brief at 5.
[48] Staff Opening Brief at 5.

Staff suggests that retirement work orders should include the following information: (1) whether the retirement cost utilized is actual or estimated; (b) the name of the water company or system from which the plant was removed; (c) the date of the retirement; (d) the NARUC account number from which the plant was removed; (e) the reason for the retirement; and (f) appropriate approvals on the work orders.

Applicants do not object to Staff's recommendations, and state that the issue of retirements is not in dispute.[49]

RUCO did not take issue with the final retirement figure.[50]

The parties have consensually resolved the issue of plant retirements with respect to this rate case. Liberty Water has devised a written retirement policy that appears to conform to NARUC Guidelines. On a going-forward basis, whatever the original cost of the plant item, the Company should account for retired plant consistent with NARUC guidelines.

C. Advances in Aid of Construction and Customer Meter Deposit Balances.

Staff states that it proposes a balance of $6,784,313 for Advances in Aid of Construction ("AIAC"), while the Applicants propose an AIAC balance of $6,781,443, a difference of $2,870.[51] Staff believes that it calculated the amount of Customer Deposits and AIAC correctly and that Customer Meter Deposits are appropriately part of the AIAC balance.[52]

Applicants state that they and Staff are in agreement that AIAC balances plus Customer Meter Deposits total $7,341,048.[53] Applicants explain that Staff's proposed AIAC balance is $6,784,313 and proposed customer meter deposit balance is $556,735, and that Applicants' proposed AIAC balance is $6,781,443 and proposed Customer Meter Deposits balance is $559,605.[54]

Pursuant to Arizona Administrative Code ("A.A.C.") R14-2-405.B, Customer Meter Deposits are paid by customers to establish new service lines and meters. The amount is typically approved by the Commission in connection with the rates and charges in a rate case. Pursuant to A.A.C. R14-2-

[49] Applicants Reply Closing Brief at 4.
[50] RUCO Reply Brief at 2.
[51] Staff Opening Brief at 8.
[52] *Citing,* A.A.C. R14-2-405.B: "An applicant for service shall pay to the utility as a refundable advance in aid of construction the sum set forth in the utility's tariff for each size service and meter."
[53] Applicants Reply Closing Brief at 5.
[54] *Id.*

405.B, the Service Line and Meter Deposits are refunded by an annual credit of 1/10 of the amount received applied to the November water bill. The Customer Meter Deposits are a source of non-investor capital which support the cost of installing new service connections. As a source of non-investor supplied capital, they are appropriately subtracted from rate base as a refundable advance.

Applicants do not dispute that Deposits for Service Lines and Meters should be deducted from rate base. Applicants are concerned that the $2,780 difference in the Customer Meter balance not be double-counted. Staff's witness testified that her customer meter balance is correct, however, the record does not include sufficient information to evaluate the claim. Ultimately, because the parties are in agreement about the total of the AIAC and Customer Meter Deposit balances, it is not critical to determine the exact customer meter account balance for purposes of establishing the appropriate deduction from rate base. The total deduction from rate base for both AIAC and Customer Meter Deposits is $7,341,048.

D. Calculation of Accumulated Amortization of Contributions in Aid of Construction ("CIAC").

Staff recommends $230,987 in Accumulated Amortization of CIAC, a difference of $417 from the Applicants' proposed balance of $230,570. Staff states the difference is the a result of the methodology used to compute the composite rate—the Company utilizes a composite amortization rate that includes non-depreciable plant, while Staff only used depreciable plant in the determination of the composite amortization rate.[55]

Staff argues that land is not depreciable and consequently is not amortizable, and should be excluded from the calculation of the amortization rate. Staff cites to the NARUC Guideline that provides that CIAC should be amortized over a period equal to the estimated service life of the contributed asset.[56] Staff states that the balance of the depreciation account and the accumulated amortization of CIAC should be equal, and since land does not depreciate like other plant items, and is not part of the depreciation expenses, if the depreciation expense is to balance with the accumulated amortization of CIAC balance, land must be removed from both.[57]

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[55] Staff Opening Brief at 8.
[56] Ex S-7, Brown Surr at 36.
[57] Staff Reply Brief at 6.

Applicants argue that the method of calculating CIAC amortization should be revenue neutral. Applicants assert that land funded with CIAC will be subject to the composite amortization of all CIAC, which will ensure revenue neutrality. Applicants state that if it is assumed that all plant is funded with CIAC, then individual plant assets should not be excluded from CIAC without a sound basis.

RUCO agrees with the Company's methodology used to determine amortization of CIAC, stating that the amortization rate must include non-depreciable plant in order to be revenue neutral.[58]

A composite amortization rate for CIAC is utilized when it is assumed that all plant is funded with CIAC. We agree that land can be funded with CIAC as well as any other type of asset. However, because land is assumed to have an infinite service life, it nether depreciates, nor should it be amortized. Thus, we agree that Staff's approach to remove non-depreciable assets from CIAC amortization is appropriate.

Staff has long held its position, and the effect of the parties' difference of opinion is not substantial in this case. Although the Company provides a demonstration of how in theory Staff's position would negatively affect the Company's cash flow, it did not provide sufficient data specific to this case to convince us that the Company is actually harmed.

Thus, on a going-forward basis, we adopt Staff's position on CIAC amortization.

E. Depreciation Methodology

Staff recommends that the Applicants convert from the group depreciation methodology to the individual asset methodology.[59]

Applicants dispute Staff's position in this case that the individual asset method of depreciation is "typically recommended by Staff." Applicants believe that the group depreciation method is the most commonly used depreciation method at the Commission, noting that all of their affiliates utilize the group depreciation method, as do most of the utilities for which Mr. Bourassa, the Applicants' rate consultant, works. Applicants assert that the group method is generally used in conjunction with Staff's "typical and customary" depreciation rates because it is the most administratively efficient

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[58] RUCO Opening Brief at 5.
[59] Staff Opening Brief at 6.

method for keeping track of depreciation.[60]

Applicants state that NARUC requires the use of straight-line depreciation and the removal of retired plant, and that they now have a policy to retire plant and that they use straight-line depreciation. Applicants urge the Commission to continue to authorize the use of the group depreciation method.

RUCO has no issue with the group depreciation method nor with the Applicants' proposed level of accumulated depreciation.[61]

During the course of the hearing in this matter, the issue of depreciation methodology and asset retirements became intertwined.[62] The issue appears to have arisen because the Company was not recognizing retired plant appropriately. Plant balances have now been resolved for ratemaking purposes. As long as the Company properly accounts for plant retirements, the group depreciation methodology appears to be an acceptable methodology which has been used in this jurisdiction. The group methodology is not inconsistent with the requirement to use the straight-line depreciation methodology. Accordingly, we will allow the Company to continue to use the group depreciation methodology, and accumulated depreciation and depreciation expense will be calculated using the group depreciation method.

F. Customer Security Deposits

Staff recommends decreasing the Company's rate base by the Customer Security Deposit balance to reflect that Customer Security Deposits are customer-provided capital. Staff argues that its methodology is one of the methods approved by NARUC. Staff states that during the test year, Bella Vista received $175,850 in Customer Security Deposits, NSWC received $7,972 and SSWC received $22,298, for a total of $206,120. Staff recognizes that under its proposed methodology for treating Customer Security Deposits, the associated interest expense on those deposits is an appropriate operating expense. Staff did not include an associated interest expense in this case because the Applicants did not provide Staff with the appropriate documentation to demonstrate that any interest

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[60] Tr. at 1051.
[61] RUCO Opening Brief at 5.
[62] Tr. at 883-902.

was paid to customers during the test year.[63] Staff argues that it is not acceptable to multiply the ending Security Deposit Balance by the authorized interest rate, or 6 percent, to derive the appropriate interest expense, because that calculation does not arrive at the actual interest expense paid.

Applicants believe that Staff's recommendation to deduct Customer Security Deposits from rate base is another way to lower the utility's rate base, and they argue that Staff did not offer reliable authority that would support Staff's position.[64] Applicants argue that Customer Security Deposits are not like meter deposits or deposits paid by developers for extension of service because: Customer Security Deposits are short-term deposits held by the utility to secure payment for utility service rendered; they do not provide the utility with a source of capital for its own use; and they are required for only certain customers, are held for different lengths of time, and are typically refundable within one year.[65] Applicants agree that the Commission should deduct zero-cost capital from rate base when the utility has beneficial use of the capital in lieu of its own, but also assert that short-term security deposits do not fall into such category of zero-cost capital.[66]

RUCO does not deduct Customer Security Deposits from rate base.[67]

With respect to Customer Security Deposits, the NARUC Rate Case and Audit Manual provides as follows:

> Customer deposits are shown as a liability on the utility's balance sheet and represent a source of non-investor supplied capital. Customer deposits are generally treated one of three ways.
>
> The first method does not reduce rate base by the customer deposits balance and classifies any interest accrued or paid on those deposits as a below-the-line (or non-operating) expense. This method allows the utility to earn a return on a rate base that has not been reduced by the amount of customer deposits, and then allows it to use that return to pay the interest that is required to be returned to customers with the return of that deposit. One consideration in using this method is whether the return allowed on rate base is higher than the return that the utility is required to pay on its customer deposits. If so, the utility may be allowed to earn more than is necessary, and return that difference to shareholders.
>
> The second method reduces rate base by the customer deposits balance,

[63] Staff Opening Brief at 10.
[64] Applicants Initial Opening Brief at 47-48.
[65] *Id.* at 47-48.
[66] *Id.* at 48.
[67] RUCO Final Schedules at SURR RLM-2.

> and classifies any interest accrued or paid on those deposits as an above-the-line (or operating) expense that is included in the revenue requirement computation. The interest that the utility must pay is generally deemed to be a legitimate expense that must be recovered in one form or another.
>
> The third method includes the liability for customer deposits in the utility's capital structure at a zero cost, reducing the overall rate of return. If interest is paid on the customers' deposits, the utility can recover that interest expense as an above-the-line (or operating) expense.

In the LPSCO rate case (Docket No. SW-01428A-09-0103) the Commission opted to adopt Staff's position to deduct Customer Security Deposits from rate base.[68] This position is consistent with NARUC, and recognizes that there are no constraints on the Company's use of these funds which are provided by ratepayers, and that the utility should not be permitted to earn a rate of return on any plant that may be purchased with the non-investor-supplied funds.

We find in this case that Staff's position is reasonable and the Customer Security Deposits should be deducted from rate base. While NARUC also recognizes the Company's position as acceptable, under that approach, if the authorized rate of return is greater than the interest rate the utility is required to pay in deposits, the utility may earn more than is necessary to pay the interest on deposits.

Our acceptance of Staff's position is consistent with the treatment we approved for BVWC's sister utility, LPSCO, and is also consistent with the approved treatment of CIAC or AIAC we have approved in other cases when the utility has argued that non-investor funds that have not yet been used to install plant should not be deducted from rate base. All three of these sources of funds are non-investor-provided capital.

The Company could have provided its actual interest expense related to Customer Security Deposits, but did not do so in this case. In future cases, we may allow interest paid on Customer Security Deposits as a reasonable operating expense if adequate evidence is presented to support such expense.

G. Accumulated Deferred Income Taxes ("ADIT")

Applicants propose an ADIT balance of $572,006 on a consolidated basis. This is a deduction from rate base, which indicates that in the test year, Applicants paid less in taxes than they collected

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[68] Decision No. 72026 at 16-17.

in rates for taxes.

Staff and Applicants do not disagree on the ADIT methodology to use in this case, but Staff recommends a consolidated ADIT of $626,933, which Staff states is due to different plant values. None of the parties disagree on methodology. Because we adopt Staff's plant values, for rate-making purposes, we adopt Staff's ADIT calculation.

H. Summary of Rate Base

Based on the foregoing, we adopt a consolidated rate base of $7,577,710 as shown below:

Plant In Service	$26,505,766
Less: Accumulated Depreciation	10,442,498
Net Plant in Service	$16,063,268
Less:	
Contributions in Aid of Construction	$ 542,445
Less: Accumulated Amortization	(230,987)
Net CIAC	311,458
Advances in Aid of Construction	6,781,443
Service Line and Meter Advances	559,605
Customer Security Deposits	206,120
Deferred income Tax Credits	626,933
Original Cost Rate Base	**$7,577,710**

III. INCOME STATEMENT ADJUSTMENTS

A. Rate Case Expense

The Company proposes a rate case expense of $375,000, to be amortized over three years, for an annual rate case expense of $125,000, on a consolidated basis.[69] Applicants state that this amount reflects a $75,000 downward adjustment from the $450,000 of rate case expense that the Company originally estimated.[70] They note that the expense is for three separate rate applications and a fourth

[69] Applicants Initial Closing Brief at 50.
[70] Applicants Reply Closing Brief at 26.

filing to support the consolidation, and includes substantial amounts of testimony and schedules, discovery and six days of hearings. Applicants state that they will incur more than $375,000 in total rate case expense, but that their shareholders will be responsible for the expenses that exceed the authorized amount.[71]

Staff recommends a total rate case expense of $202,316, and normalizes that amount over three years, resulting in an annual rate case expense of $67,439 on a consolidated basis.[72] Staff compared the requested rate case expense with other multiple system utilities in Arizona and concludes that the requested expense is higher than for similar companies and that a more reasonable expense should be approved. Staff asserts that the Applicants have done little to minimize the components of rate case expense by relying on outside consultants and lawyers.[73]

RUCO claims that the Applicants only provided documentation for actual rate case expenses through February 2010, of $59,206, and an estimate of $450,000 for total rate case expense.[74] RUCO believes the $450,000 estimate to be excessive, and calculated what it believed would be a reasonable expense based on the Company's estimate of rate case expense in the Black Mountain Sewer Co. rate case.[75] RUCO believes that the Black Mountain rate case expense is a valid comparison because although the current case involves the issue of consolidation, after Staff and RUCO filed their direct testimonies, there was no dispute about consolidation and RUCO believes the matter became a typical rate case.[76] RUCO states it did review the actual rate case expense invoices through the filing of Final Schedules, but did not revise its recommendation.[77]

RUCO recommends a total rate case expense of $200,000, and reduces that amount by half in order to share the cost equally with shareholders. RUCO normalized the $100,000 over three years, for a rate case expense of $33,000 per year.[78] RUCO states that in deciding this issue, the Commission must determine whether the Applicants have shown that their rate case expense is

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[71] Applicants Initial Closing Brief at 51.
[72] Staff's Final Schedules at CSB-4.
[73] Staff Opening Brief at 16.
[74] RUCO Closing Brief at 17.
[75] *Id.* at 17-18.
[76] *Id.* at 19.
[77] *Id.* at 20.
[78] *Id.* at 21.

sufficiently documented, reasonable, and necessary to provide utility service. RUCO also suggests that rate case expense is equally beneficial to shareholders, who should bear an equal portion of the expense, and also bear any portion that is considered excessive.[79]

Applicants dispute Staff's claim that the Companies relied excessively on outside consultants, as they used only one outside witness and internally handled data requests. Applicants claim they worked hard after the filing of testimonies to narrow the issues with Staff and RUCO, and those efforts, while increasing some of the rate case expense prior to hearing, ultimately resulted in a lower rate case expense in what was a complex case. They question whether the other dockets cited by Staff involved a consolidation request which required additional testimony and explanation, how big the other systems were, and whether they had the same background as the McLain systems. Applicants argue that the fact that consolidation was not contested in this case did not relieve them of their obligation to make a record or reduce the amount of paperwork. Applicants argue that RUCO also failed to rebut their request with substantial evidence and has not met its own burden to show that its recommended rate case expense of $100,000 normalized over three years is reasonable.[80]

The rate case expense in this proceeding was complicated by the issues of consolidation. Additional testimony and schedules were required, even if the issue was not contested. Furthermore, this is the first rate case since APUC gained ownership of NSWC and SSWC. Although the parties were able to reach agreement on a number of issues, there were significant issues that were submitted for resolution and the parties worked behind the scenes to narrow issues and correct schedules. The record does not support a finding that Applicants relied unduly on outside consultants. Comparison with other proceedings offers some guidance on what is reasonable, but the individual circumstances of each case must also be considered.

In addition to the foregoing factors, we also consider the size of the utility and which stakeholders benefit from the requested relief. In this case, the BVWC customer base of less than 10,000, is relatively small compared to some of the other entities we regulate who use a shared services model. While we acknowledge that both ratepayers and shareholders will benefit from

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[79] *Id.* at 17 and 21.
[80] Applicants Reply Closing Brief at 29.

consolidation, given the relatively small customer base, in this case, it is reasonable for shareholders to bear more of the cost of the docket than has been proposed by Applicants.

Thus, under these circumstances, we find that a consolidated rate case expense of $300,000 normalized over three years, for an annual rate case expense of $100,000, is reasonable.

B. Central Office Cost Allocation

Applicants' parent uses a shared services model, which includes the allocation of the costs incurred by APUC's operating affiliate, APT, to its regulated and non-regulated subsidiaries. [81]

There is no dispute in this proceeding about the allocation of Liberty Water expenses. Liberty Water provides day-to-day operations to the Applicants and its other regulated utilities.[82] Liberty Water charges operations and engineering personnel at cost, based on the employee's hourly rate, grossed up by 35 percent for obligations such as taxes, benefits, retirement and insurance. Costs which cannot be allocated on an hourly basis are allocated based on the relative customer counts of the regulated utilities. Overhead costs are allocated based on a "four factor" methodology that considers relative size based on total plant, total customers, expenses and labor.[83]

APT provides financial, strategic management, compliance, administrative and support services to the Liberty Water utilities, as well as to APUC's unregulated facilities. The APT office is located in Oakville, Ontario, Canada. According to the Company, APT's executive management and administrative support includes accounting and finance, human resources, employee benefits, regulatory and information systems services. Applicants argue that the APT services are necessary to allow BVWC and the other Liberty Water utilities to have access to capital markets for capital projects and operations, and are necessary for BVWC to provide a high level of service at the lowest cost. The Applicants state that no direct labor costs are included in the Central Office Cost allocation from APT, but instead the costs include professional services like third-party legal services, accounting services, tax planning and filings, and required audit services. The headquarters administrative costs also include costs for licenses, fees and permits, information technology/systems, payroll and HRIS maintenance contracts, as well as rent and depreciation of office furniture,

[81] The APT Costs can be referred to as the Central Office Cost Pool, Central Office Costs or APT Costs.
[82] Ex A-18, Eichler Reb. at 4, and Ex PE-RB-1.
[83] Ex A-18 at PE-RB-1.

equipment and computers in the Ontario central office.

APUC allocates the Central Office Costs to BVWC in two phases. The first phase allocates the costs to Liberty Water, based on the number of regulated and unregulated facilities. In the second phase, Liberty Water allocates the Central Office Costs between BVWC and its other regulated utilities based on customer counts. The Applicants' total adjusted APT Central Office Cost pool is $3,567,363.[84] Applicants allocate 75.71 percent of the Central Office Cost pool to APUC and its unregulated facilities (46 facilities), and 24.29 percent to Liberty Water's utilities (17 regulated utilities, including the three applicants). Of the $866,360 that the Applicants allocate to the 17 regulated utilities, 14.52 percent, or $125,830, is allocated to the consolidated BVWC companies.[85]

Applicants claim the Central Office Costs are incurred for the benefit of all the regulated utilities and their customers, and are not capable of being directly charged to the separate operating assets.[86] They claim that they have shown that BVWC's customers benefit from the APT services from access to capital financing, reduced operating costs and sound fiscal management.[87] Applicants argue that the remediation of the McLain systems demonstrates the benefits of the Liberty Water model, as Liberty Water was able to invest substantial capital in the systems to resolve problems and render high quality utility service. Applicants state that the former McLain systems would not have access to the capital from the TSX without the APT costs.

Applicants also argue that the APT costs are nominal, with a per customer cost of $1.09 per month or $13.08 per year.[88] Applicants state that among 23 comparable water companies, BVWC ranks 8th in terms of total operating costs, and that its operating cost per customer of $396.77 is substantially less than the average cost for the 23 comparable companies, which was $467.91.[89] Finally, Applicants argue the Commission should approve the APT cost allocations because the Commission has approved the corporate cost allocation models used by Global Water and Arizona-American, which they claim mirror Liberty Water's model.[90]

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[84] Applicants' Final Schedule C-2, page 8.
[85] Applicants Initial Closing Brief at 22.
[86] Ex A-18, at PE-RB1.
[87] Tr. at 381-391.
[88] Ex A-18 at 16-18; Exhibit PE-RB3; Tr. at 390-92.
[89] Tr. at 392-93; Ex A-18 Exhibit PE-RB4; Ex A-19, Eichler RJ at 14, Exhibit PE RJ3.
[90] Applicants Initial Closing Brief at 22.

RUCO believes that the requested APT costs are unreasonable, unnecessary to provide utility service, insufficiently documented and were not useful or otherwise beneficial to ratepayers.[91] RUCO argues that the Applicants did not demonstrate that they allocated the APT costs to the regulated affiliates in a manner consistent with NARUC guidelines.

RUCO also argues that because APUC generates revenues predominantly from its unregulated activities, closer scrutiny of affiliate transactions is warranted.[92] RUCO disagrees that all of the APT costs are indirect costs which should be shared by all subsidiaries.[93] RUCO's witness believes that the invoices are inadequate to determine whether the costs relate to direct costs which should be allocated to a specific utility, or whether they are indirect or common costs which can be allocated to all affiliates. RUCO also argues that the APT costs should be excluded because the Applicants have not demonstrated that the costs are necessary to provide utility service. RUCO asserts that "the Company has failed to demonstrate how the APT costs contributed to the improvement of BVWC or are beneficial to the Arizona ratepayers."[94]

Further, RUCO argues the APT costs should be excluded because Applicants have not demonstrated that the billings from affiliates are at the lesser of market or cost as required under the NARUC Guidelines regarding Cost Allocations and Affiliate Transactions.[95] RUCO believes that the rent paid by APT to Bristol Circle Partners requires extra scrutiny because Bristol Circle Partners is owned or controlled by the same individuals who are also APT managers. RUCO states that in response to data requests, Applicants provided information about market rents, but did not provide information about the costs to purchase or construct the building, which RUCO claims is necessary to determine if the rent expense is the lower of cost or market.

Consequently, RUCO reduced the APT pool by $3.68 million, and recommended allocating only expenses related to tax, audit, depreciation and legal. However, due to RUCO's position that documentation was inadequate, RUCO only allocated 25 percent of the tax, audit, depreciation and

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[91] RUCO Closing Brief at 8.
[92] Tr. at 712-717; RUCO Closing Brief at 10.
[93] RUCO Closing Brief at 9.
[94] Tr. at 712-717; RUCO Closing Brief at 11.
[95] RUCO Closing Brief at 11-13.

legal costs, or $416,941,[96] and then allocated 25.35 percent of that amount to the Liberty Water regulated entities. RUCO then allocated the Liberty Water portion to the regulated entities based on customer counts, which resulted in an allocation of $15,352 to BVWC on a consolidated basis.[97]

RUCO believes that a better methodology for allocating APT Central Office Costs would be to bill utilities for direct costs and allocate indirect costs on a revenue basis rather than treating each facility the same regardless of revenue or customer size.[98] RUCO states that in the test year, the revenue of all APT affiliates was $218,000,000, while during the same period, BVWC's total revenue was $4,023,022. According to RUCO, dividing BVWC's total test year book revenue by the total revenue of APT affiliates results in an allocation factor of 1.84 percent based on revenue.[99]

RUCO is concerned that the Applicants are attempting to shift the burden of proof that its expenses are reasonable by claiming that Staff and RUCO have not shown that they are unreasonable with "substantial evidence."[100] RUCO argues that the Commission has rejected the contention that RUCO has the burden of disproving expenses, and once a party challenges the company's position with "some credible evidence," it is incumbent on the utility to demonstrate the reasonableness of its proposals.[101] RUCO further asserts that there is no presumption of reasonableness in favor of the utility.[102]

Staff recommends $3,132 be allocated to each utility, for a total allocation of $9,672.51 on a consolidated basis.[103] Staff does not agree that all of the costs that the Applicants include in the cost pool should be allocated to the regulated subsidiaries. Staff states that it reviewed the underlying invoices and determined that the Applicants had not identified the costs as direct or indirect as required by the NARUC Guidelines of Cost Allocation and Affiliate Transactions. From its review, Staff believed that almost all of the costs were attributable to the operations of APUC or one of its affiliates. As a result, Staff assigned 90 percent of the Central Cost Pool to APUC, and allocated the

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[96] *Id.* at 15.
[97] RUCO's Final Schedules.
[98] RUCO Closing Brief at 14.
[99] *Id.* RUCO does not believe the 1.84 allocation factor should be applied to the entire APT pool because RUCO does not believe that Applicants adequately documented the costs.
[100] RUCO Reply Brief at 3.
[101] Decision No. 68487 (February 23, 2006).
[102] *See* Decision No. 68487 at 21-22.
[103] Staff Opening Brief at 16.

other 10 percent to APUC's subsidiaries.[104] Staff believes that the driving force behind most of the costs is to advance the interests of the parent.[105] Staff further believes that the amounts allocated to the regulated entities should not exceed the amounts the regulated entities would incur on a stand-alone basis. Staff argues that when costs incurred primarily for the benefit of an unregulated affiliate are allocated as overhead/common costs, the costs of the unregulated entity are unfairly shifted to the captive customers of the regulated utility.

Staff also disagreed with the formula Applicants used to allocate the common costs. Staff recommends an allocation factor of 1/70.5 or 1.42 percent.[106] Staff argues that APUC has to perform some type of monitoring of its interests in affiliate companies even if it does not have an equity interest in the facility.[107] Staff argues that the Applicants' entire argument in support of the cost pool and its allocation ignores the ratemaking principles underlying recovery of expenses, i.e., were the expenses incurred reasonable and necessary for the provision of service to ratepayers? Staff believes that the Company has not adequately demonstrated that all of the costs in the pool are related to providing service to its ratepayers.[108]

Staff states that it is not opposed to the concept of a shared services model, but has concerns that any excessive costs be disallowed. Staff urges the Applicants to review the cost pool and only include those expenses that are necessary to provide services to the ratepayer.

Applicants argue that Staff has not articulated any reason that the allocation method is unfair.[109] They assert that Staff and RUCO are being arbitrary and excessive by presumptively disallowing the majority of the APT costs.[110] Applicants assert that BVWC provides high quality service at reasonable and low operating costs, and argue that Staff and RUCO fail to meet their burden of proof to support their disallowance. Applicants believe that neither Staff nor RUCO rebut the Applicants' showing that the APT costs are necessary under a shared services model.[111]

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[104] *Id.* at 13.
[105] *Id.* at 14.
[106] Staff based its calculation on an average of 70.5 facilities based on the APUC 2007 and 2008 Annual Reports which list 70 and 71 facilities owned.
[107] Staff Opening Brief at 13.
[108] Staff Reply Brief at 9.
[109] Applicants Initial Closing Brief at 27.
[110] *Id.* at 31.
[111] *Id.* at 23-24.

Applicants argue that it is undisputed that BVWC could not obtain capital from the capital markets without incurring the APT costs. Thus, Applicants claim there is a direct benefit to BVWC from the services provided by APT, and BVWC should pay its share of the APT costs. Applicants assert that it is incorrect to claim that BVWC could obtain capital from the TSX without the incurrence of the APT costs. Applicants note that BVWC must be part of the parent company's consolidated audits and tax services in order to receive funds from stock sales on the TSX. If, as Staff and RUCO suggest, APUC should use its access to capital markets to the benefit of BVWC, then, Applicants argue, fairness requires that BVWC share in the costs to obtain that capital.

The APT Cost Pool allocation to the Liberty Water affiliates has been at issue in every Liberty Water utility rate case. As the parties have reviewed the costs that have been included in the Central Cost Pool, they have identified certain expenses that should have been directly billed to one or another of APUC's facilities, as well as expenses which were not adequately documented or not appropriate to be recovered from utility ratepayers. Each rate case has refined the process. When invoices have been identified as being direct expenses of a particular affiliate, those costs have been removed from the Central Cost Pool. As of this BVWC rate case, the invoices have been thoroughly reviewed. In this case, Staff and RUCO have not identified any particular invoices in the remaining APT Cost Pool which should be directly charged to a particular facility other than BVWC, or expenses that should not be charged to ratepayers such as the "hootenanny" at issue in the RRUI rate case (Docket No. WS-02676A-09-0257).

As the Commission recognized in the Black Mountain, LPSCO and RRUI dockets,[112] the Liberty Water regulated utilities receive a direct benefit from the activities of APUC and APT in connection with APUC's activities related to its listing on the TSX and its resultant access to capital. Therefore, as we found in these other Liberty Water utility rate cases, the APT Central Cost Pool expenses related to the parent's ability to access the capital markets should be allocated to the regulated utilities in a reasonable manner.

We continue to find that the Applicants' two part methodology of allocating the authorized

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[112] Decision No. 71865 (September 1, 2010) (Black Mountain); Decision N. 72026 (December 10, 2010) (LPSCO); and Decision No. 72059 (January 7, 2011) (Rio Rico).

APT Central Cost Pool costs to the regulated utilities is reasonable. We also find in this case that the Applicants have met their burden to demonstrate that APT Central Office Cost related to audit, tax, legal, and license fees and permits are necessary expenses for APUC to be listed on the TSX and to access capital. Consistent with past decisions, we find that escrow fees, trustee fees and shareholder communication fees are related to activities that primarily benefit shareholders and are appropriately disallowed for ratemaking purposes.

Applicants bear the burden of proof to demonstrate that the regulated utility received a direct benefit from the APT Costs. Because of the lack of records demonstrating the activities of the APT managers, the Applicants have not demonstrated what proportion, if any, of the APT management fees are appropriately allocated to the regulated utilities. Applicants must demonstrate that the regulated utilities received a benefit from the activities of the managers and that those activities were not duplicative of the services provided by the Liberty Water managers.

Additionally, the common costs sought to be allocated to the regulated utilities must be reasonable based on the size of the utility. A small utility in southern Arizona may not need financial and strategic planning expertise beyond that provided by the Liberty Water personnel. Applicants have not convinced us that BVWC ratepayers should be responsible for the Central Office Costs related to rent, office expenses and depreciation associated with the Ontario office.

Thus, we continue to adopt the general allocation methodology we most recently approved in the RRUI rate case, as follows:

1. Allowable common APT expenses for BVWC in this case shall be limited to audit, tax, legal and license fees and permits;
2. The allowable common costs shall be allocated to Liberty Water affiliates based on the number of regulated Liberty Water companies (15) divided by the total number of companies owned or operated by (68), i.e. 22.05 percent;[113]
3. The Liberty Water allocation shall be further allocated to BVWC on the

[113] Because we approve the consolidation of the three companies into one entity, for purposes of allocating the APT Central Office Costs, it is reasonable to utilize the configuration of the Company after consolidation.

basis of the percentage of consolidated BVWC customers to the total number of Liberty Water customers. For the 2008 test year, BVWC represented 14.52 percent of Liberty Water's total customers.

In the test year, the total APT Central Office costs associated with audit, tax, legal and license fees and permits was $1,303,712.[114] Of that amount, 22.05 percent, or $287,468, is allocable to Liberty Water; of the Liberty Water amount, 14.52 percent, or $41,740, is applicable to BVWC.

C. Liberty Water Outside Services

Staff reduced Outside Services expense by $36,038 related to the Company's adjustment to annualize increased employee costs at Liberty Water.[115] Staff averaged the Liberty Water Outside Services expense for 2008 and 2009 to mitigate the effect of the Company not using competitive bids.[116]

The Company does not believe that a "competitive bid" standard is the measure by which these costs should be determined to be reasonable, but rather asserts that the standard should be whether Liberty Water unreasonably compensates its employees.[117]

Ms. Brown testified that the Companies did not present Staff with sufficient evidence for Staff to determine if the increased costs were justified or market based.[118] Neither party addressed this issue in their closing briefs, although the issue was discussed in written testimony and the Company raised the issue in its "Request for Corrections to Recommended Opinion and Order" filed on March 24, 2011. For the purposes of this rate case, we adopt Staff's adjustment. Staff averaged the 2008 and 2009 Liberty Water Outside Services expense to determine an appropriate expense level. Based on the record in this proceeding, Staff's adjustment is reasonable.

D. Income Statement Summary

Based on the foregoing, we find BVWC's adjusted test year revenues to be $4,162,136 and its adjusted test year expenses to be $3,955,520, which results in test year adjusted operating income of $206,615, for a return of 2.73 percent on the test year FVRB of $7,577,710.

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[114] Applicants' Final Schedules, BVWC Consol. at C-3, page 8.
[115] Ex A-13 Bourassa Consolidated Dir at 11 and Sch C-2 at 8; Ex S-6 at 39.
[116] Ex S-7 at 27-30.
[117] Ex A-14 Bourassa Rb at 29.
[118] Ex S-6 at 39.

IV. COST OF CAPITAL

The parties' positions on the cost of capital components are summarized as follows:

	Cost of Debt	Cost of Equity	WACC
Applicants[119]	6.28%	10.9%	9.85%
RUCO[120]	6.27%	9.0%	8.42%
Staff[121]	6.3%	9.3%	8.8%

The cost of capital is the opportunity cost represented by anticipated returns that are foregone by choosing one investment over another, or, in other words, the return that investors expect from a venture.[122] The WACC is the average of the cost rates on all issued securities adjusted to reflect their relative amounts in the company's capital structure.[123] Thus, the WACC for a particular company is determined based on the cost of its debt and the cost of its equity, multiplied by the proportion of the debt and equity that comprise its total capital.

The cost of debt is determined by the interest rate of the company's debt instruments. The cost of equity ("COE") is determined by the market, and represents investors' expected returns, not realized accounting returns.[124] The COE is estimated using various methodologies, most commonly, and in this case, witnesses used the Discounted Cash Flow ("DCF") method and the Capital Asset Pricing Model ("CAPM"). Despite using the same basic methodologies, as is often the case, witnesses derive differing results due to their use of different assumptions and inputs. The witnesses used a representative sample group of publicly traded utilities to estimate the COE for BVWC.

The DCF uses the present value of the current average market price of the sample group and shareholder expected future cash flows (primarily dividends) to determine the stock value of the subject utility.[125] The CAPM model describes the relationship between a security's investment risk and its market rate of return.[126]The CAPM assumes that investors require a return that is

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[119] Applicants Final schedules – consol., C-2 at p 9.
[120] RUCO Final Schedules, COC, WAR-1.
[121] Staff's Final Schedules at PMC-1; Staff Opening Brief at 19.
[122] Ex S-1, Chavez Dir. at 4.
[123] *Id.*
[124] *Id.* at 10.
[125] *Id.* at 15.
[126] *Id.* at 27.

commensurate with the level of risk associated with a particular security.[127] Under the CAPM, the expected return is equal to the risk-free interest rate plus the product of the market risk premium, multiplied by beta, where beta represents the riskiness of the investment relative to the market.[128]

In this case, Applicants seek a rate of return on rate base using a WACC of 9.85 percent. Applicants calculate the WACC using the consolidated capital structure at the end of the test year, which consisted of 77.4 percent equity and 22.6 percent debt. Applicants recommend a cost of debt of 6.28 percent based on the average debt costs for Bella Vista, as NSWC and SSWC do not have any debt. Applicants request a COE of 10.9 percent based on its witness, Mr. Bourassa's, analysis.[129]

Mr. Bourassa utilized the DCF and the CAPM, which the Commission has relied upon in numerous rate cases. Mr. Bourassa adjusted the COE produced by his DCF and CAPM calculations downward by 60 basis points to account for the lower debt level in the Applicants' capital structure as compared to the sample group, and then adjusted the COE upward by 50 basis points to account for: the Applicants' small size relative to the proxy companies; the Companies' lack of investment liquidity; and additional risks that the Applicants believe result from the particular rate-making methods employed in Arizona.[130]

RUCO utilized a capital structure consisting of 21.08 percent debt and 78.92 percent equity, which is RUCO's calculation of the capital structure at the end of the test year.[131] RUCO recommends a cost of equity of 9.0 percent.[132] RUCO also performed a DCF and CAPM analysis and recommends a cost of equity that is at the high end of the ranges of its analyses. RUCO utilized samples of publicly traded water and natural gas providers.

According to RUCO, the Applicants' proposed COE is overstated because it is based upon a CAPM analysis which relies on a high market risk premium, ignores the geometric mean of market returns, and uses a long-term treasury instrument which RUCO contends inflates the market risk premium.[133] RUCO argues that its own methodology that uses the geometric mean and the five-year

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[127] *Id.* at 27-28.
[128] *Id.* at 28.
[129] Applicants Initial Opening Brief at 52.
[130] *Id.* at 53.
[131] RUCO's Final Schedules WAR-1.
[132] *Id.* at 22.
[133] Ex RUCO-8 at 21.

treasury rate is a more accurate method to calculate market risk premium.[134] RUCO opposes the attempt to apply a small company risk premium because BVWC received all of its capital from its parent, which does not suffer from the alleged small firm risks.[135] RUCO also argues that its use of a historic market risk premium to derive a COE is more reliable than the Applicants' approach of using analyst projections of market return because RUCO believes that past performance is a better indicator of future performance than analyst projections.[136]

Staff recommends a capital structure for the consolidated companies consisting of 18.7 percent debt and 81.3 percent equity, a Cost of Debt of 6.3 percent, and a COE of 9.3 percent, which results in an overall rate of return of 8.8 percent.[137] Staff updated the Company's capital structure to March 31, 2010.[138]

Staff argues that its recommended 9.3 percent COE is based on sound and well-accepted methodologies that have consistently been utilized by the Commission. Staff used two versions of the DCF Model, the constant growth DCF and the multi-stage DCF. Staff recommends against heavy reliance on analysts' forecasts, and states that its DCF methodology gives equal weight to historic data and analysts' forecasts. Staff's overall CAPM COE is 10.6 percent, and includes both Staff's CAPM estimate using the historical market risk premium (8.6 percent) and the current market risk premium CAPM (12.5 percent).

Staff utilized the Hamada Method to adjust the COE downward by 100 basis points to account for the Applicants' lower financial risk from having less debt than the sample companies. Staff acknowledges that the Hamada methodology was originally developed utilizing market values of equity rather than book values, but argues that the use of book values to estimate the financial risk adjustment "is prudent and reasonable in a regulatory environment."[139] Staff also argues that using the average beta of the sample utilities is appropriate because there is no basis to assume that the Company would have a higher beta than the sample as the market does not reward unique risk

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[134] RUCO Closing Brief at 25.
[135] *Id.* at 22.
[136] *Id.* at 24.
[137] Staff Opening Brief at 19.
[138] Ex S-2, Chavez Surr. at PMC-9.
[139] *Id.* at 21.

because it can be diversified away.[140]

Staff argues that firm-specific risk is not relevant to determining the COE. Staff asserts that the Companies are less risky than the sample water companies, and also that there is no evidence that Arizona has a less favorable regulatory environment than the sample companies. Staff notes that the Commission has consistently rejected proposals for a "small firm risk premium." Staff believes that an important factor in this case is that Applicants are subsidiaries of a publicly traded company and have access to the capital markets, which removes the main thrust for why a small firm risk premium would otherwise be needed.

Applicants assert that Staff's DCF methodology double counts historic growth rates and that RUCO's sample group is flawed because it includes gas distribution companies in addition to water utilities.[141] Applicants believe that Staff's Hamada adjustment is overstated because Staff did not adjust beta due to the difference in size between the Applicants and the larger sample companies and because Staff uses book value, when Applicants believe that a market value is more appropriate.

We find that the capital structure at the end of the test year, consisting of 77.4 percent equity and 22.6 percent debt is appropriate. This capital structure most closely matches the adjustments adopted herein. There is no precise number for the appropriate COE, rather we use estimates based on judgment calls of what inputs are most reasonable. We find that in this case, a COE of 9.5 percent and cost of debt of 6.28 percent is reasonable. This COE is the same cost that the Commission approved in the recently concluded RRUI rate case.[142] RRUI is BVWC's sister utility, and while the COE in the RRUI rate case was the result of a compromise in that docket, the agreed 9.5 percent COE is within the ranges of returns that have been recommended in this case. In addition, the capital structure agreed upon in the RRUI matter (80 percent equity and 20 percent debt) is similar to the actual capital structure in this case. Consequently, we approve a WACC of 8.8 percent as follows:

	Amount	%	Cost	WACC
Debt	$2,697,323	22.6%	6.28%	1.4%
Equity	5,812,207	77.4%	9.5%	7.4%

[140] Staff Reply Brief at 10.
[141] *Id.* at 55.
[142] Decision No. 72059 at 33.

Total	7,509,530	100.0%	8.8%

V. REVENUE REQUIREMENT

Based on our findings herein, we determine that BVWC is entitled to a gross revenue increase of $760,150, or 18.26 percent.

FVRB	$7,577,710
Adjusted Operating Income	$206,615
Required Rate of Return	8.8%
Required Operating Income	$666,838
Operating Income Deficiency	$460,223
Gross Rev. Conv. Factor	1.65170
Gross Revenue Increase	$760,150
Adjusted Test Year Revenue	$4,162,136
Approved Annual Revenue	$4,922,286
Percentage Revenue Increase	18.26%

VI. RATE DESIGN, HOOKUP FEE TARIFF, LOW INCOME TARIFF AND ENGINEERING ISSUES.

A. Rate Design

Based on their revenue requirements, the parties proposed the following rates and charges for the consolidated BVWC:

	Current	Proposed Rates		
	Bella Vista[143]	Company[144]	RUCO[145]	Staff[146]
MONTHLY USAGE CHARGE:				
5/8" x ¾" Meter	$15.00	$17.00	$15.55	$12.00
¾" Meter	22.70	25.50	23.32	12.00
1" Meter	28.10	38.25	34.98	25.00

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143 The monthly service charge for SSWC and NSWC 5/8" x ¾" meters is $31.00 and the service charges for larger meters are also higher than the corresponding charges for BVWC.

144 Applicants' Final Schedules at H-3.

145 RUCO's Final Schedules at RLM-RD1.

146 Staff's Final Schedules at CSB-7 RD.

1 ½" Meter	34.50	76.50	69.96	50.00
2" Meter	42.25	95.20	87.06	80.00
3" Meter	121.90	150.40	174.12	160.00
4" Meter	173.00	318.75	291.50	250.00
6" Meter	950.00	850.00	777.34	500.00
8" Meter	1,295.00	1,360.00	1,243.75	880.00
Commodity Rates – per 1,000 gallons				
5/8" x ¾" Meter – Residential				
0- 5,000 gallons	$0.97	N/A	N/A	N/A
5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A
0- 4,000 gallons	N/A	$1.79	$1.714	$0.90
4,000 gallons to 10,000	N/A	2.39	2.5816	2.00
Over 10,000 gallons	N/A	2.94	3.3624	3.526
5/8" Meter - Commercial				
0- 5,000 gallons	$0.97	N/A	N/A	N/A
5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A
0- 4,000 gallons	N/A	2.09	1.5318	2.00
Over 4,000 gallons	N/A	2.89	2.3994	3.526
¾" Meter - Residential				
0- 5,000 gallons	$0.97	N/A	N/A	N/A
5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A
0- 4,000 gallons		1.79	1.7140	0.90
4,000 gallons to 10,000	N/A	2.39	2.5816	2.00
Over 10,000 gallons	N/A	2.94	3.3624	3.526
¾" Meter - Commercial				
0- 5,000 gallons	$0.97	N/A	N/A	N/A
5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A
0- 4,000 gallons	N/A	2.09	1.5318	2.00
Over 4,000 gallons	N/A	2.89	2.3994	3.526
1" Meter – All Classes (except standpipe)				
0- 5,000 gallons	$0.97	N/A	N/A	N/A
5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A

0 to 10,000 gallons	N/A	2.09	1.5318	2.00
Over 10,000 gallons	N/A	2.89	2.3994	3.526
1 ½" Meter – All Classes (except standpipe)				
0- 5,000 gallons	$0.97	N/A	N/A	N/A
5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A
0 to 25,000 gallons	N/A	2.09	1.5318	N/A
Over 25,000 gallons	N/A	2.89	2.3994	N/A
0 to 29,000 gallons	N/A	N/A	N/A	2.00
Over 29,000 gallons	N/A	N/A	N/A	3.526
2" Meter – All Classes (except standpipe)				
0- 5,000 gallons	$0.97	N/A	N/A	N/A
5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A
0 to 50,000 gallons	N/A	2.09	1.5318	2.00
Over 50,000 gallons	N/A	2.89	2.3994	3.526
3" Meter – All Classes (except standpipe)				
0- 5,000 gallons	$0.97	N/A	N/A	N/A
5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A
0 to 80,000 gallons	N/A	2.09	1.5318	N/A
Over 80,000 gallons	N/A	2.89	2.3994	N/A
0 to 115,000 gallons	N/A	N/A	N/A	2.00
Over 115,000 gallons	N/A	N/A	N/A	3.526
4" Meter – All Classes (except standpipe)				
0- 5,000 gallons	$0.97	N/A	N/A	N/A
5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A
0 to 350,000 gallons	N/A	2.09	1.5318	N/A
Over 350,000 gallons	N/A	2.89	2.3994	N/A
0 to 188,000 gallons	N/A	N/A	N/A	2.00
Over 188,000 gallons	N/A	N/A	N/A	3.526
6" Meter – All Classes (except standpipe)				
0- 5,000 gallons	$0.97	N/A	N/A	N/A

5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A
0 to 450,000 gallons	N/A	2.09	1.5318	N/A
Over 450,000 gallons	N/A	2.89	2.3994	N/A
0 to 394,000 gallons	N/A	N/A	N/A	2.00
Over 394,000 gallons	N/A	N/A	N/A	3.526
8" Meter – All Classes (except standpipe)				
0- 5,000 gallons	$0.97	N/A	N/A	N/A
5,000 – 25,000 gallons	1.89	N/A	N/A	N/A
Over 25,000 gallons	2.41	N/A	N/A	N/A
0 to 720,000 gallons	N/A	2.09	1.5318	N/A
Over 720,000 gallons	N/A	2.89	2.3994	N/A
0 to 642,000 gallons	N/A	N/A	N/A	2.00
Over 642,000 gallons	N/A	N/A	N/A	3.526
Standpipe (hydrant, bulk)	N/A	2.94	3.3624	3.526

Mr. Bourassa prepared a Cost of Service Study ("COSS") for BVWC. A cost of service study analyzes the adequacy of water revenues and the revenue requirements to be met by each class of customers.[147] A study allocates plant and expenses into cost and asset functions which are then allocated to customer classifications, and attempts to identify the costs of serving the customer classes. On a consolidated basis, Mr. Bourassa's COSS indicated that the monthly minimum for the 5/8 residential meter class should be $33.13.[148]

Applicants note that under all three parties' consolidated rates, there will be a single tariff for all customers, irrespective of which system they are on; all use an inverted tier rate design with three tiers for the 5/8 inch residential meters and two tiers for the larger residential, commercial and irrigation customers. However, Applicants believe that Staff's rate design moves collection of revenue away from small residential customers, not only to promote water conservation, but to artificially keep rates low for small residential customers.[149] The Company is concerned that despite

[147] Ex A-7 Bourassa Dir Bella Vista at 14.
[148] Ex A-13 Bourassa Dir Consolidated at 23.
[149] Ex A-16 Bourassa Rj at 29.

Staff recommending a 10.6 percent increase, under Staff's rate design, 77 percent of the Company's customers would experience a 2.5 percent decrease and will pay a rate of return on rate base of less than 2.5 percent, as compared to commercial customers that would be paying a return of over 24 percent.[150] Applicants believe that Staff could not substantiate any problems with the Company's COSS,[151] and claim that when Mr. Bourassa modified his study in response to Staff's criticisms, there was no appreciable impact on returns.[152]

Applicants also claim that Staff's rate design will increase the risk of revenue erosion.[153] Applicants argue that their proposed rate design promotes conservation through principles that recognize cost of service, gradualism and fundamental fairness, and send the right price signal to customers about the need to conserve water.[154]

Staff states that it recommends a rate structure that recognizes the growing importance of managing water as a finite resource and promotes more efficient water use. Staff also claims that its rate structure provides an economic benefit to customers who limit consumption.

Staff believes the Applicants' COSS overstates the costs allocated to the residential customer class. Specifically, Staff disputed allocating 100 percent of the costs of rental, health and life insurance, regulatory commission expense, rate case expense and miscellaneous to the Customer Function.[155] Moreover, Staff notes that the COSS is a guideline and tool for designing rates, but that there are other important rate making principles that influence the rate design, such as gradualism, promoting efficient use, and uniformity among customer classes.[156]

RUCO states that its stand-alone rate design allocates required revenue between residential, commercial and industrial ratepayers in the same percentages as the Company, but reflects RUCO's recommended revenue requirements.[157] RUCO does not oppose the Applicants' proposed consolidated rate design, but offers two alternatives—"Option F" and "Option G" which RUCO

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[150] Applicants Initial Closing Brief at 58.
[151] Tr. at 1001.
[152] Ex A-16 at 31-34; Tr. at 1042-1044.
[153] *Id.* at 37-38.
[154] Applicants Initial Closing Brief at 59.
[155] Staff Opening Brief at 18.
[156] *Id.*
[157] RUCO Closing Brief at 7.

claims mitigate rate shock while also ensuring ratepayers in NSWC and SSWC systems do not garner an unearned benefit at the expense of Bella Vista's ratepayers.[158]

Under RUCO's Option F, the average residential Bella Vista customer would incur an increase of $2.70 (based on RUCO's recommended revenue requirement) and bear some of the costs of the other two systems. In the event the Commission wishes to reduce Bella Vista's "subsidy" of the NSWC and SSWC system, RUCO proposed its Option G. Under Option G, all systems would have the same basic rates, but NSWC and SSWC ratepayers would pay a surcharge bringing their rates up to a level equal to their current rates and the average Bella Vista customer would pay a $0.35 increase (after all credits) instead of the $2.70 subsidy under Option F.[159]

Although we appreciate the spirit of RUCO's Option G, we believe that it may cause confusion and lead to charges of discriminatory treatment from ratepayers. As discussed in our consideration of the consolidation issue, all of the systems, including the Bella Vista system, receive benefits from consolidation and we believe the rates we approve herein are fair and equitable to all ratepayers.

The current monthly service charge for Bella Vista 5/8" x ¾" residential customer is $15.00, and for SSWC and NSWC customers it is $31.00. Staff recommended a monthly service charge of $12.00, which is lower than any system's current monthly service charge. We agree that that although it is appropriate to set the fixed portion of the bill at a level that allows the Company to collect approximately 30-50 percent of its authorized revenues, in this case, moving the monthly service charge from $31.00 to Staff's recommended $12.00 would be too abrupt of an adjustment. Accordingly, we believe that maintaining the $15.00 charge for the 5/8" x ¾" residential Bella Vista customers and reducing the NSWC and SSWC monthly service charge to $15.00 is appropriate at this time.[160] Thus, based on the revenue requirement we authorize herein, we approve the following rates and charges:

. . .

[158] *Id.* at 7 and 30.
[159] *Id.* at 31.
[160] Under these rates, 55.96 percent of revenue is generated from the fixed charge.

MONTHLY CUSTOMER CHARGE:

5/8" x ¾" Meter	$15.00
¾" Meter	15.00
1" Meter	35.00
1 ½" Meter	70.00
2" Meter	120.00
3" Meter	240.00
4" Meter	375.00
6" Meter	750.00
8" Meter	1,200.00

Commodity Rates – per 1,000 gallons

5/8" x ¾" Meter – Residential	
0- 4,000 gallons	$1.45
4,000 gallons to 10,000	2.21
Over 10,000 gallons	2.72
5/8" Meter - Commercial	
0- 4,000 gallons	2.21
Over 4,000 gallons	2.72
¾" Meter - Residential	
0- 4,000 gallons	1.45
4,000 gallons to 10,000	2.21
Over 10,000 gallons	2.72
¾" Meter - Commercial	
0- 4,000 gallons	2.21
Over 4,000 gallons	2.72
1" Meter – All Classes (except standpipe)	
0 to 10,000 gallons	2.21
Over 10,000 gallons	2.72
1 ½" Meter - All Classes (except standpipe)	
0 to 26,000 gallons	2.21
Over 26,000 gallons	2.72
2" Meter – All Classes (except standpipe)	
0 to 45,000 gallons	2.21
Over 45,000 gallons	2.72
3" Meter – All Classes (except standpipe)	
0 to 98,000 gallons	2.21

Over 98,000 gallons	2.72
4" Meter – All Classes (except standpipe)	
0 to 158,000 gallons	2.21
Over 158,000 gallons	2.72
6" Meter – All Classes (except standpipe)	
0 to 327,000 gallons	2.21
Over 327,000 gallons	2.72
8" Meter – All Classes (except standpipe)	
0 to 584,000 gallons	2.21
Over 584,000 gallons	2.72
Standpipe (hydrant, bulk)	2.72
Fire Sprinklers – 4 inch	Note 1
Fire Sprinklers – 6 inch	Note 1
Fire Sprinklers – 8 inch	Note 1

Note 1 2% of the equivalent monthly meter size or $10 whichever is greater for all meter sizes.

There were no objections to the Company's proposed Service Line and Meter Installation Charges, and there was no significant disagreement on the amounts of Services Charges. We approve the Service Charge schedule as recommended by Staff, which modifies the Company proposed charges slightly, but which charges comport with our rules and are consistent with other recently approved charges. Thus, we authorize the following Service Line and Meter Installation Charges and Services Charges:

SERVICE LINE AND METER INSTALLATION CHARGES
(Refundable Pursuant to A.A.C. R14-2-405)

	Service Line Charge	Meter Installation Charge	Total
5/8" x ¾" Meter	$1,765	$105	$1,870
¾" Meter	1,765	180	1,945
1" Meter	1,765	240	2,005
1 ½" Meter	At Cost	At Cost	At Cost
2" Meter/ Turbine	At Cost	At Cost	At Cost
2" Meter/ Compound	At Cost	At Cost	At Cost
3" Meter/ Turbine	At Cost	At Cost	At Cost
3" Meter/ Compound	At Cost	At Cost	At Cost
4" Meter/ Turbine	At Cost	At Cost	At Cost

4" Meter/ Compound	At Cost	At Cost	At Cost
6" Meter/ Turbine	At Cost	At Cost	At Cost
6" Meter/ Compound	At Cost	At Cost	At Cost
8" & Large	At Cost	At Cost	At Cost

SERVICE CHARGES:

Establishment (Regular Hours)	$30.00
Establishment (After Hours)	45.00
Re-Establishment (Within 12 Months)	(a)
Reconnection (Delinquent)	$30.00
Reconnection (After Hours)	45.00
Meter Test (If Correct)	30.00
Deposit	(b)
Deposit Interest	(b)
NSF Check	$15.00
Deferred Payment – per month	1.5%
Meter Reread (If Correct)	$15.00
Late Charge	1.5% (c)
Service Calls – Flat Rate/After Hours	$50.00
Moving Meter at Customer Request	Cost

(a) Minimum charge times number of full months off the system per A.A.C. R14-2-403(D).

(b) Per A.A.C. R14-2-403(B) Residential – two times the average bill; Commercial – two and one-half times the average bill.

(c) 1.5% of unpaid balance.

In addition to the collection of regular rates, the utility will collect from its customers a proportionate share of any privilege, sales, use, and franchise tax per A.A.C. R14-2-409D(5).

Under these authorized rates, the average 5/8 inch residential Bella Vista ratepayer using 6,612 gallons per month would experience a monthly increase of $3.68 or 16.05 percent, from $26.57 to $26.58. The median residential 5/8 inch meter Bella Vista customer using 4,500 gallons per month would see an increase of $2.54, or 13.12 percent, from $19.37 to $21.91.

The average residential 5/8 inch meter NSWC ratepayer using 5,755 gallons per month would experience a monthly decrease of $18.40 or 42.71 percent, from $43.08 to $24.68; the median 5/8 inch meter NSWC residential customer using 4,500 gallons per month would see a decrease of

$18.10, or 45.24 percent, from $40.00 to $21.91.[161]

The average residential 5/8 inch meter SSWC ratepayer using 5,581 gallons per month would experience a monthly decrease of $18.30 or 42.97 percent, from $42.60 to $24.29; the median 5/8 inch residential SSWC customer using 4,500 gallons would see a decrease of $18.10, or 45.24 percent, from $40.00 to $21.91.[162]

B. Low Income Tariff

Applicants proposed a Low Income Tariff and have accepted Staff's recommended modifications.[163] The tariff is similar to the Low Income Tariff we approved for RRUI.[164] Under the terms of the Low Income Tariff, qualifying customers receive a 15 percent discount applied to the regular filed tariff. Customers must reapply every two years and provide proof of eligibility. For a household of two to qualify, total gross annual income cannot exceed $21,855, and for a household of four, gross annual income cannot exceed $33,075.[165]

The cost of the Low Income Tariff is recovered from those customers who pay tariffed rates by means of a commodity surcharge, to be determined annually based on the costs of the program in the previous twelve months.[166] BVWC would maintain a balancing account to track program costs and collections from non-participants.[167]

We find that a Low Income Tariff, as modified by Staff's recommendations in this proceeding, is fair and reasonable and in the public interest. The Low Income Tariff is consistent with that approved in the RRUI rate case, except that the costs of the program in this case should be collected by means of a surcharge on all classes of non-participants, and not just residential users.[168] BVWC shall track the direct costs of the program (i.e. those costs directly associated with the program, and which would not be incurred in the absence of the program), and account for these costs

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[161] The majority of the decrease is attributable to the reduction in the monthly customer charge after consolidation. The current NSWC customer charge is $31.00, thus of the $18.40 total decrease for the average NSWC customer, $16.00 or 87 percent, is due to the decrease in the monthly customer charge.
[162] The SSWC monthly customer charge also decreases from $31.00 to $15.00, thus accounting for 87 percent of the $18.30 average decrease.
[163] Ex A-14 Bourassa Reb. (Rate Base, Income, Rate Design) at 39.
[164] Ex A-6 Sorenson RJ at 12.
[165] See Low Income Tariff attached to Applicants' Final Schedules.
[166] Ex A-13 Bourassa Dir. at 31.
[167] *Id.* at 32.
[168] Ex S-8 at 16.

in a separate account. The Company shall file for Commission approval of the surcharge after the Low Income Tariff has been in effect for 12 months. We concur with Staff's recommendation that participation be limited to 2,400 customers (i.e., approximately 30 percent of residential customers).

Consequently, we direct Applicants to file a Low Income Tariff that is consistent with our findings.

C. Hook-up Fee (HUF) Tariff

NSWC and SSWC currently have approved HUF Tariffs starting at $1,000 for a 5/8 inch meter.[169] Bella Vista does not have an existing HUF Tariff. In this proceeding, Applicants requested a HUF tariff for the consolidated entity that starts at $1,600 for the 5/8 inch meter with the following fee schedule:[170]

Off-Site Water HUF Table

Meter Size	Size Factor	Total Fee
5/8" x ¾"	1	$1,600
¾"	1.5	$2,400
1"	2.5	$4,000
1 ½"	5	$8,000
2"	8	$12,800
3"	16	$25,600
4"	25	$40,000
6" or larger	50	$80,000

The Applicants' proposed HUF includes language not found in Staff's HUF Tariff template. Staff and RUCO object to the proposed changes to the template tariff.

The tariff language that is at dispute is as follows:

> The Company shall not record amounts collected under this tariff as CIAC until such amounts have been expended for plant.

Staff recommends a HUF Tariff for the consolidated BVWC as proposed by the Companies,

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[169] Ex S-3.
[170] Applicants' Final Schedules at H-3 at 9.

but which does not include the language quoted above.[171] Staff believes that the HUFs are contributions and should be deducted from rate base as is any other contribution. Staff argues that the Applicants' position that the HUF would not be considered CIAC until there is offsetting plant in service is misguided, as the classification of contributed funds as CIAC does not hinge upon whether it is spent or unexpended, but rather on whether it: 1) was provided by someone other that the company's owner/investor; 2) is non-refundable; and 3) is for the purpose of funding plant. Staff argues that the Applicants' position is contradicted by NARUC's definition of CIAC which provides: "CIAC and customer advances are payments made by customers generally to fund plant additions for new or expanded service." Staff believes this definition of CIAC supports Staff's position that CIAC is non-investor supplied capital at the time the money is received, and not when the plant is built.

RUCO also opposes the Applicant's proposed "non-CIAC" language for the HUF. RUCO believes that HUF proceeds are CIAC and must be recorded as such upon receipt to comply with existing rules, NARUC standards, and the precedence of prior Commission rulings involving Johnson Utilities and UNS Electric.[172] RUCO believes that under the Applicants' proposal the Company will have beneficial use of the funds in the HUF account and that as result, the Commission should reject that part of the proposed HUF that allows recording the funds as CIAC only upon completion of the plant.[173]

RUCO argues that the Applicants' proposal would result in a poor public policy, necessitating Staff to "chase the CIAC."[174] RUCO argues that recording the HUF funds as CIAC before they are spent on plant does not harm the utility and any reduction in rate base experienced up front is recovered on the back end.[175] RUCO argues that on the other hand, approving the Applicants' methodology would burden Staff and potentially harm ratepayers if plant is added without a corresponding entry in the CIAC account. According to RUCO, if Staff is unable to follow the trail of unrecorded CIAC, the Company would end up with the unjust benefit of earning a return on assets that were paid for by others, and ratepayers would essentially be paying twice—once through HUFs

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[171] Ex S-4, Scott Surr. at 5.
[172] Decision No. 60223 (May 27, 1997) and Decision No. 70011 (November 27, 2007); *see* RUCO Closing Brief at 31.
[173] RUCO Closing Brief at 32.
[174] *Id.* at 34.
[175] *Id.*

and again through rates.[176]

Applicants state that they proposed a HUF tariff as a means of raising capital to finance backbone plant needed to serve new development in its CC&N, and that the planned use of HUF funds to build plant is part of an overall capitalization that is designed to equitably apportion the overall costs of service in a manner that allows rates to remain within a reasonable range over time. With their proposed CIAC language, Applicants state that they believed they were offering the Commission a solution to the problem of what happens when utilities end up with unexpended CIAC being deducted from their rate bases.[177] Applicants state that the proposed language "does not convert non-investor supplied capital into shareholder *investment*, but simply seeks to postpone CIAC treatment until such time as the plant is actually funded."[178] Applicants assert that until the funds are expended, the utility does not have the beneficial use of the HUF funds because they are merely sitting in a bank account collecting interest that inures to the HUF account.

Applicants argue that it is poor policy to use the receipt of HUFs to lower rates given that the utility can require that the same plant be funded as an advance under a line extension agreement or be funded with investor supplied capital, which they assert could lead to higher rates.[179] Applicants argue that Staff's and RUCO's objections are motivated by a one-sided elimination of rate base that directly benefits customers at shareholder expense.[180] They argue the utility gets no benefit from the unexpended HUF funds while they are sitting in the bank earning interest.

Applicants argue that Staff cannot reconcile its position with the entirety of the NARUC definition of CIAC, and that Staff ignores the second part of the definition that reads "and which is utilized to offset the acquisition, improvement or construction costs of the utility's property, facilities or equipment used to provide utility service to the public."[181] Applicants argue that this language indicates that CIAC does not exist until something is spent on plant. Applicants note that there are other payments from third parties, such as Advances in Aid of Construction, that are not CIAC, and

[176] *Id.* at 35.
[177] Applicants Initial Closing Brief at 60.
[178] *Id.*
[179] *Citing* A.A.C. R14-2-406 and R14-2-606; Applicants' Opening Brief at 61.
[180] Applicants Initial Closing Brief at 60.
[181] Ex A-6 at 4.

that even HUFs are not always treated by the Commission as CIAC.[182]

Section 217 of the NARUC USOA defines CIAC as follows:

271. Contributions in Aid of Construction

A. This account shall include:

1. Any amount or item of money, services or property received by a utility, from any person or governmental agency, any portion of which is provided at no cost to the utility, which represents an addition or transfer to the capital of the utility, and which is utilized to offset the acquisition, improvement or construction costs of the utility's property, facilities, or equipment used to provide utility services to the public.

We find that HUF funds meet this definition and are appropriately deducted from rate base as non-investor supplied capital. However we think that such deductions should not occur until such amounts have been expended for plant. We will therefore require the Company to include the following language in its HUF tariff:

The company shall record amounts collected under the tariff as CIAC; however, such amounts shall not be deducted from rate base until such amounts have been expended for plant.

D. Non-Account Water

Staff states that it could not determine the "true" water loss for the Applicants because of the mismatch of the meter reading data.[183] Consequently, Staff recommends that the Applicants monitor their various water systems for a 12-month period to prepare a water loss report, and that they should coordinate when they read the production meters each month with customer monthly meter readings. Staff states that if the reported water loss is greater than 10 percent, Applicants should submit a detailed cost/benefit analysis containing a detailed analysis and plan to reduce the water loss to 10 percent or less. If it is not cost effective to achieve the targeted water loss, Staff recommends that the Applicants submit a detailed analysis that supports that position.[184]

Applicants accept Staff's recommendations concerning non-account water.[185]

We find Staff's recommendation to be reasonable.

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[182] Tr. at 573; Mr. Coley testified that in the past, HUFs were treated as revenue.
[183] Ex S-4 at 4.
[184] Staff Opening Brief at 23.
[185] Ex A-6 at 2.

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Having considered the entire record herein and being fully advised in the premises, the Commission finds, concludes, and orders that:

FINDINGS OF FACT

1. On August 31, 2009, NSWC, SSWC and Bella Vista filed applications for rate increases with the Commission.

2. On August 31, 2009, Applicants filed a Joint Application for Approval of Authority to Transfer Utility Assets from NSWC and SSWC to Bella Vista pursuant to A.R.S. § 40-285.

3. On September 1, 2009, the Applicants filed Motions to Consolidate the rate applications and the Joint Application.

4. On September 30, 2009, Staff notified the Applicants that their rate applications were sufficient. NSWC and SSWC were classified as Class C utilities and Bella Vista was classified as a Class B utility.

5. By Procedural Order dated October 5, 2009, a Procedural Conference was set to discuss consolidation and the procedures for processing these applications.

6. On October 19, 2009, Staff filed a Notice indicating it has no objection to the consolidation of these dockets.

7. During a Procedural Conference on October 23, 2009, Staff, the Applicants and RUCO appeared through counsel. All parties agreed that the matters should be consolidated for judicial efficiency and that they would confer and jointly propose a schedule for filing testimony and the hearing in these matters.

8. On October 27, 2009, RUCO filed an Application to Intervene.

9. By Procedural Order dated November 9, 2009, the matter was set for hearing to commence on June 28, 2010, various procedural guidelines were established, and RUCO was granted intervention.

10. On March 26, 2010, Applicants filed Certification of Publication and Proof of Mailing. Notification of the hearing set for June 28, 2010, was published in the *Sierra Vista Herald* and *Bisbee Daily Review* on December 31, 2009. Applicants mailed notice to customers on

December 30, 2009.

11. On April 9, 2010, Staff filed a Motion for an extension of time to file its Direct Testimony which was granted by Procedural Order dated April 13, 2010.

12. On April 12, 2010, RUCO filed the Direct Testimony of Jodi Jerich, William Rigsby, Rodney Moore and Timothy Coley.

13. On April 14, 2010, Staff filed the Direct Testimony of Crystal Brown, Pedro Chaves and Marlin Scott Jr.

14. On April 27, 2010, Staff filed the Rate Design and Consolidation of Operations Direct Testimony of Ms. Brown.

15. On April 29, 2010, Applicants requested a modification of the testimony and hearing schedule.

16. By Procedural Order dated May 3, 2010, the hearing was continued until July 21, and 22, 2010, in Tucson, Arizona, and additional days were scheduled for August 16-19, 2010, in Phoenix, Arizona. The testimony deadlines were extended commensurately.

17. On May 25, 2010, Applicants filed Rebuttal Testimony for Gregory Sorensen, Peter Eichler, and Thomas Bourassa.

18. On June 16, 2010, RUCO filed notice of errata correcting typographical errors in Mr. Rigsby's Supplemental Direct Testimony.

19. On June 18, 2010, Staff filed the Surrebuttal Testimony of Ms. Brown, Mr. Chavez and Mr. Scott; and RUCO filed the Surrebuttal Testimony of Ms. Jerich, Mr. Rigsby, Mr. Moore and Mr. Coley.

20. On June 28, 2010, (the originally scheduled and noticed date of the hearing), the Commission convened a public comment session in Tucson, Arizona.

21. On July 7, 2010, Applicants filed the Rejoinder Testimony of Mr. Sorensen, Mr. Eichler and Mr. Bourassa.

22. The hearing convened as scheduled on July 21, 2010, at the Commission's offices in Tucson, Arizona, and continued on July 22, 2010, in Tucson, and on August 16-19, 2010, at the Commission's offices in Phoenix, Arizona.

23. On August 11, 2010, RUCO filed a Notice of Errata to Ex. THC-4 to Mr. Coley's Surrebuttal Testimony.

24. On September 10, 2010, RUCO filed its Final Schedules, and on September 17, 2010 Staff and Applicants filed Final Schedules.

25. On October 5, 2010, RUCO and Applicants filed their Closing Briefs and Staff filed revised Final Schedules.

26. On October 6, 2010, Staff filed its Closing Brief.

27. On October 28, 2010, all parties filed their Reply Briefs.

28. The Commission received 10 written comments from customers who, in general, were opposed to the magnitude of the proposed increase and expressed concern about Bella Vista customers being asked to support the operations of the NSWC and SSWC systems. No customers appeared at the June 28, 2010, Public Comment Meeting or at the commencement of the July 21, 2010, hearing to give public comment.

29. Bella Vista, NSWC and SSWC are subsidiaries of Liberty Water. They provide service in Cochise County, Arizona and are located in close proximity to each other, with Bella Vista and SSWC being physically interconnected.

30. In the test year, Bella Vista provided water utility service to approximately 8,500 connections, NSWC served 349 connections and SSWC served 789 connections.

31. It is in the public interest to consolidate the operations and rates of Bella Vista, NSWC and SSWC because of the cost savings associated with economies of sale, the benefits of a larger customer base, the benefits of improved water supply, and benefits of creating a small regional water provider.

32. BVWC is not located within an AMA.

33. The consolidated BVWC has a FVRB of $7,577,10 at the end of the test year.

34. In the test year, the consolidated BVWC had revenues totaling $4,162,136, which produced operating income of $206,615, a return of 2.73 percent on FVRB.

35. A rate of return of 8.8 percent is reasonable and appropriate for the consolidated BVWC.

36. As discussed herein, BVWC is entitled to a gross revenue increase of $666,838, or 18.26 percent, over test year revenues.

37. The rates and charges authorized herein are reasonably calculated to provide the Company an opportunity to earn its authorized revenue requirement and are fair and reasonable.

38. Under these authorized rates, the average 5/8 inch residential Bella Vista ratepayer using 6,612 gallons per month would experience a monthly increase of $3.68 or 16.05 percent, from $26.57 to $26.58. The median residential 5/8 inch meter Bella Vista customer using 4,500 gallons per month would see an increase of $2.54, or 13.12 percent, from $19.37 to $21.91.

39. The average residential 5/8 inch meter NSWC ratepayer using 5,755 gallons per month would experience a monthly decrease of $18.40 or 42.71 percent, from $43.08 to $24.68; the median 5/8 inch meter NSWC residential customer using 4,500 gallons per month would see a decrease of $18.10, or 45.24 percent, from $40.00 to $21.91.

40. The average residential 5/8 inch meter SSWC ratepayer using 5,581 gallons per month would experience a monthly decrease of $18.30 or 42.97 percent, from $42.60 to $24.29; the median 5/8 inch residential SSWC customer using 4,500 gallons would see a decrease of $18.10, or 45.24 percent, from $40.00 to $21.91

41. Funds received from HUFs are a form of non-investor supplied, zero-cost capital for the utility and are appropriately treated as CIAC.

42. The HUF tariff as proposed by the Company is in the public interest if modified to reflect that amounts collected under the tariff shall be recorded as CIAC, but shall not be deducted from rate base until such amounts have been expended on plant.

43. Because they will henceforth be part of the consolidated BVWC, it is not in the public interest to have different charges in effect for different areas of the territory, and authority for the currently authorized HUFs for NSWC and SSWC should be withdrawn.

44. The Low Income Tariff and surcharge mechanism proposed in this proceeding, as reflected in the Applicants' Final Schedules, is fair and reasonable and in the public interest. Initially, participation in the Low Income Tariff is limited to 2,400 residential households.

45. Staff's recommendations concerning non-account water loss reports are reasonable

and should be adopted.

46. We believe that all water companies in Arizona should be required to do everything that is reasonably possible to conserve Arizona's precious groundwater. Although we commend Bella Vista for voluntarily implementing several BMPs, we believe it is reasonable to the Companies implement at least five BMPs in the form of tariffs that substantially conform to the templates created by Staff, available at the Commission's website. The implementation should be accomplished by the Companies submitting at least five BMP tariffs for the Commission's review and consideration. A maximum of two of these BMP tariffs may come from the "Public Awareness/Public Relations" or "Education and Training" categories of the BMPs. The Company may request cost recovery of actual costs associated with the BMPs implemented in its next general rate application.

CONCLUSIONS OF LAW

1. Bella Vista, NSWC and SSWC are public service corporations within the meaning of Article XV of the Arizona Constitution and A.R.S. §§40-250, 40-251, 40-367, 40-202, 40-321, 40-285, 40-331 and 40-361.

2. The Commission has jurisdiction over Bella Vista, NSWC and SSWC and the subject matter contained in the Applicants' rate applications and joint application to consolidate operations and rates.

3. Notice of the proceeding was provided in conformance with law.

4. Consolidation of operations and rates for Bella Vista, NSWC and SSWC is in the public interest.

5. Bella Vista is a fit and proper entity to own and operate the utility assets of NSWC and SSWC.

6. The rates, charges and conditions of service established herein are just and reasonable and in the public interest.

7. The HUF Tariff, as modified as discussed herein, is fair and reasonable and in the public interest.

8. The Low Income Tariff proposed in this matter, as modified Staff's recommendations, is fair and reasonable and in the public interest.

9. Staff's recommendations concerning non-account water and reporting are reasonable and should be adopted.

ORDER

IT IS THEREFORE ORDERED that the Joint Application to Consolidate Operations and Transfer Utility Assets is approved and the Certificates of Convenience and Necessity of Northern Sunrise Water Company and Southern Sunrise Water Company Commission are hereby transferred to Bella Vista Water Company pursuant to A.R.S. §40-285, and Northern Sunrise Water Company and Southern Sunrise Water Company are authorized to transfer their assets to Bella Vista Water Company.

IT IS FURTHER ORDERED that Bella Vista Water Company is hereby authorized and directed to file with the Commission, on or before March 31, 2011, revised schedules of rates and charges consistent with the discussion herein.

IT IS FURTHER ORDERED that the revised schedules of rates and charges shall be effective for all service on and after April 1, 2011.

IT IS FURTHER ORDERED that Bella Vista Water Company's proposed Low Income Tariff, as modified by Staff's recommendations, is approved; and Bella Vista Water Company is authorized to collect the costs of the program, as discussed herein, by means of a surcharge to be approved by the Commission and assessed on non-participating customers.

IT IS FURTHER ORDERED that Bella Vista Water Company shall file with its revised schedules of rates and charges, a Low Income Tariff that comports with this Decision and shall within 30 days of the effective date of this Order provide notice to its customers of the Low Income Tariff and how to apply, in a form acceptable to Staff.

IT IS FURTHER ORDERED that Bella Vista Water Company shall notify its customers of the revised schedules of rates and charges authorized herein by means of an insert in its next regularly scheduled billing, or by separate mailing, in a form acceptable to Staff.

IT IS FURTHER ORDERED that Bella Vista Water Company shall monitor its water systems for a 12-month period to prepare a water loss report to be filed with Docket Control within 45 days after the end of the 12-month period, as a compliance item in this docket, and shall coordinate when the production meters are read each month with customer monthly meter readings in a manner that yields information necessary to monitor non-account water with reasonable accuracy; if the reported water loss is greater than 10 percent, Bella Vista Water Company shall submit a detailed cost/benefit analysis containing a detailed analysis and plan to reduce the water loss to 10 percent or less, and if it is not cost effective to achieve the targeted water loss, Bella Vista Water Company shall submit a detailed analysis that supports that position.

IT IS FURTHER ORDERED that the Hook-up Fee Tariff as modified herein is approved, and Bella Vista Water Company should file a Hook-up Fee Tariff in a form that comports with Staff's template Hook-up Fee Tariff, with the inclusion of the language concerning the treatment of the fees as CIAC as discussed herein, as a compliance item in this docket, within 30 days of the effective date of this Decision.

IT IS FURTHER ORDERED that the authority for the Hook-up Fee Tariffs for the territories of the Northern Sunrise Water Company and Southern Sunrise Water Company is hereby withdrawn.

IT IS FURTHER ORDERED that Bella Vista Water Company shall file with Docket Control, as a compliance item in this docket, within 90 days of the effective date of this Decision, at least five Best Management Practices in the form of tariffs that substantially conform to the templates created by Staff available at the Commission's website, for the Commission's review and consideration. A maximum of two of these BMPs may come from the "Public Awareness/Public Relations" or "Education and Training" categories of the BMPs as outlined by the ADWR in its Modified Non-Per Capita Conservation Program and relevant ADWR documents.

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IT IS FURTHER ORDERED that Bella Vista Water Company shall report the data and information for each of its water systems by ADEQ Public Water System.

IT IS FURTHER ORDERED that this Decision shall become effective immediately.

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN | COMMISSIONER

COMMISSIONER | COMMISSIONER | COMMISSIONER

IN WITNESS WHEREOF, I, ERNEST G. JOHNSON, Executive Director of the Arizona Corporation Commission, have hereunto set my hand and caused the official seal of the Commission to be affixed at the Capitol, in the City of Phoenix, this 7th day of April, 2011.

ERNEST G. JOHNSON
EXECUTIVE DIRECTOR

DISSENT

DISSENT

SERVICE LIST FOR: BELLA VISTA WATER COMPANY, NORTHERN SUNRISE WATER COMPANY and SOUTHERN SUNRISE WATER COMPANY

DOCKET NOS.: W-02465A-09-0411, W-20453A-09-0412, W-20454A-09-0413, W-02465A-09-0414, W-20453A-09-0414, and W-20454A-09-0414

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