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**MEMORANDUM
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Arizona Corporation Commission

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MAY 23 2011

TO: Docket Control
FROM: Steven M. Olea
Director
Utilities Division

2011 MAY 23 P 4: 47 D
EA for SMD
AZ CORP COMMISSION
DOCKET CONTROL

DOCKETED BY

DATE: May 23, 2011

RE: SUPPLEMENTAL STAFF REPORT FOR CERBAT WATER COMPANY'S
APPLICATION FOR A PERMANENT RATE INCREASE
(DOCKET NO. W-02391A-10-0218)

Attached is the Supplemental Staff Report for Cerbat Water Company's application for a permanent rate increase.

SMO:All:tdp

Originator: Alexander Ibhade Igwe, CPA

Service List for: Cerbat Water Company.
Docket No. W-02391A-10-0218

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**STAFF REPORT
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION**

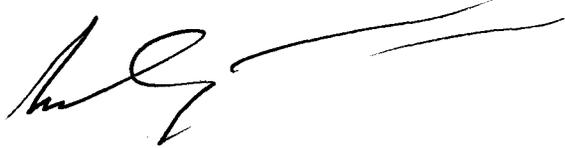
**CERBAT WATER COMPANY
DOCKET NO. W-02391A-10-0218**

**APPLICATION
FOR A
PERMANENT RATE INCREASE**

MAY 23, 2011

STAFF ACKNOWLEDGMENT

The Supplemental Staff Report for Cerbat Water Company, Docket No. W-02391A-10-0218 was the responsibility of the Staff members listed below. Alexander Ihhade Igwe was responsible for the review and analysis of the Company's application for a permanent rate increase, revenue requirement, rate base, and rate design.

A handwritten signature in black ink, appearing to read 'A. Igwe', with a long horizontal flourish extending to the right.

Alexander Ihhade Igwe, CPA
Executive Consultant III

**EXECUTIVE SUMMARY
CERBAT WATER COMPANY
DOCKET NO. W-02391A-10-0218**

On May 20, 2011, Staff filed their comments in Docket Nos. W-02391A-11-0166 and W-02391A-10-0218 , recommending that the Arizona Corporation Commission (“Commission”) approve a Well Repairs Surcharge for Cerbat Water Company, (“Cerbat or “Company”), in the amount of \$12.52 per customer per month. A Commission verbal motion on April 27, 2011 required Cerbat to file for an emergency rate or surcharge if the Claude K Neal Family Trust (“Trust”) transfers ownership of its well and related facilities to Cerbat, by May 13, 2011. On May 13, 2011, Cerbat filed a report stating that the Trust has transferred its well to Cerbat through a Quitclaim Deed and Bill of Sale dated May 12, 2011. Based on this filing, Staff recommended a Well Repairs Surcharge of \$12.52 per customer per month.

Ordinarily, a company’s ownership of its own well means that it does not have a purchase water expense. Here, Cerbat had been purchasing water from the Trust, but as a result of Cerbat’s acquisition of its own water source, it will no longer have the expense of purchasing water from the Trust. As a result, the purchased water expense of \$29,707 reflected in the pending rate case would normally have been eliminated from cost of service. Staff, however, is recommending reclassifying the \$29,707 from “purchased water expense” to “repairs and maintenance expense.” This reclassification is intended to provide adequate additional cash flow for the maintenance and repairs of Cerbat’s newly acquired well and related facilities from the Trust.

This reclassification does not affect Staff’s recommended cost of service because it has no impact on Staff’s recommended revenue requirement and rate design in the rate proceeding. As shown on Schedule 6, if Staff’s recommended Well Repairs Surcharge and Staff’s recommended rates in the rate proceeding are approved by the Commission, a typical residential customer, on a 3/4-inch by 5/8-inch meter, with a median usage of 4,569-gallons, will experience a monthly increase of \$13.00 or 50.9 percent.

Finally, it is pertinent to note that Cerbat’s future rate application will be reviewed based on actual test year cost of service, without regard to Well Repairs Surcharge. Staff recommends that the Commission order Staff to fully examine the Company’s management of proceeds of Well Repairs Surcharge during its next rate case.

SCHEDULES

REVISED TYPICAL BILL ANALYSIS Schedule AII-6

On April 27, 2011, the Arizona Corporation Commission ("Commission") approved a motion requiring Cerbat Water Company ("Cerbat" or "Company") to file an application for an emergency rate increase or surcharge by May 13, 2011, if the Company wanted the Commission to consider the possible implementation of an emergency rate surcharge during the Commission's Open Meeting on May 24 and 25, 2011. The emergency rate surcharge is intended to pay off the cost of repairs related to the Trust well, if ownership of the well is transferred from the Trust to Cerbat.

On May 13, the Company filed a report stating that the Trust has transferred its well to Cerbat through a Quitclaim Deed and a Bill of Sale dated May 12, 2011. Also, the Company claimed that its accrued cost of well repairs was approximately \$120,000, and proposed a surcharge of no less than \$10.00 per customer per month.

Pursuant to the Commission's verbal motion, Staff filed its comments on the Company's proposal, recommending a Well Repairs Surcharge of \$12.52 per customer per month. This surcharge is intended to facilitate the Company's ability to defray past due obligations related to its new ownership of the well over three years.

Staff is filing this supplemental report to address the impact of Staff's proposed Well Repairs Surcharge on the pending rate case. Staff finds that with the transfer of the Trust well to Cerbat, except for extraordinary circumstances, the Company does not have to purchase water for provision of service. Ordinarily, the cost of purchased water of \$29,707 recommended in this proceeding should have been eliminated. Because future cost of operating and maintaining the Company's newly acquired well is not known and measurable at this juncture, Staff recommends that \$29,707 previously recommended for purchased water expense be reclassified to repairs and maintenance expense.

Staff recommends that the Company utilize this increase in repairs and maintenance expense for repairs and maintenance of the newly acquired well, additional water testing expense and purchased power. Also, the Company could expend the funds on repairs and maintenance of other facilities necessary for provision of service. Staff's recommendation does not change cost of service, revenue requirement or rate design in this rate proceeding. As shown on Schedule AII-6, if Staff's recommended Well Repairs Surcharge and rates recommended in the rate proceeding are approved, a typical residential customer, on a 3/4-inch by 5/8-inch meter, with a median usage of 4,569-gallons, will experience a monthly increase of \$13.00 or 50.9 percent.

Finally, it is pertinent to note that Cerbat's future rate filing will be reviewed based on actual test year cost of service, without regard to Well Repairs Surcharge. Staff recommends that the Commission order Staff to fully examine the Company's management of proceeds of Well Repairs Surcharge during its next rate case.

TYPICAL BILL ANALYSIS WITH SURCHARGE
General Service 3/4 - Inch Meter

Average Number of Customers: 260

<u>Company Proposed</u>	<u>Gallons</u>	<u>Present Rates</u>	<u>Proposed Rates</u>	<u>Dollar Increase</u>	<u>Percent Increase</u>
Average Usage	7,605	\$32.11	\$48.46	\$16.35	50.9%
Median Usage	4,569	\$25.54	\$38.78	\$13.24	51.9%
<u>Staff Proposed</u>					
Average Usage	7,605	\$32.11	\$46.13	\$14.02	43.7%
Median Usage	4,569	\$25.54	\$38.54	\$13.00	50.9%

Present & Proposed Rates (Without Taxes)
General Service 3/4 - Inch Meter

<u>Gallons Consumption</u>	<u>Present Rates</u>	<u>Company Proposed Rates</u>	<u>% Increase</u>	<u>Staff Proposed Rates</u>	<u>% Increase</u>
0	\$18.00	\$27.36	52.0%	\$30.52	69.6%
1,000	19.65	29.86	52.0%	32.17	63.7%
2,000	21.30	32.36	51.9%	33.82	58.8%
3,000	22.95	34.86	51.9%	35.47	54.6%
4,000	24.60	37.36	51.9%	37.12	50.9%
5,000	26.25	39.86	51.8%	39.62	50.9%
6,000	28.50	43.16	51.4%	42.12	47.8%
7,000	30.75	46.46	51.1%	44.62	45.1%
8,000	33.00	49.76	50.8%	47.12	42.8%
9,000	35.25	53.06	50.5%	49.62	40.8%
10,000	37.50	56.36	50.3%	53.27	42.1%
15,000	48.75	72.86	49.5%	71.52	46.7%
20,000	60.00	93.61	56.0%	89.77	49.6%
25,000	73.25	114.36	56.1%	108.02	47.5%
50,000	139.50	218.11	56.4%	199.27	42.8%
75,000	205.75	321.86	56.4%	290.52	41.2%
100,000	272.00	425.61	56.5%	381.77	40.4%
125,000	338.25	529.36	56.5%	473.02	39.8%
150,000	404.50	633.11	56.5%	564.27	39.5%
175,000	470.75	736.86	56.5%	655.52	39.3%
200,000	537.00	840.61	56.5%	746.77	39.1%