

ORIGINAL

OPEN MEETING AGENDA ITEM



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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

DOCKETED

AUG 9 2011

DOCKETED BY [Signature]

COMMISSIONERS

2011 AUG -9 P 2:48

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

AZ CORP COMMISSION DOCKET CONTROL

IN THE MATTER OF THE APPLICATION OF JOHNSON UTILITIES, LLC, DBA JOHNSON UTILITIES COMPANY FOR AN INCREASE IN ITS WATER AND WASTEWATER RATES FOR CUSTOMERS WITHIN PINAL COUNTY, ARIZONA.

DOCKET NO. WS-02987A-08-0180

NOTICE OF FILING JOHNSON UTILITIES' PROPOSED AMENDMENT NO. 11 AND RESPONSE TO CHAIRMAN PIERCE'S AUGUST 4, 2011 LETTER

Brownstein Hyatt Farber Schreck, LLP
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Phoenix, AZ 85004

In a letter dated August 4, 2011, Chairman Pierce stated that it would be helpful if the parties docketed proposed amendments for the convenience of the Arizona Corporation Commission ("Commission") by August 9, 2011. Accordingly, Johnson Utilities, LLC, dba Johnson Utilities Company ("Company") hereby files its Proposed Amendment No. 11 regarding the Petition to Amend Decision 71854 Pursuant to A.R.S. §40-252 (the "Petition") and urges the Commission to adopt the amendment at its Open Meeting on August 11, 2011.

A. Relief Requested by Johnson Utilities.

In its Petition, Johnson Utilities requested that the Commission amend Decision 71854 as follows:

1. Changing the \$40 per month late fee in the Company's wastewater division tariff to a late fee of 1.5% per month on the unpaid account balance, consistent with the Company's water division tariff.
2. Adding back into rate base wastewater division plant of \$18,244,755 which was erroneously disallowed in the rate case. This amount consists of: (i) a \$10,892,391 deduction to rate base for alleged inadequately supported wastewater plant costs; and (ii) a \$7,352,364 deduction to rate base for alleged affiliate profit associated with affiliate-constructed wastewater plant.
3. Removing from rate base \$6,931,078 in unexpended test year hook-up fees.

- 1 4. Reinstating the Company's previously authorized hook-up fees for new
- 2 water and sewer connections.
- 3 5. Establishing a rate of return for the Company based upon its weighted
- 4 average cost of capital in the range of 8.18% to 11.89%.
- 5 6. Reclassifying \$2,201,386 of wastewater plant erroneously as post test year
- 6 wastewater plant in the rate case application to test year plant-in-service.
- 7 7. Including in plant-in-service post test-year wastewater plant of \$1,021,076
- 8 which is necessary to serve the test year-end level of customers.
- 9 8. Including imputed income tax expense in the Company's revenue
- 10 requirement, consistent with the understanding hereinafter described.

11 On July 26, 2011, Johnson Utilities filed an amendment to the Petition: (i) modifying the
12 Company's request under item 5 above to seek a rate of return based upon a weighted average
13 cost of capital ("WACC") of only 8.00%; and (ii) clarifying the Company's request under item 8
14 above to make clear that the Company is not seeking imputed income tax expense in this case,
15 but rather an amendment to Decision 71854 to include the following language, consistent with
16 the Commission's recent Decision 72177:

17 The Commission has agreed to examine the merits of imputing income tax
18 expenses to S-corps and LLCs in its ongoing water workshops (Docket No. W-
19 00000C-06-0149). While we believe it is prudent to follow the current policy
20 today, we do not wish to prejudice Johnson Utilities in the event the Commission
21 determines to alter its policy in the future. Accordingly, in the event the
22 Commission alters its policy in the future, Johnson Utilities may file a motion to
23 amend this Order prospectively, and Johnson Utilities' authorized revenue
24 requirement hereunder, pursuant to A.R.S. §40-252, to reflect the change in
25 Commission policy.

26 Thus, in the event the Commission subsequently adopts a policy which allows a limited
27 liability company such as Johnson Utilities to include imputed income tax expense in its revenue
28 requirement, the Company will file a new petition under A.R.S. §40-252 to amend Decision
71854 prospectively to request income tax expense in the Company's authorized revenue
requirement.

29 **B. Rate Impacts of Relief Requested.**

30 The relief requested in item 1 (wastewater late payment charge), item 4 (water and
31 wastewater hook-up fees) and item 8 (income tax expense) does not impact current water or
32 wastewater rates.

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11 class mail this 9th day of August, 2011, to:

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JOHNSON UTILITIES PROPOSED AMENDMENT #11

COMPANY: Johnson Utilities Company AGENDA ITEM NO. U-12

DOCKET NO. WS-02987A-08-0180 OPEN MEETING DATE: August 11, 2011

Sewer Plant in Service

Page 8, lines 19-20, DELETE:

"We believe the record does not support a specific disallowance figure for the water division, notwithstanding the Company's record keeping issues as discussed in this proceeding."

AND REPLACE WITH:

"We believe the record does not support a specific disallowance to plant in service, notwithstanding the Company's record keeping issues as discussed in this proceeding. Accordingly, we will not adopt Staff's recommended disallowance of \$7,433,707 for the water division and \$10,892,391 for the wastewater division."

Page 8, line 20, DELETE "Further" AND REPLACE WITH "However."

DELETE the section captioned "*AIAC and CIAC Related to Unsupported Plant*" beginning at page 9, line 22½, and continuing through page 10, line 11.

Post Test Year Sewer Plant and Reclassification of Post Test Year Sewer Plant

Page 10, line 19, DELETE "\$1,201,108" AND REPLACE WITH "\$1,021,108."¹

DELETE the paragraph at page 14, lines 5½-19, AND REPLACE WITH:

"We believe Johnson Utilities presented credible evidence that \$2,201,386 of sewer plant was misclassified as post test year plant in the Company's rate application and that it should be reclassified as test year plant. Accordingly, the \$2,201,386 of post test year sewer plant will be reclassified as test year plant in service."

"We also believe the Company presented credible evidence that the Parks lift station and the Queen Creek leach field are prudent and necessary to serve the test year level of customers, that they are revenue neutral, and that they are necessary for system reliability. The Commission has allowed *pro forma* adjustments, including post test year plant, in order to ensure a proper matching of plant to test year customers and to more accurately reflect reality during the period that rates will be in effect. Accordingly, we will increase the Company's test year plant in service by \$1,021,108 to include the Parks lift station and the Queen Creek leach field."

¹ This amendment corrects a typographical error in the decision.

Affiliate Profit

Beginning at page 31, line 23½, DELETE:

"After considering all the evidence presented, we find that the record is insufficient to support specific plant in service adjustments for the water division. Rather than estimating an appropriate adjustment and excluding plant costs from the Company's rate base, we believe it is appropriate to make adjustments to the authorized operating margin."

AND REPLACE WITH:

"After considering all the evidence presented, we find that the record is insufficient to support additional plant in service adjustments for affiliate profit beyond the adjustments of \$469,832 for the water division and \$800,179 for the wastewater division that were included in the Company's rate application."

DELETE the sentence beginning on page 32, line 13½, and ending on line 14½.

Unexpended Hook-Up Fees

DELETE page 35, lines 3-13½, AND REPLACE WITH:

"We find that HUF funds meet the definition of Contributions in Aid of Construction found in Section 271 of the NARUC USOA 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, consistent with our Decision 72251. Accordingly, we will not include \$6,931,078 of unexpended water HUFs and \$16,505 in sewer HUFs in the CIAC balance in rate base."

Fair Value Rate Base Summary

Page 35, line 16½, DELETE "\$2,414,613" AND REPLACE WITH "\$4,516,464."

Page 35, line 16½, DELETE "\$136,562" AND REPLACE WITH "\$17,323,177."

Income Tax Expense

DELETE beginning with the words "We agree" on page 46, line 20, and continuing through the end of the paragraph on page 47, line 7½, AND REPLACE WITH:

"As an LLC, Johnson Utilities does not pay income taxes. It has long been the policy of this Commission not to impute a hypothetical income tax expense to "pass through" entities such as Johnson Utilities. The Company's owners chose the business form they believed was beneficial to the owners, and knew, or should have known about the long-standing Commission policy. Regardless of the members' knowledge, however, we find that it is fair and reasonable to

continue the Commission policy not to impute an income tax expense when the utility is a pass-through entity for tax purposes.

At a recent Commission open meeting, the Commission agreed to examine the merits of imputing income tax expenses to S-corporations and LLCs in its ongoing water workshops (Docket No. W-00000C-06-0149). While we believe it is prudent to follow the current policy today, we do not wish to prejudice Johnson Utilities in the event the Commission determines to alter its policy in the future. Accordingly, in the event the Commission alters its policy in the future, Johnson Utilities may file a motion to amend this Order prospectively, and Johnson Utilities' authorized revenue requirement hereunder, pursuant to A.R.S. § 40-252, to reflect the change in Commission policy."

At page 74, immediately before the ordering paragraph on line 8, ADD a new ordering paragraph as follows:

"IT IS FURTHER ORDERED that in the event the Commission alters its policy to allow S-corporation and LLC entities to impute a hypothetical income tax expense for ratemaking purposes, Johnson Utilities, LLC dba Johnson Utilities Company may file a motion to amend this Order prospectively, and Johnson Utilities, LLC dba Johnson Utilities Company's authorized revenue requirement hereunder, pursuant to A.R.S. § 40-252, to reflect the change in Commission policy."

Operating Income Summary

Page 47, lines 13½-15, DELETE:

	Water Division	Wastewater Division
Adjusted test year revenues	\$13,172,899	\$11,354,014
Test year operating expenses	\$9,553,304	\$9,432,270
Test year operating income	\$3,619,595	\$1,921,744

AND REPLACE WITH:

	Water Division	Wastewater Division
Adjusted test year revenues	\$13,172,899	\$11,354,014
Test year operating expenses	\$9,744,373	\$10,169,118
Test year operating income	\$3,428,526	\$1,184,897

Cost of Capital

DELETE page 49, line 8½, through page 50, line 15½, AND REPLACE WITH:

"Considering the entire record in this case, long-held Commission practices, as well as other recent decisions of this Commission, we find an 8.00% overall rate of return on rate base."

Authorized Increase/Decrease

Page 50, lines 19-22½, DELETE:

"The adjusted test year operating income for the water division was \$3,619,595. A 3 percent operating margin for the Company's water division results in operating income of \$293,218. Based on our findings herein, we determine that the Company's gross revenue for its water division should decrease by \$3,398,960."

AND REPLACE WITH:

"The adjusted test year operating income for the water division was \$3,428,526. An 8 percent rate of return for the Company's water division results in operating income of \$361,317. Based on our findings herein, we determine that the Company's gross revenue for its water division should decrease by \$3,134,137."

Beginning at page 50, line 25, continuing through page 51, line 2, DELETE:

"The adjusted test year operating income for the wastewater division was \$1,921,744. A 3 percent operating margin for the Company's wastewater division results in operating income of \$290,610. Based on our findings herein, we determine that the revenues for the Company's wastewater division should decrease by \$1,667,019."

AND REPLACE WITH:

"The adjusted test year operating income for the wastewater division was \$1,184,897. An 8 percent rate of return for the Company's wastewater division results in operating income of \$1,385,854. Based on our findings herein, we determine that the revenues for the Company's wastewater division should increase by \$205,379."

Hook-Up Fee Tariff

DELETE from page 52, line 7½ through line 14½, AND REPLACE WITH:

"We agree with the Company that it should be permitted to continue to collect HUFs."

DELETE Finding of Fact 104 at page 68, lines 21-24, AND REPLACE WITH:

"It is reasonable and in the public interest to continue the Company's authority to collect additional HUFs for both its water and wastewater divisions under the Company's current HUF tariff."

Page 70, line 27, DELETE "discontinue" AND REPLACE WITH "continue."

DELETE Conclusion of Law 10, page 71, lines 1-3, and renumber the remaining Conclusions of Law.

Page 72, line 19, DELETE "discontinued" AND REPLACE WITH "continued."

DELETE the ordering paragraph at page 72, lines 21-24.

Water Rates

Finding of Fact 89, page 67, line 2, DELETE "\$2,414,613" AND REPLACE WITH "\$4,516,464."

Finding of Fact 90, page 67, line 4, DELETE "\$9,553,304" AND REPLACE WITH "\$9,744,373."

Finding of Fact 90, page 67, line 5, DELETE "\$3,619,595" AND REPLACE WITH "\$3,428,526."

Finding of Fact 92, page 67, lines 10-14, DELETE:

"Because the Company's adjusted FVRB for its water division is negative, a rate of return calculation is not meaningful. Based on the unique circumstances of this case, it is appropriate to use an operating margin to set fair and reasonable rates, and to allow a 3 percent operating margin, for revenues of \$9,773,939. This represents a \$3,398,960, or 25.80 percent, revenue decrease from \$13,172,899 to \$9,773,939."

AND REPLACE WITH:

"It is appropriate to use an 8.00 percent rate of return on the Company's fair value rate base. Based upon an 8.00 percent rate of return, the Company's revenue requirement is \$10,038,762. This represents a \$3,134,137, or 23.79 percent, revenue decrease from \$13,172,899 to \$10,038,762."

Finding of Fact 93, page 67, line 15, DELETE "\$3,398,960" AND REPLACE WITH "\$3,134,137."

Finding of Fact 96, page 67, lines 24-26, DELETE:

"Under the rates adopted herein, an average usage (6,931 gallons/month) residential water customer on a ¾-inch meter would experience a monthly rate decrease of \$12.78, approximately 30.01 percent, from \$42.59 per month to \$29.81 per month."

AND REPLACE WITH:

"Under the rates adopted herein, an average usage (6,931 gallons/month) residential water customer on a ¾-inch meter would experience a monthly rate decrease of \$11.73, approximately 27.54 percent, from \$42.59 per month to \$30.86 per month."

Conclusion of Law 4, page 70, lines 12-14, DELETE:

"The fair value of the Company's water division rate base is (\$2,414,613) and therefore a rate of return analysis is not reasonable. Authorizing an operating margin of 3 percent produces rates and charges that are just and reasonable."

AND REPLACE WITH:

"The fair value of the Company's water division rate base is \$4,516,464. Authorizing a rate of return of 8.00 percent produces rates and charges that are just and reasonable."

Wastewater Rates

Finding of Fact 97, page 67, line 28, DELETE "\$136,562" AND REPLACE WITH "\$17,323,177."

Finding of Fact 98, page 68, line 3, DELETE "\$9,432,270" AND REPLACE WITH "\$10,169,118."

Finding of Fact 98, page 68, line 3, DELETE "\$1,921,744" AND REPLACE WITH "\$1,184,897."

Finding of Fact 100, page 68, lines 8-12, DELETE:

"Because the Company's adjusted FVRB for its wastewater division is so small, a rate of return calculation is not meaningful. Based on the unique circumstances of this case, it is appropriate to use an operating margin to set fair and reasonable rates, and to allow a 3 percent operating margin, for operating income of \$290,610. This represents a \$1,667,019, or 14.68 percent, revenue decrease from \$11,354,014 to \$9,686,995."

AND REPLACE WITH:

"It is appropriate to use an 8.00 percent rate of return on the Company's fair value rate base. Based upon an 8.00 percent rate of return, the Company's revenue requirement is \$1,385,854. This represents a \$205,379, or 1.81 percent, revenue increase from \$11,354,014 to \$11,559,393."

Finding of Fact 102, page 68, lines 16-18, DELETE:

"Under the rates adopted herein, a residential wastewater customer on a ¾ inch water meter would experience a decrease of \$5.71, approximately 14.83 percent, from \$38.50 per month to \$32.79 per month."

AND REPLACE WITH:

"Under the rates adopted herein, a residential wastewater customer on a ¾ inch water meter would experience an increase of \$0.70, approximately 1.81 percent, from \$38.50 per month to \$39.20 per month."

Conclusion of Law 5, page 70, lines 15-17, DELETE:

"The fair value of the Company's wastewater division rate base is \$136,562 and therefore a rate of return analysis is not reasonable. Authorizing an operating margin of 3 percent produces rates and charges that are just and reasonable."

AND REPLACE WITH:

"The fair value of the Company's wastewater division rate base is \$17,323,177. Authorizing a rate of return of 8.00 percent produces rates and charges that are just and reasonable."

Exhibit A to Decision 71854²

Exhibit A, page 1, DELETE:

Monthly Usage Charge	
5/8" x 3/4" Meter	\$11.00
3/4" Meter	\$16.50
1" Meter	\$27.50
1-1/2" Meter	\$55.00
2" Meter	\$88.00
3" Meter	\$176.00
4" Meter	\$275.00
6" Meter	\$550.00
8" Meter	\$880.00
10" Meter	\$1,265.00

AND REPLACE WITH:

Monthly Usage Charge	
5/8" x 3/4" Meter	\$11.70
3/4" Meter	\$17.55
1" Meter	\$29.25
1-1/2" Meter	\$58.50
2" Meter	\$93.60
3" Meter	\$187.20
4" Meter	\$292.50
6" Meter	\$585.00
8" Meter	\$936.00
10" Meter	\$1,345.50

² The original Exhibit A to Decision 71854 was replaced with a corrected Exhibit A adopted in Decision 71910 dated September 28, 2010.

Exhibit A, page 3, DELETE:

Monthly Usage Charge	
5/8" Meter	\$29.8100
3/4" Meter	\$32.7900
1" Meter	\$41.7300
1-1/2" Meter	\$53.6508
2" Meter	\$86.4400
3" Meter	\$327.8700
4" Meter	\$625.9300
6" Meter	\$864.3700
8" Meter	\$1,092.6000
10" Meter	\$1,748.3300
Effluent: per 1,000 gallons	\$0.5280
Per acre foot	170.3200

AND REPLACE WITH:

Monthly Usage Charge	
5/8" Meter	\$35.6300
3/4" Meter	\$39.2000
1" Meter	\$49.8900
1-1/2" Meter	\$64.1500
2" Meter	\$103.3500
3" Meter	\$392.0100
4" Meter	\$748.3800
6" Meter	\$1,033.4700
8" Meter	\$1,425.2000
10" Meter	\$2,048.7300
Effluent: per 1,000 gallons	\$0.63
Per acre foot	\$205.29

Exhibit A, page 3, on the line identified as "Late Charge, Per Month" DELETE "40.00" and REPLACE with "1.50%."

MAKE ALL CONFORMING CHANGES