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**ORIGINAL**

MEMORANDUM

TO: Docket Control

FROM: Steven M. Olea  
Director  
Utilities Division

DATE: April 27, 2012

RE: STAFF REPORT FOR PICACHO WATER IMPROVEMENT CORPORATION'S APPLICATION FOR AN EMERGENCY RATE INCREASE (DOCKET NO. W-01774A-12-0089).

Attached is the Staff Report for Picacho Water Improvement Corporation's ("Company") application for an emergency rate increase. Staff recommends approval of an emergency revenue increase as described herein.

Any party who wishes may file comments to the Staff Report with the Commission's Docket Control by 4:00 p.m. on or before May 4, 2012.

SMO:JMM:red

Originator: Jeffrey M. Michlik

Arizona Corporation Commission  
**DOCKETED**

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Service List for: Picacho Water Improvement Corporation  
Docket No. W-01774A-12-0089

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**STAFF REPORT  
UTILITIES DIVISION  
ARIZONA CORPORATION COMMISSION**

**PICACHO WATER IMPROVEMENT CORPORATION**

**DOCKET NO. W-01774A-12-0089**

**APPLICATION FOR AN  
EMERGENCY RATE INCREASE**

**APRIL 26, 2012**

## STAFF ACKNOWLEDGMENT

The Staff Report for Picacho Water Improvement Corporation, Docket No. W-0177A-12-0089 is the responsibility of the Staff members listed below. Jeffrey M. Michlik is responsible for the financial review and analysis of the Company's application. Del Smith is responsible for the engineering and technical analysis. Trish Meeter is responsible for reviewing the Commission's records on customer complaints filed with the Commission.



Jeffrey M. Michlik  
Public Utilities Analyst V



Del Smith  
Engineering Supervisor



Trish Meeter  
Consumer Analyst I

**EXECUTIVE SUMMARY**  
**PICACHO WATER IMPROVEMENT CORPORATION**  
**DOCKET NO. W-01774A-12-0089**

Picacho Water Improvement Corporation ("Company") is engaged in the business of providing water services to customers in the unincorporated community of Picacho (Picacho Village), southeast of Eloy in Pinal County, Arizona. The Company provides services to approximately 70 metered customers and its current rates became effective July 1, 1987, per Arizona Corporation Commission Decision No. 55612.

**EMERGENCY RATE CASE**

The Company's emergency rate application requests an increase in revenues of \$88,308 per year in order to remain financially solvent.

**STAFF RECOMMENDATIONS**

Staff recommends approval of an emergency revenue increase of \$43,888 annualized.

Staff further recommends that the Company file a general rate case application within 12 months of a Commission Decision in this matter.

Staff further recommends that the Company file, in conjunction with the ordered rate application filing, a financing application if the Company intends to borrow money to address any infrastructure needs that remain after the Interstate-10 realignment.

Staff further recommends that the Company coordinate the reading of its well meters and individual customer meters on a monthly basis and report this data in its Utilities Division annual report going forward.

Staff further recommends that, in the event the water loss reported in any Annual Report is greater than 10 percent, the Company shall prepare a report containing a detailed analysis and plan to reduce water loss to less than 10 percent. If the Company believes it is not cost effective to reduce the water loss to less than 10 percent, it should submit a detailed cost benefit analysis to support its opinion. In no case shall the Company allow water loss to be greater than 15 percent. The water loss reduction report or the detailed analysis, whichever is submitted per this recommendation, shall be docketed as a compliance item no later than March 31 of the year following the excessive water loss.

Staff further recommends that the Company seek a technical assistance grant from Arizona Department of Environmental Quality ("ADEQ"), to complete a more comprehensive evaluation of the water system post Arizona Department of Transportation ("ADOT") construction prior to investing in the proposed tank repair.

Staff further recommends that the Company file as a compliance item in this Docket proof of its application for a technical assistance grant with the appropriate authority within 45 days of the effective date of the Commission's Decision in this matter.

Staff further recommends that the Company file a curtailment tariff as soon as possible, but no later than forty-five (45) days after the effective date of the Commission Decision in this matter. The tariff should be filed with Docket Control as a compliance item under this same docket number for Staff's review and certification, and the tariff should generally conform to the sample tariff found on the Commission's web site at <http://www.azcc.gov/Divisions/Utilities/forms/CurtailmentStandard2009.doc>.

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## INTRODUCTION

On March 8, 2012, Picacho Water Improvement Corporation ("PWIC" or "Company") filed an application for an emergency rate increase with the Arizona Corporation Commission ("Commission"). A Procedural Order dated March 23, 2012, established May, 7, 2012, as the date for a hearing on the application.

The Company's application implies that the cause of the emergency is the Arizona Department of Transportation's ("ADOT") realigning of a curved section of Interstate 10, that passes through the community of Picacho, which will result in approximately 75 properties being acquired, vacated and demolished as part of the project.<sup>1</sup>

Attorney General Opinion No. 71-17, allows for interim or emergency rates when one of three conditions is present: (1) sudden change brings hardship to a company; (2) the company is insolvent; or (3) the condition of the company is such that its ability to maintain service pending a formal rate determination is in serious doubt.

The Company in its emergency rate application asserts that each of these three conditions has been met, as follows:

1) Situation of sudden change which brings hardship to a Company.

The sudden loss of 53 water users from 127 (42%) due to ADOT's acquisitions causes an immediate reduction of revenue from approximately \$6,666 per month to \$3,866 per month. This loss of users is permanent with no possibility of new settlement in Picacho in the foreseeable future. The situation occurred due to ADOT realignment of Interstate-10 through the Village of Picacho. Mitigation was expected and promised for three years, however, PWIC<sup>2</sup> is now told that no compensation will be paid by ADOT.

All attempts to appeal, arbitrate, and reverse this position have failed to date. We have involved the ACC in our dilemma. In addition to loss of ratepayers, PWIC has accumulated \$50,000 in debt directly related to the impact of ADOT's project over the last 4 years. Our Capital Improvement Plan (To be coupled with rate increase application) has been delayed 3 years due first to uncertainty about the new alignment of Interstate-10 and now to loss of ratepayers to spread the cost of improvements. The CIP was begun in 2006 and could not be completed until May 2009 because of the uncertainty of how to address three different Interstate-10 placement scenarios. We have accumulated engineering, legal, matching fund

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<sup>1</sup> Some of the homes have already been acquired, vacated and demolished.

<sup>2</sup> Picacho Water Improvement Corporation refers to itself as PWIC.

contributions and endless communications and meetings to present our legitimate claims. Extra demands are placed on the Water Company daily due to ADOT demolition and construction activity. Response to two mainline breaks (caused by ADOT) alone cost over \$6,000. ADOT has refused to create a memorandum of understanding or formal mechanism for mitigating its impact. We are endlessly blue staking, identifying pipes, removing meters, fixing pipes, etc.

- 2) Situation where Company is insolvent.

PWIC is insolvent due to the above. Any major equipment breakdown will precipitate a financial crisis.

- 3) Situation where ability of Company to maintain service (pending a formal rate determination) is in serious doubt.

Without some kind of breakthrough with ADOT and/or the Federal Highway Administration (Appears doubtful at this time), operating revenue will be exhausted within 1 month. Any equipment failure (Pump failure for example) cannot be paid for. PWIC has continuous demands by ADOT for services due to its demolition activity in our franchise.

In support of the above, the inability of the Commission to grant permanent rate relief within a reasonable time would be grounds for granting interim relief. This would require that the Company demonstrate that the period needed to grant permanent relief would not be reasonable, given the emergency condition present.

Our financial needs are immediate or we may be forced to curtail services in an emergency fashion leaving residents without water. The ACC has had no influence over ADOT's position.

The Company requests an additional \$83,308 per year in revenues to remain in business, but it did not provide any proposed method or mechanism for recovery of the additional revenue requested.

## **COMPANY BACKGROUND**

The Company is engaged in the business of providing water services to customers in the unincorporated community of Picacho (Picacho Village), southeast of Eloy in Pinal County, Arizona. The Company provides services to approximately 70 metered customers, and its current rates became effective July 1, 1987, per Commission Decision No. 55612.

On March 8, 2012, the Company filed the Emergency rate case described herein.

## **CUSTOMERS**

In response to Staff data request JMM 1-2, the Company stated that it now provides service to 68 residential 5/8 x 3/4-inch metered customers and 2 two-inch metered customers.<sup>3</sup>

## **COMPLIANCE**

A check of the Commission's Compliance database shows no delinquencies for the Company. However, as discussed below, the Company has incurred long-term debt without Commission authorization in violation of A.R.S §40-301.

## **CONSUMER SERVICES ANALYSIS**

Consumer Services reports that the Company is currently in good standing with the Corporations Division.

A search of the Utilities Division database from January 1, 2009, through April 10, 2012, indicates that there have been zero complaints, zero inquires, and zero opinions opposing the emergency rate case request.

## **ENGINEERING ANALYSIS**

### *System Analysis*

The Company's water system well production capacity is 325 gallons per minute (currently there is one well serving the water system),<sup>4</sup> and the system currently has 200,000 gallons of storage capacity. The system has no fire hydrants, and there is no fire flow requirement.

### *Engineering Memorandum*

A discussion of Staff's technical findings and conclusions is provided in the attached Engineering Memorandum.

### *Ability to Maintain Service*

Staff concludes that the Company has adequate production and storage capacity to serve its existing customers and reasonable growth.

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<sup>3</sup> Prior to initiation of ADOT's I-10 realignment project, the Company provided service to 123 residential 5/8 x 3/4-inch metered customers and 2-two-inch metered customers.

<sup>4</sup> The Company has an interconnect agreement with the Picacho Elementary School Public Water System as an alternate source. The Company is not purchasing any water from this alternative.

## FINANCIAL ANALYSIS

Staff applies Attorney General Opinion No. 71-17 when determining if an emergency condition exists. That opinion allows interim or emergency rates when one of three conditions is present: (1) sudden change brings hardship to a company; (2) the company is insolvent; or (3) the condition of the company is such that its ability to maintain service pending a formal rate determination is in serious doubt.

Staff's analysis of each of these three conditions is presented below:

### *Condition One: Sudden change brings hardship to the company*

The Company has known about the Interstate-10 realignment for several years.<sup>5</sup> Staff became aware of the potential effects of the road realignment in October 2011, when Staff met with representatives of ADOT at their request. Staff subsequently coordinated phone calls and meetings that included Staff, ADOT and the Company to facilitate a better understanding of the Company's situation. Staff suggested several times that the Company file requests for a rate increase and financing and, on November 30, 2011, provided Mr. Holmes with both emergency and permanent rate applications and information about the related processes and procedures. Staff again encouraged Mr. Holmes to file for a permanent rate increase, which could be processed without a hearing. Accordingly, Staff concludes that emergency condition one has not been met because there has been no sudden change that brought hardship to the Company.

### *Condition Two: The Company is insolvent*

The Company's annual report for the year ending December 31, 2010, submitted to the Utilities Division of the Commission, indicates an operating loss of \$4,385. The Company's cash flow from operations, assuming no repayment of principal on \$45,000 of long-term debt, is negative \$6,278 (-\$4,385 operating loss - \$3,388 interest expense + \$1,497 depreciation expense). The Company's 2010 annual report shows that it has three loans: (Great Western Bank, October 28, 2003, \$25,000; Mrs. Holmes, March 1, 2006, \$5,000; and Hank Holmes, March 1, 2007, \$15,000.)<sup>6</sup> According to the Company's 2010 annual report, it repaid \$1,000 of principal on the Great Western Bank loan in 2010 and that was the only repayment of these loans since their inception. The 2010 annual report also shows a \$19,464 negative equity position caused by accumulated losses of \$32,803 and a cash balance of \$6,814. This financial information shows that the Company has been operating at a loss over an extended period and has borrowed \$45,000 of which \$6,814 remained on hand at the end of 2010 to cover continuing cash deficiencies. Moreover, the Company's negative equity position and outstanding debt are significant obstacles for issuing additional debt. The Company's negative cash flow and its

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<sup>5</sup> Per review of correspondence between ADOT and the Company, the Company states that its first meaningful contact occurred on April 13, 2009.

<sup>6</sup> The Company has not obtained Commission authorization to issue debt as required by A.R.S. § 40-301. The Company refinanced the Great Western Bank loan in the amount of \$24,667 on February 4, 2011. These debt issuances are invalid without the required regulatory approvals.

limited ability to issue additional debt will result in its inability to pay its obligations as they come due once its cash balance is absorbed. Loss of a large portion of the Company's customer base is likely to exacerbate the Company's cash flows compared to the 2010 results. Thus, the Company does not have the capacity to cover any additional costs related to the ADOT I-10 realignment. Accordingly, Staff concludes that the Company is insolvent, and it meets emergency condition two.<sup>7</sup>

*Condition Three: The Company's ability to maintain service pending a formal rate determination is in serious doubt*

As described in Staff's engineering memorandum, the Company is in compliance with the Arizona Department of Water Resources ("ADWR") reporting requirements, it is in compliance with the Arizona Department of Environmental Quality ("ADEQ") requirements, it is currently delivering water that meets water quality standards and it has adequate production and storage capacity to serve its existing customers and reasonable growth. Accordingly, Staff concludes that emergency condition three has not been met.

*Staff's determination of whether emergency interim rates are warranted*

Staff concludes that one of the conditions for eligibility for emergency rates exists – the Company is insolvent.

### **COMPANY'S PROPOSED EMERGENCY REVENUE CALCULATION**

The Company's application states that it would need an additional \$83,308<sup>8</sup> per year in revenue to remain in business, summarized as follows:

1. Lost Revenue from operations (Fixed Costs)	\$24,000
2. Emergency Fund	\$15,000
3. Temporary Patch Failing 200,000 Storage Tank	\$20,000
4. Engineering (Response to ADOT)	\$10,000
5. Increased Operations responding to I-10 construction	\$15,000
6. Service on \$25,000 loan	<u>\$ 4,308</u>
	\$88,308 per year

In its response to Staff data request JMM 1-3, the Company described its calculation of each component as follows.

1. Lost revenue from operations (\$24,000):

$$\text{Average Revenue per Year} = \$65,000 \times 0.42 \text{ (42\% of ratepayers lost)} = \$27,300.^9$$

<sup>7</sup> Staff notes that the Company has greatly contributed to its own insolvency by not filing rate applications despite years of operating without a profit and by borrowing funds without regulatory approval.

<sup>8</sup> \$83,308 is apparently a typographical error since the sum of detailed request is \$88,308 per year.

2. Emergency fund (\$15,000):

Over the years a major repair (pulling a failed pump, etc) has cost PWIC in the range of \$10,000 plus or minus. We have averaged a major every 2 years. The last two repairs required urgent loans from stockholders. PWIC has no reserves to handle major repairs and \$15,000 in reserves would allow continued operation despite expected emergencies.

3. Temporary patch for storage tank (\$20,000):

Please see Attachment A which is a bid for placing a steel ring 2 feet high around the base of our 200,000 gal storage tank which is past its useful lifetime (50 years), is rusted out at the bottom and bulging, has been welded several times, could fail at any time, and would be very expensive to replace. The bid is for \$25,000, but we are hoping to negotiate lower. See attached Picture labeled Attachment B. It is estimated that this will extend the life of the tank for 5-10 years. This time would allow PWIC to replace with loans or grants.

4. Engineering response to ADOT (\$10,000):

In August of 2011, PWIC hired a Water Engineer (Bill Collings) specifically for the purpose of representing us in interactions with ADOT which we could not avoid. We are to interface with their engineers in the design and placement of replacement mainlines to maintain the integrity of our system. Attachment C is the unsigned contract with Mr. Collings' rates. ADOT denies responsibility for this impact even though it is necessitated by their construction. For the four month period August 2011 - Jan 2012 we have paid Mr. Collings \$3450. This expense is expected to continue at approximately the same level/ rate over the next two years during ADOT's demolition and construction. Four months at \$3450 computes to \$10,350 per year.

5. Increased operations responding to Interstate-10 construction (\$15,000):

ADOT's project demands a lot of our operator beyond what he is paid for such as endless Blue Staking, fixing breaks (most expensive of which have been mainline breaks to our Asbestos Cement main-lines), locating valves and pipes, on site availability from 30-60 minutes distant depending on whether he is at home or out on his ranch. Major breaks entail hiring a contractor with the equipment and expertise to come from Tucson. Since ADOT began demolition preparations and demolition our costs have been \$16,897 (See Attachment D) of which we have received no reimbursement. We have hope that an agreement will be reached, however that does not look possible now.

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<sup>9</sup> Staff notes the Company's calculation does not equal the \$24,000 stated in the emergency rate application.

Attachment E is ADOT's current position expressed in three different documents by Pete Mayne, Dallas Hammitt, summarizing an ADOT review of our claims, and confirmed by Pete Mayne. PWIC feels that \$15,000 year for the period of construction is very conservative.

6. Service on \$25,000 loan (\$4,308):

We apologize for providing an incorrect figure. The correct figure is \$3708/year. Attachment F is the loan document from Key Bank. In 2011, Key Bank would not renew this PWIC loan without a guarantor and President Hank Holmes, became the stockholder guarantor for the PWIC Loan. At that time mitigation compensation from ADOT had been promised and seemed eminent, part of which would be used to pay off the loan. That now has changed. The monthly payment, interest and principal is \$309.00 month x 12 = \$3708.00 year. The loan exists because PWIC has had to divert revenue to respond to ADOT's impact rather than to this loan.

**STAFF'S RECOMMENDED EMERGENCY INTERIM RATES AND REVENUE CALCULATION**

Since Staff deems the Company insolvent due to insufficient generation of cash flow to meet on-going obligations, the purpose of any authorized emergency rates would be to satisfy the cash flow deficiency until rates can be established in a general rate case. Based on the Company's 2010 reported operating results and analysis of the Company's emergency rate application, Staff has calculated a \$43,888 annualized cash flow deficit, as follows:

*Per Annual Report:*

Operating Income/(Loss)	\$ (4,385)
Depreciation Expense	(1,497)
Interest Expense	(3,388)
Principal Repayment	(1,000)
Advance Refunds	<u>0</u>
Cash Flow Per Annual Report	<u>\$ (5,276)</u>

*Staff Adjustments:*

Interest Expense	\$ 3,388
Principal Repayment	1,000
Adjusted 2010 Cash Flow	(888)
Pro forma Lost Revenue	(24,000)
Allowance for incremental I-10 realignment costs	(15,000)
Allowance for Contingencies	(4,000)
Total Annualized Cash Flow Deficiency	<u>\$(43,888)</u>

As shown in the calculation, Staff removed the debt principal and interest payments because the Company has not obtained Commission authorization for these loans; accordingly, they are invalid. Due to the Company's insolvency, Staff concludes that evaluation of any request for approval of the Company's loans should be conducted within the context of the Company's general rate case that will follow this emergency rate case. Staff's cash flow deficiency calculation reflects the Company's estimate for lost revenue and incremental Interstate-10 realignment costs, as Staff concludes that these estimates are reasonable. The \$4,000 allowance for contingencies recognizes the inability to accurately estimate the incremental costs of the Interstate-10 realignment, as well as potential deviation in other expenses from that experienced in 2010. Staff concludes that the Company's emergency request for Engineering costs related to the Interstate-10 construction and costs to temporarily patch the storage tank should not be included in the emergency rates. Payment of the Engineering costs has not been shown to be urgent, and Staff does not support patching the storage tank until a more comprehensive evaluation of the water system post ADOT construction has been performed.

Staff has examined the Company's current tariff schedule which was approved in Decision No. 55612 and notes that the current monthly charge for a 5/8 x 3/4-inch metered customer is \$14.00 and for a 2-inch metered customer is \$21.00. Staff also notes that the commodity charge is \$1.50 per 1,000 gallons, and no charge for the first 2,000 gallons.

Staff recommends the following emergency interim rate surcharges to provide the cash flow deficiency. The emergency interim rate surcharge should appear as a separate line item on the customer's bill, in addition to the monthly minimum amount and commodity charge. Staff recommends the following surcharge per customer:

5/8 x 3/4-inch metered customer	\$50.80
2-inch metered customer	\$101.60

The surcharge amounts were derived as follows:

Meter Size	Monthly Surcharge	Number of Customer	x 12	Yearly Revenue Amount
5/8 x 3/4-inch	\$50.80	68	12	\$41,453
2-inch	\$101.60	2	12	\$ 2,438
				\$43,891

Staff has prepared a typical bill analysis based on usage of 5,000 gallons per month. Staff did not have billing determinants for calculating the actual average and median usage. Moreover, the existing billing determinants may not be representative of the remaining customers, i.e., usage of the remaining customers may vary from those of the lost customers. A 5/8 x 3/4-inch metered customer using 5,000 gallons would experience a \$36.80 dollar increase, or a 198.92 percent increase, in his/her monthly bill, from \$18.50 to \$55.30, under Staff's recommended interim rates.

## **OTHER ITEMS**

Staff also advises the Company that the emergency rates are potentially refundable in the event that the Commission determines during the ensuing permanent rate case that the Company collections were excessive.

In response to Staff data request JMM 1-1, the Company indicated that it had previously avoided applying for a rate increase because of its understanding that the process required hiring an attorney and was expensive (\$20,000). Staff notes that, unless the Company's requested annual revenues exceed \$250,000, the Company is eligible to file the "short form" rate application, and it is not required to hire an attorney or other consultants.

## **STAFF RECOMMENDATIONS**

Staff recommends approval of an emergency revenue increase of \$43,888 annualized.

Staff further recommends that the Company file a general rate case application within 12 months of a Commission Decision in this matter.

Staff further recommends that the Company file, in conjunction with the ordered rate application filing, a financing application if the Company intends to borrow money to address any infrastructure needs that remain after the Interstate-10 realignment.

Staff further recommends that the Company coordinate the reading of its well meters and individual customer meters on a monthly basis and report this data in its Utilities Division annual report going forward.

Staff further recommends that in the event the water loss reported in any Annual Report is greater than 10 percent, the Company shall prepare a report containing a detailed analysis and plan to reduce water loss to less than 10 percent. If the Company believes it is not cost effective to reduce the water loss to less than 10 percent, it should submit a detailed cost benefit analysis to support its opinion. In no case shall the Company allow water loss to be greater than 15 percent. The water loss reduction report or the detailed analysis, whichever is submitted per this recommendation, shall be docketed as a compliance item no later than March 31 of the year following the excessive water loss.

Staff further recommends that the Company seek a technical assistance grant from ADEQ, to complete a more comprehensive evaluation of the water system post ADOT construction prior to investing in the proposed tank repair.

Staff further recommends that the Company file as a compliance item in this Docket proof of its application for a technical assistance grant with the appropriate authority within 45 days of the effective date of the Commission's Decision in this matter.

Staff further recommends that the Company file a curtailment tariff as soon as possible, but no later than forty-five (45) days after the effective date of the Commission Decision in this matter. The tariff should be filed with Docket Control as a compliance item under this same docket number for Staff's review and certification, and the tariff should generally conform to the sample tariff found on the Commission's web site at <http://www.azcc.gov/Divisions/Utilities/forms/CurtailmentStandard2009.doc>.

**MEMORANDUM**

**DATE:** April 20, 2012

**TO:** Jeff Michlik  
Public Utility Analyst V

**FROM:** Del Smith *DS*  
Engineering Supervisor

**RE:** **Picacho Water Improvement Corporation  
Application for Approval of an Emergency Rate Increase  
(Docket No. W-01774A-12-0089)**

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**Introduction**

Picacho Water Improvement Corporation ("Company" or "Picacho") serves the Village of Picacho. The Village of Picacho is located where State Route 87 intersects with Interstate 10 ("I-10") southeast of Eloy. The Company serves a four square mile area which includes all of Sections 14, 15, 22 and 23 of Township 8 South and Range 8 East in Pinal County.

On March 8, 2012, the Company filed with the Arizona Corporation Commission ("Commission" or "ACC") an application for an emergency rate increase. The Company indicated that its request for an emergency rate increase was necessary, because it has experienced the sudden loss of 53 of its water users, with an immediate reduction in revenue of \$2,806, as well as a number of expenses resulting from activity caused by the Arizona Department of Transportation's ("ADOT's") realignment of I-10 through the Village of Picacho. The Company reported that prior to disconnections due to the realignment there were 129 customers served and subsequent to disconnections there will be 70 customers.<sup>1</sup> Picacho's current rates were approved in Commission Decision No. 55612, effective June 17, 1987. According to the Company's operator septic tanks are used in Picacho's service area for wastewater service.

**Picacho Water System**Description of the Water System

The Picacho water system was visited on March 30, 2012, by Del Smith, of Commission Utilities Division Staff ("Staff"), in the accompaniment of Mr. Ed Kile. Mr. Kile is responsible for the day-to-day operation of the Picacho water system and is the Company's Certified Operator. The Picacho facility is classified as a Grade 1 Distribution system and Mr. Kile is a Grade 1

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<sup>1</sup> See Company's response to JMM 1-2.

Distribution system and Treatment plant Certified Operator. Mr. Kile's Arizona Department of Environmental Quality ("ADEQ") Operator Identification Number is OP001151.

The yard at the operating well site (Water Plant No. 1 located north of I-10) was reasonably well maintained and the in-service plant (i.e., well, tanks, visible pipe and valves) seemed to be in good working order. Staff did not observe any existing leaks at the well site or in the distribution area. The storage tank and pressure tank at Water Plant No. 1 were in poor condition due to age. The storage tank showed signs of multiple repairs at its base. Staff, however, did not see anything to indicate that a major failure was imminent or about to occur. Staff observed that the plant at the secondary well site (Water Plant No. 2 located south of I-10) had been disconnected from the system and was not in-service. The inactive plant included the well (Arizona Department of Water Resources ("ADWR") Registration No. 55-622044) and a pressure tank.<sup>2</sup>

The water system consists of one operating well (ADWR Registration No. 55-622043) which has a pump yield of 325 gallons per minute ("GPM"). The well feeds water to one 200,000 gallon storage tank. Water pressure in the system is increased prior to being delivered to customers through a booster system consisting of two 25 horsepower booster pumps and a 7,500 gallon hydro-pneumatic pressure tank. The distribution system includes a combination of 4-inch, 6-inch and 8-inch asbestos-cement pipe ("ACP"). Picacho has an interconnection agreement with the Picacho Elementary School (ADEQ Public Water System ("PWS") No. 11-072) which would enable it to purchase water from an alternative source. Staff understands this agreement has never been used.

### System Analysis

The Picacho water system well production capacity is 325 GPM (currently there is one well serving the water system and no water is being purchased from the school) and the system currently has 200,000 gallons of storage capacity. There are no fire hydrants and the system does not have a fire flow requirement. The Company reported 3,456,000 gallons sold during the peak month of November 2011. Staff concludes that the Company has adequate production and storage capacity to serve its existing customers and reasonable growth.

### Water Loss

Non-account water should be 10 percent or less. It is important to be able to reconcile the difference between water sold and the water produced by the source. A water balance will allow a company to identify water and revenue losses due to leakage, theft and flushing. Lost water for Picacho was calculated to be over 19 percent in 2011 which exceeds Staff's recommended threshold of 10 percent. Staff noted that in reviewing prior year annual report records for 2007, 2008 and 2009 that the Company had lost water levels that were less than 10 percent. Staff believes that the water loss may be higher in 2011 due in part to ADOT demolition activities and the resulting main line breaks.

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<sup>2</sup> The inactive well was taken off-line several years ago due to maintenance issues and a high operating cost.

The Company also reported the same gallons pumped each month during 2011 which invalidates the result since the calculation should be based on the actual quantity of gallons pumped each month as read at the source meter. Staff recommends that the Company coordinate the reading of its well meters and individual customer meters on a monthly basis and report this data in its Commission Annual Reports going forward.<sup>3</sup> Staff further recommends in the event the water loss reported in any Annual Report is greater than 10 percent, the Company shall prepare a report containing a detailed analysis and plan to reduce water loss to less than 10 percent. If the Company believes it is not cost effective to reduce the water loss to less than 10 percent, it should submit a detailed cost benefit analysis to support its opinion. In no case shall the Company allow water loss to be greater than 15 percent. The water loss reduction report or the detailed analysis, whichever is submitted per this recommendation, shall be docketed as a compliance item no later than March 31 of the year following the excessive water loss.

## **ADEQ Compliance**

### Drinking Water Compliance Status Report

Staff received an ADEQ Drinking Water Compliance Status Report dated November 18, 2011, in which ADEQ reported that the Picacho water system, PWS No. 11-042, is in compliance with ADEQ requirements and is currently delivering water that meets water quality standards required by Arizona Administrative Code, Title 18, Chapter 4.

### September 9, 2011 Sanitary Survey

The last ADEQ compliance inspection of the Picacho water system occurred on September 9, 2011. Based upon the inspection, ADEQ determined that the operation and maintenance of the physical plant was in compliance with ADEQ Rules. In the report the ADEQ inspector noted that the storage tank and pressure tank were in poor condition due to age. No ADEQ action resulted from the inspection.

## **ADWR Compliance**

ADWR reported in an email sent to Staff on March 22, 2012, that there were no issues for Picacho and that the Company was in compliance with ADWR reporting requirements.

## **ACC Compliance**

A check of the Utilities Division Compliance Database indicates that there are currently no delinquent compliance items for Picacho.

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<sup>3</sup> The Company shall collect the data needed to accurately complete the water use data sheets contained in the Annual Report form.

## **Other Issues**

### Temporary Patch Failing 200,000 Storage Tank (Old Deteriorating 200,000 Gallon Storage Tank Nearing End of Useful Service Life)

The Company's only storage reservoir is old and in need of replacement. In its application for an emergency rate increase the Company requested \$20,000<sup>4</sup> to extend the life of this storage tank until the Company can obtain funds to replace the tank. The Company indicated that the tank was past its useful life of 50 years, was rusted out at the bottom, and could fail at any time. While ADEQ noted in its last inspection report that this storage tank was in poor condition, it concluded that the operation and maintenance of the water system was in compliance with its Rules. In addition, Staff did not see anything during its inspection to indicate that a major failure of this tank was imminent or about to occur. At this time Staff believes it would be more prudent to seek a technical assistance grant from ADEQ to complete a more comprehensive evaluation of the water system post ADOT construction. The economics of replacing the existing 200,000 gallon storage tank with a smaller capacity tank is one option that the Company should consider.

### Increased Operations Responding to I-10 Construction (Pipe Repair Expenses Directly Related to ADOT Demolition and Construction Activity)

According to the Company it is incurring unforeseen pipe repair expenses directly related to the I-10 realignment demolition and construction activity. The majority of the distribution system pipe is made of ACP.<sup>5</sup> This Pipe is approaching the end of its useful service life and like all old pipe is more prone to failure due to leaks, breaks, cracking and joint separation, especially in an area where heavy equipment is being operated. During its site inspection Staff observed the area where major leaks had occurred and where heavy equipment operation and demolition activities were continuing in close proximity to the Company's lines. It is reasonable to expect that more breaks will occur as the construction continues. The Company reported that it has already spent almost \$17,000 on pipe repairs directly related to ADOT activity. Staff concludes that the Company's estimate of costs to cover unforeseen pipe repair expenses is reasonable.

### Cross Connection /Backflow Tariff

The Company has an approved Cross Connection Tariff.

### Curtailement Tariff

The Company does not have an approved Curtailement Tariff. Staff recommends that the Company file a curtailement tariff as soon as possible, but no later than forty-five (45) days after the effective date of the Commission Decision in this matter. The tariff shall be filed with Docket Control as a compliance item under this same docket number for Staff's review and

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<sup>4</sup> The actual bid received to complete the proposed tank repairs was for \$25,000. The Company was hoping to negotiate the lower \$20,000 figure.

<sup>5</sup> ACP is no longer used for this purpose due to the danger of asbestos exposure during production, installation and maintenance of the pipe.

certification. Staff further recommends that the tariff shall generally conform to the sample tariff found on the Commission's web site at <http://www.azcc.gov/Divisions/Utilities/forms/CurtailmentStandard2009.doc>.

## **Summary**

### **Conclusions**

1. Staff concludes that the Company has adequate production and storage capacity to serve its existing customers and reasonable growth.
2. ADWR reported that there were no outstanding issues for Picacho and that the Company was in compliance with ADWR reporting requirements.
3. ADEQ reported that the Picacho water system is in compliance with ADEQ requirements and is currently delivering water that meets water quality standards required by Arizona Administrative Code, Title 18, Chapter 4.
4. A check of the ACC Utilities Division Compliance Database indicates that there are currently no delinquent compliance items for Picacho.
5. Staff concludes that the Company's estimate of costs to cover unforeseen pipe repair expenses is reasonable.

### **Recommendations**

1. Staff recommends that the Company coordinate the reading of its well meters and individual customer meters on a monthly basis and report this data in its Commission Annual Reports going forward. Staff further recommends in the event the water loss reported in any Annual Report is greater than 10 percent, the Company shall prepare a report containing a detailed analysis and plan to reduce water loss to less than 10 percent. If the Company believes it is not cost effective to reduce the water loss to less than 10 percent, it should submit a detailed cost benefit analysis to support its opinion. In no case shall the Company allow water loss to be greater than 15 percent. The water loss reduction report or the detailed analysis, whichever is submitted per this recommendation, shall be docketed as a compliance item no later than March 31 of the year following the excessive water loss.
2. Staff recommends the Company seek a technical assistance grant from ADEQ, to complete a more comprehensive evaluation of the water system post ADOT construction prior to investing in the proposed tank repair. Staff recommends that the Company file as a compliance item in this Docket proof of its application for a technical assistance grant with the appropriate authority within 45 days of the effective date of the Commission's Decision in this matter.

3. Staff recommends that the Company file a curtailment tariff as soon as possible, but no later than forty-five (45) days after the effective date of the Commission Decision in this matter. The tariff shall be filed with Docket Control as a compliance item under this same docket number for Staff's review and certification. Staff further recommends that the tariff shall generally conform to the sample tariff found on the Commission's web site at <http://www.azcc.gov/Divisions/Utilities/forms/CurtailmentStandard2009.doc>.