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BRENDA BURNS

OPEN MEETING ITEM

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Arizona Corporation Commission
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DOCKETED BY

ARIZONA CORPORATION COMMISSION

DATE: MAY 8, 2012

DOCKET NOS.: W-01651B-99-0351 and W-01651B-99-0406

TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Jane L. Rodda. The recommendation has been filed in the form of an Opinion and Order on:

VAIL WATER COMPNAY
(REOPEN DECISION NO. 62450)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and thirteen (13) copies of the exceptions with the Commission's Docket Control at the address listed below by **4:00** p.m. on or before:

MAY 17, 2012

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Open Meeting to be held on:

MAY 22, 2012 and MAY 23, 2012

For more information, you may contact Docket Control at (602) 542-3477 or the Hearing Division at (602) 542-4250. For information about the Open Meeting, contact the Executive Director's Office at (602) 542-3931.

ERNEST G. JOHNSON
EXECUTIVE DIRECTOR

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

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

IN THE MATTER OF THE APPLICATION OF VAIL WATER COMPANY FOR AUTHORITY TO ISSUE PROMISSORY NOTE(S) AND OTHER EVIDENCE OF INDEBTEDNESS PAYABLE AT PERIODS OF MORE THAN TWELVE MONTHS AFTER THE DATE OF ISSUANCE.	DOCKET NO. W-01651B-99-0351
IN THE MATTER OF THE APPLICATION OF VAIL WATER COMPANY FOR A RATE INCREASE.	DOCKET NO. W-01651B-99-0406 DECISION NO. _____

OPINION AND ORDER

DATE OF HEARING:	January 26, 2012, and March 29, 2012
PLACE OF HEARING:	Tucson, Arizona
ADMINISTRATIVE LAW JUDGE:	Jane L. Rodda
APPEARANCES:	Mr. Michael Hallam and Mr. Matt Bingham, LEWIS AND ROCA, LLC, on behalf of Vail Water Company; and Ms. Bridget A. Humphrey, Staff Attorney, Legal Division, on behalf of the Utilities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

* * * * * * * * * *

Having considered the entire record herein and being fully advised in the premises, the Arizona Corporation Commission ("Commission") finds, concludes, and orders that:

FINDINGS OF FACT

1. On December 1, 2011, the Commission voted to reopen Docket No. W-01651B-99-0406 and Decision No. 62450 (April 14, 2000) for the purpose of taking evidence to determine the

following: 1) a plan for the direct use of Central Arizona Project ("CAP") water in Vail Water Company's ("VWC") service area; 2) whether funds collected from Hook-up Fees and a CAP Surcharge authorized in Decision No. 62450 should be refunded; 3) whether the Company should be assessed penalties for failing to comply with Decision No. 62450; and 4) whether to grant the Company's request for an extension of the deadline in Decision No. 62450 to file Final Plans for the direct use of CAP water.

Background

2. In Decision No. 62450 the Commission granted VWC a rate increase, and approved the Company's request for authority to borrow from the Arizona Water Infrastructure Finance Authority ("WIFA") to finance system improvements. As part of Decision No. 62450, the Commission authorized VWC to implement a CAP Hook-up Fee and a CAP surcharge.

3. The Commission conditioned the CAP Hook-up Fee and Surcharge on the following:[1]

a. The tariff would apply to all new subdivisions and line extension agreements that are approved for the north system from the end of 1998 TY forward. Once the interconnection between the north and south systems is completed, the tariff would apply to all new subdivisions and line extension agreements in the combined north and south systems;

b. VWC must be recharging CAP water within 6 months of this Decision;[2]

c. All CAP Hook-Up Fees and CAP Service charges are to be placed in a separate interest bearing account;

d. Revenue collected from the CAP Hook-up Fee and CAP Service Charge can be used for paying the CAP holding fee and Municipal and Industrial ("M&I") costs, and the Hook-up Fees could also be used for CAP-related capital projects;[3]

e. The CAP Service Charge shall be identified as a separate line item charge on the customer bill;

f. Final plans for the direct use of CAP water within VWC's service

[1] Decision No. 62450 at Findings of Fact ("FOF") No. 25 and Conclusions of Law ("COL") No. 7.

[2] Decision No. 62450 contemplated that until VWC could use its CAP allocation to provide water to its customers, it would recharge the water. VWC has been recharging its CAP allocation in Marana near the CAP canal at a recharge facility operated by Kai Farms. The recharge facility is over 30 miles from VWC's service area. *See* Transcript of the January 26, and March 29, 2012 hearings ("Tr.") at 45.

[3] Staff's recommendations as set forth in FOF 25 originally would have limited the use of the Hook-up Fees and Surcharge to the CAP holding fees and M&I costs, but the Commission expanded the permissible uses of the funds when it adopted Decision No. 62450. *See* Decision No. 62450 at COL No. 7.

territory are to be submitted to the Commission no later than December 31, 2010;

g. VWC must directly use the CAP allocation within its service territory by December 31, 2015;

h. Time extensions would only be allowed for good cause;[4]

i. VWC shall submit annual reports to the Utilities Division Director detailing the progress of plans to use CAP water directly in its service territory and plans for actual construction of any necessary facilities. The reports shall be submitted each July 1, beginning in 2001;

j. If VWC does not comply with either of the timeframes in f or g, all CAP charges will cease at that time and any monies remaining in the CAP account shall be refunded in a manner to be determined by the Commission at that time;

k. The Commission shall allow Staff to automatically impose fines and/or other sanctions against Vail if the timeframes in items f or g are not met;

l. If VWC does not comply with the timeframes in items f or g and it sells its CAP allocation, any net profit shall be distributed to the customers in a manner to be determined by the Commission; and

m. VWC should submit annual reports regarding the amount of CAP Hook-up Fee and CAP Service Fees collected. The reports should be submitted by each January 31 and cover the previous calendar year, The first report should be submitted by January 31, 2001, and should contain the following information:

i. The name of each entity paying a CAP Hook-up Fee;
ii. The amount of CAP Hook-up Fee each entity paid;
iii. The amount of CAP Service Charge collected;
iv. The balance in the CAP trust account;
v. The amount of interest earned in the CAP trust account;
vi. The amount of money spent from the CAP trust account; and
vii. A description of what was paid for with monies from the CAP trust account.

4. VWC did not file Final Plans for the direct use of CAP water within its service territory by December 31, 2010.

5. On June 21, 2011, Staff sent a formal Compliance Notification Letter to VWC, stating that the Company failed to meet requirement (f) when it did not file Final Plans by December 31, 2010. This letter stated that the Company's failure to meet the deadline rendered the Company in violation of both Decision No. 62450 and Arizona Revised Statute ("A.R.S.") §40-202 which

[4] *Id.* Staff originally recommended that no time extensions be allowed.

requires the Company to comply with every "order, decision, rule or regulation" of the Commission. The letter also notified the Company that pursuant to FOF 25 (j), when the Company failed to file the Final Plans by the deadline, the CAP charges should cease and the remaining monies refunded.

6. On June 30, 2011, the Company submitted a request for an extension until November 30, 2011, to file the Final Plans. The Company stated that a viable solution for delivering CAP water to VWC had not been available until June 2011, when the City of Tucson entered into an agreement with Oro Valley to wheel CAP water. VWC believed the Oro Valley wheeling agreement would serve as a template for an agreement between Tucson and other providers, such as VWC. VWC stated that although it would approach the City of Tucson for its own wheeling agreement as soon as the Oro Valley Agreement was finalized, some time would be needed to negotiate and approve the agreement so VWC was requesting until November 30, 2011, to file the Final Plans.

7. On August 2, 2011, Staff sent a second letter to the Company entitled "Compliance Status Notification #2." In this letter, Staff wrote:

> "... consistent with Finding of Fact 25 (j), the Company should immediately cease CAP collections and propose to the Commission a mechanism to refund any monies remaining in the CAP account. This proposal should be submitted to the Commission by August 19, 2011. Further, the Company is notified that any CAP funds collected since January 1, 2011 were collected in violation of a Commission order."

8. On August 17, 2011, VWC filed a request to withdraw its earlier request for extension.

9. On August 19, 2011, VWC filed an Application to Extend Time for CAP Planning. In its Application, the Company requested an extension until June 30, 2013, to provide the Final Plans for direct use of CAP water. VWC indicated that in 2010, Tucson Water approved the Joint Water Infrastructure Supply and Planning Study which lead to the adoption of the City/County 2011-2015 Action Plan for Water Sustainability in November 2010. According to VWC, the Action Plan reaffirmed the goal of enabling Tucson Water to become a CAP wheeling entity in the Tucson valley.[5] VWC also stated that following the approval of the Tucson/Oro Valley wheeling agreement in June 2011, it contacted Tucson Water and negotiations began in earnest. Tucson Water estimated

[5] *See* www.tucsonpimawaterstudy.com.

that the process to develop a wheeling agreement would take between six and twelve months.[6] The Company explained it was seeking the Commission's permission to provide the Final Plans by June 30, 2013, and that it was not asking for an extension of the 2015 deadline for the direct delivery of CAP water to VWC. The Company asserted that although it was unable to have a solution for the direct use of CAP water by the end of 2010, the direct use of CAP remains a goal that the Commission should encourage; that the millions of dollars already spent to secure the CAP supply will have been wasted if the deadline to file Final Plans was not adjusted "to comport with Tucson Water's availability"; and that the Company needed the City to be a willing partner which meant that the Company could not have exclusive control of the terms or timing of any Final Plans.

10. On November 1, 2011, Staff filed a Memorandum setting forth Staff's conclusions and recommendations. Staff believed that VWC was in violation of Decision No. 62450 by not providing Final Plans, failing to cease collection of CAP charges, and failing to refund monies remaining in the CAP account. In addition, Staff claimed that the Company was also in violation of A.R.S. § 40-202 for not filing a proposed refunding mechanism. Staff expressed concern that the request for the extension was filed approximately six months after the due date, and only after Staff notified the Company of the compliance violation. Staff concluded that it could not recommend granting the Company's request for an extension of the deadline to file the Final Plans. Staff recommended that VWC file a status update by November 15, 2011, that clarifies: 1) whether the Company has ceased collecting CAP charges and if not, an explanation why not; 2) what refunding mechanism the Company proposes and why none was proposed earlier; 3) whether refunds have started, and if not, an explanation of why not; and 4) an accounting of the funds in the CAP account. Staff reserved the right to make further recommendations based on the quality and timeliness of the Company's status update.

11. On November 15, 2011, VWC filed a Status Update. VWC claimed that after receiving Staff's second compliance notice, it contacted Staff and was told that it should withdraw its request for an extension and seek an amendment of Decision No. 62450. The Company states that it

[6] Exhibit B to VWC's August 19, 2011, Application to Extend Time of CAP Planning.

intended its August 19, 2011, Application to be a request to amend Decision No. 62450. In addition, VWC responded to Staff's inquiries as follows: 1) VWC suspended billing for CAP Service Charges in November 2011, and if the Commission so directs, will also suspend collections of CAP Hook-up Fees; 2) within thirty days, VWC will have refunded all CAP Service Charges collected since the beginning of 2011 as credits against the customer's November water bills, and will if the Commission directs, refund unexpended CAP Hook-up Fees and other CAP Service Charges; 3) VWC believed that the Commission would not lightly abandon the objective of using CAP water in its service area by 2015, and that it believed it was acting in good faith to extend the 2010 deadline to submit engineering plans; and 4) it provided a report of the revenues and expenditures in the CAP account through November 14, 2011. VWC also described its efforts to work with Tucson Water and re-iterated the importance of importing CAP water into the Tucson Active Management Area ("Tucson AMA").

12. On November 30, 2011, VWC filed a Status Update. The Company clarified that based on the language of Decision No. 62450 that provides that refunds would be accomplished "as determined by the Commission," the Company would wait for direction from the Commission before refunding any amounts in the CAP account.

13. On December 1, 2011, the Commission voted to reopen Docket No. W-01651B-99-0406 and Decision No. 62450, in order to refer the matter to the Hearing Division to take testimony on the following topics: 1) a plan to accomplish the direct use of CAP water in VWC's service area; 2) whether there should be a refund of CAP surcharges; 3) whether penalties should be assessed against the Company for the violation of Commission Order; and 4) to consider the Company's request for a time extension to file its final plans for direct use of the CAP water. The Commission directed that all CAP charges collected that remain in the CAP account should be held in constructive trust until further order of the Commission.

14. By Procedural Order dated December 2, 2011, a Procedural Conference convened on December 14, 2011 to discuss the procedures and timeline for the proceeding. The Company requested a quick resolution in order to have the matter resolved before payments to the CAP were due in the Spring of 2012. Both parties thought that pre-filed testimony would be beneficial, but

Staff's availability did not allow a complete hearing in January 2012. The parties agreed to a bifurcated proceeding.[7]

15. By Procedural Order dated December 15, 2011, the matter was bifurcated for purposes of a hearing, with a hearing set for January 26, 2012, to address the limited issue of the Company's request to use the CAP funds held in constructive trust for annual payments related to its CAP allocation due in March 2012; and a second hearing on February 29, 2012, to address all of the other issues in the Commission's December 1, 2011 directive.

16. On January 6, 2012, VWC filed Certification that it mailed public notice of the hearings to its customers as a bill insert on December 30, 2011, as directed by the Commission's Procedural Order.

17. On January 23, 2012, VWC filed the Direct Testimony of Kip Volpe, the Company's Vice President, and Staff filed the Direct Testimony of Brian Bozzo, the Commission's Utilities Division Compliance and Enforcement Manager.

18. The hearing on the Company's request to use funds in its CAP account for payments to the CAP convened as scheduled before a duly authorized Administrative Law Judge ("ALJ") on January 26, 2012, at the Commission's Tucson offices.

19. During the January 26, 2012, hearing, the Company requested that the Commission authorize it to use funds in its CAP account to make the following payments to the CAP: $75,500 due on February 20, 2012; $89,500 due on March 20, 2012; and $75,500 due on April 20, 2012.[8] The Company argued that the direct use of CAP water in VWC's service territory remains a viable goal that will benefit VWC ratepayers, the Tucson AMA and the state of Arizona because the costs of providing CAP water to the area will be less than the cost of acquiring recharge credits from the Central Arizona Groundwater Replenishment District ("CAGRD")[9] and VWC's CAP allocation allows CAP water to benefit the Tucson valley and will help protect Arizona's claim on Colorado River water.[10]

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[7] *See* Transcript of December 14, 2011, Procedural Conference.
[8] Ex A-1, Volpe Dir at 7.
[9] Tr. at 18 and 42.
[10] Ex A-1 at 5 and Tr. at 24.

20. At the January 2012 hearing, based on the language of Decision No. 62450, Staff recommended that the Company not be allowed to use the funds remaining the CAP account to make the requested payments.[11] Staff argued that the up-coming payments could be paid with other funds,[12] or that the payments could be made late after the Commission has made a final determination in this proceeding.[13]

21. At the end of the January 26, 2012 hearing, the parties discussed whether additional information concerning project costs and financing options would be necessary in order to determine whether refunding amounts already collected for the CAP project would be in the public interest. The parties agreed that after the parties had an opportunity to confer, a Procedural Conference to discuss the scope of Phase II would be beneficial.[14]

22. On February 3, 2012, a telephonic Procedural Conference convened.[15] The Company indicated that it wished to engage in discussions with Staff the following week, and proposed keeping the hearing date of February 29, 2012, but extending the date to file Rebuttal Testimony from February 13, 2012, until February 20, 2012, to give the parties time to confer. Staff did not object to the extension of time, but indicated that if the scope of Phase II was to discuss issues beyond compliance, Staff would not have time to file testimony about how to finance the CAP project in time for a February 29, 2012 hearing. By Procedural Order dated February 6, 2012, the deadline for filing Rebuttal Testimony was extended until February 22, 2012.

23. On February 17, 2012, VWC and Staff participated in another telephonic Procedural Conference during which they requested a continuance of the hearing date by approximately 30 days to give Staff time to evaluate a proposal made by the Company that could resolve some or all of the pending issues. By Procedural Order dated February 22, 2012, the February 29, 2012 hearing was continued until March 29, 2012, and the deadline to file rebuttal testimony was extended until March 22, 2012. The Procedural Order provided that because the matter had already been noticed to VWC customers, the February 29, 2012, date would be utilized for taking public comment.

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[11] Ex S-3, Bozzo Dir at 4.
[12] *Id.*
[13] Tr. at 93.
[14] Tr. at 89-90.
[15] Tr. at 93-94.

24. On February 29, 2012, a public comment session convened. Two VWC customers appeared to provide public comment. They expressed a concern that ratepayers have been paying for the CAP project without a complete project, and concerns about how CAP water will affect water quality. The Commission also received written comment from the Director of the University of Arizona Water Resources Research Center and member of the board of the Central Arizona Water Conservation District which operates the CAP, urging the Commission to grant the deadline extension so that VWC can use its CAP water in a manner that is consistent with the management goals of the Tucson AMA.

25. On February 29, 2012, VWC filed a request, with the concurrence of Staff, that the ALJ not issue a Recommended Opinion and Order ("ROO") for Phase I until the parties have been able to conclude their discussions.[16]

26. At the request of the parties, a telephonic procedural conference convened on March 20, 2012. The parties reported that they had reached a consensual resolution of the issues raised in this proceeding, and proposed that the March 29, 2012, hearing should focus of the proposed settlement.

27. The parties docketed the Settlement Agreement on March 22, 2012.

28. A hearing convened on March 29, 2012, before a duly authorized ALJ, to address the proposed Settlement. Mr. Volpe testified for the Company, and Mr. Bozzo testified for Staff.

Settlement Agreement

29. A copy of the proposed Settlement Agreement is attached hereto as Exhibit A, and is incorporated herein by reference. The proposed Settlement provides:

(a) Staff and VWC continue to support the direct use of CAP water in VWC's service area as contemplated in Decision No. 62450;

(b) VWC will not re-instate the $0.32 per 1,000 gallons CAP Surcharge unless and until such surcharge is re-authorized as part of a rate case.

(c) VWC will re-instate the CAP Hook-up Fee.

[16] VWC was responding to an inquiry during the February 17, 2012, Procedural Conference, whether given the parties' discussions, a ROO should be issued on the limited issues addressed in Phase I of the proceeding.

(d) On or before July 31, 2012, VWC will file a rate case using a test year of December 31, 2011 ("Rate Case"), and both parties agree that filing the Rate Case will satisfy the provision of Decision No. 62450 concerning the filing of a rate case.[17] As part of the Rate Case, VWC will propose a surcharge to address costs relating to the CAP Project in an attempt to avoid the need for filing another rate case immediately after the Rate Case. Staff expressed general support for the concept of a surcharge for amounts to be paid Tucson Water under a Wheeling Agreement, M&I and delivery charges, and for other CAP-related costs, however, the agreement provides that Staff's final recommendation on such a surcharge will be formed following examination of the surcharge application and other financial information presented in the Rate Case.

(e) The deadline for submitting Final Plans for the direct use of CAP water in VWC's service territory as set forth in Decision No. 62450 is extended to June 30, 2013.

(f) VWC may use the funds collected from the CAP Surcharge and Hook-up fees (as well as the Hook-up fees that continue to be collected) in the manner intended by Decision No. 62450, including, but not limited to: permit, design, engineer, and construct and/or to acquire plant and equipment necessary to have CAP water delivered to its water system and to pay for on-going CAP M&I and delivery charges, legal fees, and costs associated with recharging water. These CAP funds are not subject to refund solely as a result of the Company's failure to submit Final Plans by December 31, 2010, but Staff reserves the right to examine the need for the use of the funds as part of the Rate Case and to continue to examine the prudence of all expenditures made from these funds.

(g) Staff will not recommend that the Commission impose any penalty or fine solely as a result of VWC's failure to make the Final Plan submission by December 31, 2010, subject to VWC meeting the June 30, 2013, deadline.

30. VWC has accumulated approximately $4.5 million in its CAP account from 2000 until December 2011, and over the same period has expended approximately $2.7 million on expenses related to maintaining its rights to the CAP allocation.[18] As of December 31, 2011, VWC had

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[17] Decision No. 62450 orders VWC to file a rate case no earlier than twelve months or later than eighteen months after the completion of the plant to be installed pursuant to that Order. Decision No. 62450 at 20. The Order does not indicate which plant's completion would trigger the rate case.

[18] *See* Amended Report of CAP Hookup Fees and CAP Service Fees Collected, filed on February 24, 2012.

approximately $1.9 million in its CAP account.[19]

31. Through December 31, 2011, approximately 75 percent of the funds added to the CAP account were provided by developers in the form of Hook-up Fees, and 25 percent was provided by ratepayers via the $0.32 per 1,000 gallons surcharge.[20]

32. Both parties continue to support the direct use of CAP water in VWC's service area, and believe that the Settlement Agreement resolves the issues raised in this docket in a fair and reasonable manner, and that its approval will advance the Commission's directive to devise a plan to move forward to achieve the direct use of CAP water in VWC's service area.[21]

33. We agree that the Settlement Agreement is a fair and reasonable resolution of all of the issues raised in this proceeding. There is no dispute that the direct use of VWC's CAP allocation in its service area will benefit the Company, the ratepayers and the Tucson AMA. The collection of the Hook-up Fees and the CAP Surcharge functioned as conceived, and the fund will allow VWC to proceed quickly to bring CAP water to its area as soon as it can finalize an agreement with Tucson Water. The Company was dependent on the City of Tucson's schedule for negotiating the CAP wheeling agreement, and it appears that the City is now ready to proceed. In addition to allowing the CAP project to proceed, the Settlement Agreement requires a rate case which will allow the Commission to consider the best way to finance the CAP project going-forward, as well as re-examine rates in light of the significant growth in the Vail area since 2000.[22]

34. The Company admits that it should have sought Commission amendment of Decision No. 62450 prior to the December 31, 2010, deadline. Mr. Volpe testified that he didn't file a request for an extension of time to file the Final Plans by December 31, 2010, because at that time, the City of Tucson was not offering a solution, and he did not know what the Final Plan would look like, or how long it would take to be able to file it.[23]

35. Although the Company should have sought an extension to file the Final Plans prior to

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[19] *Id.*
[20] Id.; *also* Tr. at 129
[21] Tr. at 105-06, 109.
[22] At the time of the last rate case, VWC had 770 customers. Decision No. 62450 at 2. Currently, VWC has approximately 3900 customers. Tr. at 35.
[23] Tr. at 18.

the deadline, and without requiring Staff to expend the time and energy that was required in this matter, the Company's failure does not appear motivated by a disregard of its obligations under Commission Orders, but rather a lack of understanding of how to modify the deadline, and a strong belief that all parties supported the CAP project as being in the public interest.[24] The Company's lack of understanding or its technical failure to file the Final Plans should not penalize ratepayers. Thus, we agree the negotiated solution that would termination the CAP Surcharge pending a rate case and not require refund at this time is in the public interest.

36. Staff feels that the Company now understands its obligations and has demonstrated progress toward the ultimate goal, and does not recommend administrative penalties at this time.[25] There is no indication the CAP funds were misused or that ratepayers suffered any harm from the failure to file the Final Plans. The Company could not comply until the City of Tucson was ready to enter into the wheeling agreement. Consequently, we adopt Staff's recommendation not to impose administrative penalties at this time.[26]

CONCLUSIONS OF LAW

1. VWC is a public service corporation within the meaning of Article XV of the Arizona Constitution and A.R.S. §§40-202, 40-203, 40-251, 40-301 and 40-302.

2. The Commission has jurisdiction over VWC and the subject matter of this proceeding.

3. Notice was provided as required by law.

4. The Settlement Agreement attached as Exhibit A resolves the issues raised in this docket in a fair and reasonable manner, and its adoption is in the public interest.

ORDER

IT IS THEREFORE ORDERED that the Settlement Agreement entered into between Vail Water Company and the Commission's Utility Division Staff, attached hereto as Exhibit A, is hereby approved.

IT IS FURTHER ORDERED that Vail Water Company may utilize the funds in its CAP

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[24] Tr. at 130-31.
[25] Tr. at 150.
[26] The Company has incurred costs associated with resolving this dispute. Ratepayers should not be held responsible for the costs of this proceeding or any late fees that may be owed the CAP.

account for the purposes identified in the Settlement Agreement.

IT IS FURTHER ORDERED that any late fees associated with a delay in making 2012 CAP payments shall not be made using funds in the CAP account, and ratepayers shall not be held responsible for any such late fees.

IT IS FURTHER ORDERED that the deadline established in Decision No. 62450 for Vail Water Company to file Final Plans for the direct use of CAP water in its service area is hereby extended until June 30, 2013.

IT IS FURTHER ORDERED that Vail Water Company shall file a rate case no later than July 31, 2012, using a test year of December 31, 2011, and that such filing will be deemed to have satisfied the requirements of Decision No. 62450 to file a rate case.

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IT IS FURTHER ORDERED that Vail Water Company is authorized to collect the CAP Hook-up Fees authorized in Decision No. 62450, but that the CAP Surcharge is terminated, both effective immediately.

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 _____day of _____ 2012.

_____
ERNEST G. JOHNSON
EXCUTIVE DIRECTOR

DISSENT _____

DISSENT _____

SERVICE LIST FOR: VAIL WATER COMPANY

DOCKET NOS.: W-01651B-99-0351 and W-01651B-99-0406

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RECEIVED
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LEGAL DIV.
ARIZ. CORPORATION COMMISSION

SETTLEMENT AGREEMENT

The purpose of this Settlement Agreement ("Agreement") is to settle issues related to Arizona Corporation Commission Docket Nos. W-01651B-99-0351 and W-01651B-99-0406, as reopened by the Arizona Corporation Commission ("Commission") on December 1, 2011. This Agreement is entered into by Vail Water Company ("Vail") and the Arizona Corporation Commission Utilities Division ("Staff"). Vail and Staff may be referred to as a "Party" and collectively, as the "Parties."

Terms And Conditions

In consideration of the promises and agreements contained herein, the Parties agree that the following numbered sections and subsections comprise the Parties' Agreement.

1. Recitals

1.1 On December 1, 2011, the Commission voted to reopen this docket and Decision No. 62450 in order to defer the matter to the Hearing Division to take testimony to consider the Company's request for an extension of time to file its final plans for direct use of CAP water; to determine a plan to accomplish the direct use of CAP water in Vail's service area; to determine whether there should be any refund of CAP surcharges; and to determine whether to impose any penalties for violation of Decision No. 62450 for failure to file final plans by December 31, 2010.

1.2 By Procedural Order dated December 19, 2011, the Administrative Law Judge scheduled two hearing dates to address the different issues for which this docket and Decision No. 62450 was reopened.

1.3 On January 26, 2012, a hearing was held to address whether Vail should be authorized to use the surcharge funds currently held in trust to make upcoming CAP payments.

1.4 Following the January 26, 2012 hearing, Vail and Staff determined that discussions to discuss a resolution of the issues in this docket would be beneficial.

1.5 On February 8, 2012, the parties met in good faith at the Commission's offices to further discuss this matter and to exchange information relating to Vail's plans for direct use of CAP water in its service area and other issues relating to this docket.

1.6 By Procedural Order dated February 23, 2012, the second hearing date was rescheduled to March 29, 2012, to allow the parties additional time to discuss a possible resolution of this matter.

1.7 Following further telephonic discussions regarding this matter, the Parties again met in good faith on March 6, 2012, to continue to discuss a resolution of the issues for which this docket was reopened.

A-5
ADMITTED

1.8 The Parties agree and represent their belief that the terms and conditions of this Agreement will serve the public interest by providing a just and reasonable resolution of the issues presented by this case.

2. Terms of Settlement

2.1 Staff and Vail continue to support direct use of CAP water in Vail's service area as contemplated by Decision No. 62450.

2.2 Vail will not re-instate the currently authorized $0.32 per thousand gallons CAP surcharge (unless such surcharge is reinstated as part of the Rate Case addressed in Section 2.4 below).

2.3 Vail will re-instate the currently authorized CAP hook-up fee. upon decision

2.4 On or before July 31, 2012, Vail will file a rate case using a test year for the 12 months ending December 31, 2011 (the "Rate Case"). This filing will comply with the rate case filing provision of Decision No. 62450. As part of the Rate Case, Vail will propose a surcharge to address costs relating to the CAP project in an effort to avoid the need for the filing of another rate case immediately after the conclusion of the Rate Case. Staff generally supports the concept of such a surcharge for amounts to be paid Tucson Water under a Wheeling Agreement, M&I and delivery charges, as well as other CAP-related cost components; however, Staff's final recommendation on such a surcharge is subject to Staff's examination of the actual surcharge application filed by Vail and Vail's financial information as part of the Rate Case.

2.5 The deadline for submission of final plans for the direct use of CAP water in Vail's service territory set forth in Decision No. 62450 will be extended to June 30, 2013.

2.6 Vail may use the surcharge and hook up fee funds currently held by Vail (and those future hook up fees to be collected as stated in Section 2.3) in the manner intended by Decision No. 62450, including, but not limited to: to permit, design, engineer, and construct and/or to acquire plant and equipment necessary to have CAP water delivered to its water system and to pay for on-going annual CAP M&I and delivery charges, legal fees, and costs associated with recharging water. These funds will not be subject to refund solely as a result of the Company's failure to file final plans by December 31, 2010; however, Staff reserves the right to examine the need for the use of these funds as part of the Rate Case and to continue to examine the prudence of all expenditures made from these funds.

2.7 Staff will not recommend that the Commission impose any penalty or fine solely as a result of Vail's failure to make the final plan submission by December 31, 2010, subject to Vail meeting the June 30, 2013 deadline as indicated above.

3. Commission Approval

3.1 The Parties acknowledge and agree that the terms of this Agreement require Commission approval, and that the Commission will independently consider and evaluate the

terms of this Agreement. With respect to approval of this Agreement, the Parties agree as follows:

(a) To support and defend the Agreement by providing testimony as required by the Administrative Law Judge, appearing at any and all hearings, open meetings or other proceedings in the docket related to the Agreement, and taking any and all other steps reasonably necessary to obtain Commission adoption of the material terms of the Agreement.

(b) That a final, non-appealable Commission order adopting the material terms of this Agreement shall constitute Commission approval of the Agreement for purposes of the Agreement.

3.2 The Parties further agree that in the event the Commission fails to issue an order adopting all material terms of this Agreement or modifies or adds material terms to this Agreement, any or all of the Parties may withdraw from this Agreement, and such Party or Parties may pursue their respective remedies at law without prejudice. For the purposes of this Agreement, whether a term is material shall be left to the reasonable discretion of the Party choosing to withdraw from the Agreement.

4. Miscellaneous Provisions

4.1 With respect to the Parties' Agreement as set forth herein, the Parties further agree to the following general terms and conditions of their agreement:

(a) Each person whose signature appears below is fully authorized and empowered to execute this Agreement.

(b) Each Party is represented by competent legal counsel and that they understand all of the terms of this Agreement, that it has had an opportunity to participate in the drafting of this Agreement and fully review this Agreement with its counsel before signing, and that it executes this Agreement with full knowledge of the terms of the Agreement.

(c) Nothing in this Agreement shall be construed as an admission by any of the Parties that any of the positions taken by any Party in this proceeding is unreasonable or unlawful. In addition, acceptance of this Agreement by any of the Parties is without prejudice to any position taken by any party in these proceedings.

(d) This Agreement represents the Parties' mutual desire to compromise and settle in good faith certain issues in a manner consistent with the public interest. The terms and provisions of this Agreement apply solely to and are binding only in the context of the circumstances and those purposes. None of the positions taken in this Agreement by the Parties may be referred to, cited, or relied upon as precedent in any proceeding before the Commission, any other regulatory agency, or any court for any purpose except in furtherance of this Agreement.

(e) All negotiations relating to this Agreement are privileged and confidential. No Party is bound by any position asserted in negotiations, except as expressly stated in this Agreement. The Parties expressly agree that evidence of conduct or statements made in the course of negotiating this Agreement shall not be offered and are not admissible before this Commission, any other regulatory agency, or any court.

(f) Each of the terms and conditions of the Agreement is in consideration and support of all other terms. Accordingly, the terms are not severable except upon express consent of the Parties.

(g) This Agreement may be executed in counterparts. This Agreement also may be executed electronically or by facsimile.

Executed this 23rd day of March, 2012.

VAIL WATER COMPANY

By: _____

Its: President

ARIZONA CORPORATION COMMISSION
UTILITIES DIVISION STAFF

By: _____

Its: Utilities Division Director