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BEFORE THE ARIZONA CORPORATION C
Arizona Corporation Commission

COMMISSIONERS

DOCKETED

JUN - 5 2012

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

DOCKETED BY *JM*

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS ANTHEM WATER DISTRICT AND ITS SUN CITY WATER DISTRICT.

DOCKET NO. W-01303A-09-0343

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS ANTHEM/AGUA FRIA WASTEWATER DISTRICT, ITS SUN CITY WASTEWATER DISTRICT, AND ITS SUN CITY WEST WASTEWATER DISTRICT.

DOCKET NO. SW-01303A-09-0343

DECISION NO. 73227

OPINION AND ORDER

DATES OF HEARING: April 19, 2011 (Procedural Conference); October 17, 2011 (Public Comment); November 7, 2011 (Pre-Hearing Conference); November 14, 15, 16, 17, 2011.

PLACE OF HEARING: Phoenix, Arizona

ADMINISTRATIVE LAW JUDGE: Teena Jibilian

IN ATTENDANCE: Gary Pierce, Chairman
Bob Stump, Commissioner
Sandra D. Kennedy, Commissioner
Brenda Burns, Commissioner

APPEARANCES: Mr. Craig A. Marks, CRAIG A. MARKS, PLC, on behalf of Applicant;

Mr. Lawrence V. Robertson, Jr., MUNGER CHADWICK, and Ms. Judith M. Dworkin and Ms. Roxanne S. Gallagher, SACKS TIERNEY, PA, on behalf of Anthem Community Council;

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Mr. Bradley J. Herrema, BROWNSTEIN HYATT FARBER SCHRECK, LLP, on behalf of Anthem Golf and Country Club;

Ms. Michele L. Van Quathem, RYLEY CARLOCK & APPLEWHITE, PC, on behalf of Verrado Community Association, Inc. and DMB White Tank, LLC;

Mr. Jason D. Gellman, ROSHKA DEWULF & PATTEN, PLC, and Mr. Troy B. Stratman, MACK DRUCKER & WATSON, PLC, on behalf of Corte Bella Country Club Association, Inc.;

Mr. George Turner, President, Board of Directors, on behalf of Russell Ranch Homeowners Association, Inc.;

Ms. Cynthia S. Campbell, OFFICE OF THE CITY ATTORNEY, on behalf of the City of Phoenix;

Mr. Daniel W. Pozefsky, Chief Counsel, and Ms. Michelle L. Wood, Staff Attorney, on behalf of the Residential Utility Consumer Office;

Ms. Maureen A. Scott, Senior Staff Counsel, Ms. Robin Mitchell and Mr. Scott Hesla, Staff Attorneys, Legal Division, on behalf of the Utilities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

INTRODUCTION

A. Procedural History

1. Decision No. 72047

On July 2, 2009, Arizona-American Water Company¹ (“Company”) filed with the Arizona Corporation Commission (“Commission”) an application for rate increases for its Anthem Water District, Sun City Water District, Anthem-Agua Fria Wastewater District, Sun City Wastewater District, and Sun City West Wastewater District.²

Intervention in this matter was granted to the Residential Utility Consumer Office (“RUCO”); Anthem Community Council (“Anthem”); Sun City West Property Owners and Residents Association (“PORA”); W.R. Hansen; the Water Utility Association of Arizona (“WUAA”); the

¹ On February 1, 2012, Arizona-American Water Company was acquired by EPCOR Water (USA). The acquisition was approved by Commission Decision No. 72668 (November 17, 2011). Both Arizona-American Water Company and EPCOR Water (USA) will be referred to herein as “Company.”

² In addition to the districts affected by Decision No. 72047, the Company operates eight additional water and wastewater districts located in the State of Arizona.

1 Camelback Inn, Sanctuary on Camelback Mountain, the Intercontinental Montelucia Resort and Spa,
 2 and the Scottsdale Cottonwoods Resort and Suites (collectively the "Resorts"); the Town of Paradise
 3 Valley; the Anthem Golf and Country Club; Marshall Magruder; DMB White Tank, LLC ("DMB");
 4 Mashie, LLC dba Corte Bella Golf Club; Larry D. Woods; and Philip H. Cook.

5 On January 6, 2011, the Commission issued Decision No. 72047 in these dockets. An issue
 6 considered in the rate case proceeding was whether to deconsolidate the Anthem-Agua Fria
 7 Wastewater district into two new separate districts: an Anthem Wastewater district, and an Agua Fria
 8 Wastewater district. Decision No. 72047 left this docket open for the sole purpose of considering the
 9 design and implementation of stand-alone revenue requirements and rate designs for separate Anthem
 10 Wastewater and Agua Fria Wastewater districts as agreed to in the settlement reached by the
 11 Company, Anthem, RUCO and the Commission's Utilities Division ("Staff") during the Open
 12 Meeting at which Decision No. 72047 was considered.

13 Decision No. 72047 states as follows:

14 Good public policy requires the Commission to correctly assign cost responsibility
 15 for all ratemaking components in as expeditious a manner as possible, and
 16 deconsolidation of Anthem/Agua Fria Wastewater District is consistent with such
 17 action. However, the record does not include adequate rate base or operating income
 18 information to immediately implement stand-alone rate designs for the resulting
 19 Anthem Wastewater district and Agua Fria Wastewater district at this time.
 20 Therefore, we will (i) approve the rates adopted herein for Anthem/Agua Fria
 21 Wastewater district as a consolidated district on an interim basis, and (ii) order the
 22 docket in the instant proceeding to remain open for the sole purpose of considering
 23 the design and implementation of stand-alone revenue requirements and rate designs
 24 as agreed to in the settlement reached during the Open Meeting for the Anthem
 25 Wastewater district and Agua Fria Wastewater district as soon as possible. The
 26 Company shall file its initial application no later than April 1, 2011.

27 Decision No. 72047 approved an overall rate increase of 53.98 percent for all residential
 28 customers in the Company's Anthem-Agua Fria Wastewater district, and made those rates interim,
 subject to change pursuant to a Commission determination on the Company's April 1, 2011 filing.³

³ Decision No. 72047 ordered as follows:

IT IS FURTHER ORDERED that the docket in this proceeding shall remain open for the sole
 purpose of considering the design and implementation of stand-alone revenue requirements and rate
 designs as agreed to in the settlement reached during the Open Meeting for the Anthem Wastewater
 district and Agua Fria Wastewater district.

IT IS FURTHER ORDERED that Arizona-American Water Company shall file, no later than
 April 1, 2011, an application supporting consideration of stand-alone revenue requirements and rate
 designs as set forth in the Agreement reached during the Open Meeting for the Anthem Wastewater
 district and Agua Fria Wastewater district.

1 2. Compliance Application

2 On April 1, 2011, the Company complied with Decision No. 72047 by filing its Compliance
3 Application to Support Consideration of Stand-Alone Revenue Requirements and Rate Designs for
4 the Anthem-Agua Fria Wastewater District (“Compliance Application”). The filing included direct
5 testimony and exhibits concerning separate revenue requirements and separate rate designs for two
6 new Anthem Wastewater and Agua Fria Wastewater districts on a stand-alone basis, using the
7 combined revenue authorizations in Decision No. 72047.

8 On April 27, 2011, following a procedural conference at which parties discussed public notice
9 issues and the timing of discovery and pre-filing testimony, a Procedural Order was issued setting a
10 hearing schedule and associated compliance deadlines, including public notice, for a hearing on the
11 Compliance Application.

12 3. Notice of the Compliance Application and New Interventions

13 The Company provided a copy of the required notice of the Compliance Application and
14 hearing by First-Class U.S. Mail to each of its customers in the Anthem-Agua Fria Wastewater
15 district, and to each of the homeowners’ associations located in the Anthem-Agua Fria Wastewater
16 district. Following the notice, the Commission granted new intervention in this proceeding on the
17 Compliance Application to: Verrado Community Association, Inc. (“Verrado”), Corte Bella Country
18 Club Association, Inc. (“Corte Bella”), the Russell Ranch Homeowners’ Association, Inc. (“Russell
19 Ranch”), Frederick G. Botha, and the City of Phoenix (“Phoenix”).

20 4. Public Comment and Hearing

21 A public comment hearing on the Compliance Application was held at the Commission’s
22 offices on October 17, 2011. Members of the public appeared and provided comments. Comments
23 were received both in favor of, and in opposition to, deconsolidation of the Anthem-Agua Fria
24 Wastewater districts.

25 The parties prefiled the testimony of their witnesses, and an evidentiary hearing on the
26

27 IT IS FURTHER ORDERED that the rates approved herein for the Anthem/Agua Fria
28 Wastewater district are interim rates subject to change pursuant to a Commission determination on the
 above-ordered filing.
 Decision No. 72047 at 121.

1 Compliance Application was held before a duly authorized Administrative Law Judge of the
2 Commission commencing on November 14, 2011, and concluding on November 17, 2011.
3 Appearances were entered through counsel for the Company, Anthem, Corte Bella, Verrado, DMB,
4 Phoenix, RUCO and Staff. Russell Ranch appeared through its representative Mr. George Turner.
5 The parties presented evidence through witnesses and were provided an opportunity to cross-examine
6 witnesses.

7 Following the filing of Initial Post-Hearing Briefs and Post-Hearing Reply Briefs, the matter
8 was taken under advisement pending the submission of a Recommended Opinion and Order for the
9 Commission's consideration.

10 **B. Areas Affected by this Proceeding**

11 The evidence in this proceeding brought to light the fact that the territory of the Anthem-Agua
12 Fria Wastewater district is actually comprised of not simply two non-contiguous service areas served
13 by two separate wastewater systems, an "Anthem Wastewater service area" and an "Agua Fria
14 Wastewater service area," but instead of four non-contiguous service areas served by separate
15 wastewater systems.⁴ The four non-contiguous service areas of the Anthem-Agua Fria Wastewater
16 district include a service area in which intervenors Anthem and Anthem Golf and Country Club are
17 located (adjacent to northern Phoenix); a service area in which intervenors Verrado and DMB are
18 located (to the southwest of Phoenix, in Buckeye); a service area in which intervenor Russell Ranch
19 is located (near the City of Litchfield Park); and the Northeast Agua Fria service area that includes
20 intervenor Corte Bella (west of Anthem, near the City of Surprise).⁵ Testimony in this proceeding
21 indicates that wastewater from the Northeast Agua Fria area, including Coldwater Ranch, Cross
22 River, and Corte Bella, is treated by the Northwest Valley Regional Water Reclamation Facility
23 ("Northwest Valley Plant"), that also treats wastewater from the Company's Sun City West
24 Wastewater district, which district is not involved in this case.⁶

25 ⁴ Hearing Exhibit A-1, Direct Testimony of Company witness Sandra L. Murrey, at 5; Hearing Transcript ("Tr.") at 108-
26 109; Hearing Exhibit S-3.

26 ⁵ See, e.g. Tr. at 108-109; Hearing Exhibit S-3.

27 ⁶ Tr. at 108. See also Decision No. 72047, which states:

28 The Northwest Valley Regional Water Reclamation Facility ("Northwest Valley") treats wastewater
flows from both the Anthem/Agua Fria Wastewater district and the Sun City West wastewater district.
In Decision No. 70209 (March 20, 2008), the Company was ordered to allocate 68 percent of the

1 Testimony of a Company witness described how the Verrado, Russell Ranch, and Northeast
 2 Agua Fria service areas became part of the current Anthem-Agua Fria Wastewater district.⁷ The
 3 witness testified that the district was first formed in 1998, when the Certificate of Convenience and
 4 Necessity (“CC&N”) was granted to a subsidiary of Citizens Utilities Company, Citizens Water
 5 Services Company of Arizona (“Citizens Water Services”) pursuant to Commission Decision No.
 6 60975 (June 19, 1998). Initial rates were set at that time based on projections. Decision No. 64307
 7 (December 28, 2001) approved extension of the Citizens Water Services wastewater CC&N to
 8 include the Verrado service area, and authorized Citizens Water Services to charge the same rates
 9 charged for Anthem wastewater service, with the addition of a new hook-up fee that would be
 10 applicable only to Verrado customers. Arizona-American Water Company acquired Citizens Utilities
 11 Company on January 15, 2002. Decision No. 64746 (April 17, 2002) approved the application,
 12 which had been filed by Citizens Water Services, for extension of the CC&N to include the Russell
 13 Ranch Service area, with the Company name change to Arizona-American Water Company. On
 14 August 20, 2002, Arizona-American Water Company filed an application requesting the extension of
 15 the CC&N to include the Northeast Agua Fria service area. In that application, the entire district was
 16 referred to for the first time as the Anthem-Agua Fria Wastewater district. That application was
 17 approved in Decision No. 65757 (March 20, 2003).

18 At the hearing, Staff provided a Hearing Exhibit consisting of two maps depicting the location
 19 of the Anthem-Agua Fria Wastewater district and the Agua Fria Water district, in relation to the
 20 Company’s Sun City Water and Wastewater districts, its Sun City West Water and Wastewater
 21 districts, and the Anthem Water district.⁸ For ease of reference, a copy of that Hearing Exhibit is
 22 reproduced as Exhibit A, attached hereto and incorporated herein by reference.

23 No evidence was presented in this case on the rate effects of deconsolidating all four of the

24 Northwest Valley plant costs to the Sun City West Wastewater district. Decision No. 70372 (June 13,
 25 2008) ordered the allocation of 32 percent of the Northwest Valley plant costs to the Anthem/Agua Fria
 26 Wastewater district.

27 Decision No. 72047 at 18.

28 Decision No. 72047 adopted Staff’s recommendation, supported by the Company and RUCO, but with which Anthem
 disagreed, to change the allocation of the Northwest Valley Plant to the Anthem-Agua Fria Wastewater district from 32
 percent to 28 percent. Decision No. 72047 at 19-20.

⁷ Hearing Exhibit A-1at 3-6.

⁸ Hearing Exhibit S-3.

1 existing service areas in the Anthem-Agua Fria Wastewater district.⁹

2 **C. Effect of Deconsolidation**

3 According to the Company and Staff's calculations, not disputed by any party,
 4 deconsolidation of the Anthem-Agua Fria Wastewater district into two separate districts would result
 5 in an average Anthem-Agua Fria Wastewater district residential customer located in the Anthem
 6 service area experiencing a decrease of 24.80 percent from the rates implemented on January 1, 2011
 7 pursuant to Decision No. 72047,¹⁰ and an average Anthem-Agua Fria Wastewater district residential
 8 customer located in the three remaining service areas experiencing an increase of 62.98 percent over
 9 the January 1, 2011, implemented rates.¹¹ As compared with test year rates, deconsolidation of the
 10 Anthem-Agua Fria Wastewater district would result in an average Anthem-Agua Fria Wastewater
 11 district residential customer located in the area serving Anthem experiencing an increase of 7.92
 12 percent over test year rates,¹² and an average Anthem-Agua Fria Wastewater district residential
 13 customer located in the three areas that serve Corte Bella, Russell Ranch, Verrado and DMB
 14 experiencing an increase of 133.90 percent over test year rates.¹³

15 Anthem is proposing that the Commission phase in the transition of deconsolidated revenues
 16 in annual steps over three years, with no overall change to revenue levels to the Company, with the
 17 Step 3 rates equal to those arrived at by Staff and the Company.¹⁴

18 **D. Summary of Positions of the Participating Parties**

19 1. Company

20 The Company takes no position concerning whether the Commission should deconsolidate the
 21 Anthem-Agua Fria Wastewater district.¹⁵ The Compliance Application included schedules for
 22 separate districts in the event of deconsolidation. In the event of deconsolidation of the Anthem-

23
 24 ⁹ See Tr. at 542-43, 605-606. Decision No. 72047 did not order the Company to file deconsolidation information for all four systems, and no party requested that the Company provide such information.

25 ¹⁰ Hearing Exhibit A-2, Schedule GWB-6; Hearing Exhibit S-1, Direct Testimony of Staff witness Gerald W. Becker, at 6-7.

26 ¹¹ Hearing Exhibit A-2, Schedule GWB-8; Hearing Exhibit S-1 at 7.

27 ¹² Hearing Exhibit A-2, Schedule GWB-2; Hearing Exhibit S-1 at 6.

28 ¹³ Hearing Exhibit A-2, Schedule GWB-4; Hearing Exhibit S-1 at 7.

¹⁴ See Hearing Exhibit Anthem-21 (Proposed Wastewater Rates).

¹⁵ Company Initial Post-Hearing Brief ("Co. Br.") at 3; Company Post-Hearing Reply Closing Brief ("Co. Reply Br.") at 4.

1 Agua Fria Wastewater district, however, the Company ultimately adopted the deconsolidated rate
2 design schedules prepared by Staff.¹⁶

3 In its Compliance Application, the Company requested that the Commission reconsider
4 whether, in the event of deconsolidation, the winter-average rate design adopted in Decision No.
5 72047 is appropriate, or whether the additional rate design change would overly confuse customers.¹⁷
6 In its Initial Post-Hearing Brief, however, the Company stated that because the winter season had
7 already begun, and residential customers had already been notified of the coming rate design change
8 to become effective June 2012, it was no longer requesting that implementation of the winter-average
9 rate design be postponed.¹⁸

10 The Company is opposed to expanding the scope of this proceeding to address the issues
11 raised by Phoenix and Russell Ranch, and requests that this docket be permanently closed following a
12 Commission determination regarding whether to deconsolidate the Anthem-Agua Fria Wastewater
13 district.¹⁹

14 2. Anthem

15 Anthem has intervened in this case on behalf of over 8,800 customers of the Company.²⁰
16 Anthem is in favor of immediate deconsolidation of the Anthem-Agua Fria Wastewater district, and
17 argues that the purpose of this proceeding is to determine how, and not whether, to deconsolidate the
18 district.²¹ Anthem asserts that the current consolidation is contrary to good public policy and unfair
19 to Anthem customers.²² Anthem proposes a three-step revenue and rate transition plan to be
20 implemented over a period of three years as presented in the testimony of Anthem's witness.²³ Under
21 the Anthem proposal, annual adjustments of approximately \$800,000 would be made progressively
22 increasing the rates of Anthem-Agua Fria Wastewater district customers not in the Anthem service
23 area while reducing the rates of Anthem-Agua Fria Wastewater district customers in the Anthem
24

25 ¹⁶ Co. Br. at 2, citing to Tr. at 48-50 and Hearing Exhibit A-2.

¹⁷ Co. Br. at 3, citing to Hearing Exhibit A-1 at 12.

¹⁸ Co. Br. at 3.

¹⁹ Co. Reply Br. at 4.

²⁰ Hearing Exhibit Anthem-1, Direct Testimony of Anthem witness Dan L. Neidlinger, at 2.

²¹ Anthem Initial Post-Hearing Brief ("Anthem Br.") at 1-6; Anthem Reply Br. at 1-2, 4-8.

²² Anthem Br. at 10.

²³ *Id.* at 9, citing to Hearing Exhibit Anthem-1, Direct Testimony of Dan L. Neidlinger, at 5.

1 service area.²⁴ Anthem contends that there is no substantial reason for the continued consolidation of
 2 “these two geographically remote and physically unconnected wastewater districts,”²⁵ and urges
 3 rejection of the Agua Fria intervenors’ legal arguments and conclusions and immediate
 4 deconsolidation of the Anthem-Agua Fria Wastewater district.²⁶

5 3. Anthem Golf and Country Club

6 The Anthem Golf and Country Club takes no position on deconsolidation, deferring to the
 7 Commission’s discretion as to whether deconsolidation of the Anthem-Agua Fria Wastewater district
 8 should be ordered in this case.²⁷ The Anthem Golf and Country Club supports the positions of DMB
 9 and Staff that the effluent rate set in Decision No. 72047 should remain unchanged whether or not the
 10 Commission orders deconsolidation and the adoption of stand-alone rates.²⁸

11 4. Verrado

12 Verrado is a non-profit corporation that serves approximately 5,892 residents located in the
 13 new community of Verrado located near the White Tank Mountains in Buckeye, Arizona.²⁹ Verrado
 14 asks that the Commission take no action at this time to deconsolidate the Anthem-Agua Fria
 15 Wastewater district.³⁰ Verrado disagrees with Anthem that the Commission agreed to deconsolidate
 16 the district in Decision No. 72047.³¹ Verrado states that due to the change made at the prior Open
 17 Meeting in this case, Agua Fria area customers are now faced with a potential 133.90 increase in
 18 wastewater rates rather than the potential 81.8 percent increase originally noticed before rates were
 19 determined in Decision No. 72047.³²

20 Verrado agrees with Staff that the Commission may consider factors in addition to cost of
 21 service in determining if the charges in the deconsolidated rate design scenario are just and
 22 reasonable.³³ Verrado argues that from the customers’ perspective, apart from the quantity of

23 ²⁴ Anthem Br. at 9.

24 ²⁵ *Id.* at 20.

25 ²⁶ Anthem Reply Br. at 4.

26 ²⁷ Hearing Exhibit Anthem CC-1, Direct Testimony of Anthem Golf and Country Club witness Desi Howe at 4.

27 ²⁸ *Id.*

28 ²⁹ Hearing Exhibit V-1, Direct Testimony of Verrado witness Melinda Gulick, President of Verrado Community Association, Inc., at 4.

³⁰ Verrado Initial Post-Hearing Brief (“Verrado Br.”) at 1-3.

³¹ Verrado Post-Hearing Reply Brief (“Verrado Reply Br.”) at 4.

³² Verrado Br. at 2.

³³ *Id.* at 3 citing to Tr. at 42, 277-278.

1 wastewater a customer generates, each customer in the district is receiving identical service from the
 2 Company, and is now paying the same, approximately \$67 per month, but that if deconsolidation is
 3 granted, even with the phase-in proposal, at the end of three years, Anthem customers would pay only
 4 about \$52 per month, with Agua Fria customers paying about \$108 per month, for the same service.³⁴
 5 Verrado contends that because deconsolidation would result in customers paying substantially
 6 different rates for the same service from the same utility in the same urban area, the deconsolidation
 7 should be rejected.³⁵ Verrado urges that if the Commission is inclined to deconsolidate, it should do
 8 so only in a future rate case where Agua Fria residents have sufficient notice of the impact to their
 9 rates prior to the determination of the Company's revenue requirement, and have the opportunity to
 10 present evidence regarding whether the three Agua Fria systems should also be deconsolidated, or
 11 perhaps joined with other Company systems such as Sun City West.³⁶

12 Verrado contends that the rate shock to the customers that would be created by
 13 deconsolidation would not be adequately mitigated by Anthem's proposed revenue transition phase-
 14 in, which would continually and substantially increase rates over a three-year period.³⁷ Verrado
 15 contends that now that the Commission has evidence regarding the rate changes that would result
 16 from the proposed deconsolidation, it is clear that the proposed rates, even with Anthem's revenue
 17 transition phase-in proposal, are not just and reasonable for Agua Fria customers.³⁸

18 5. DMB

19 DMB asks that the Commission reject deconsolidation of the Anthem-Agua Fria Wastewater
 20 district, for the reasons cited by Verrado.³⁹ DMB also agrees with Staff that the Commission may
 21 consider factors in addition to cost of service in determining if the charges in the deconsolidated rate
 22 design scenario are just and reasonable.⁴⁰

23 DMB requests that in the event deconsolidation is ordered, the Commission make no changes
 24 to the effluent rate established in Decision No. 72047, for the reasons urged by DMB and other

25 ³⁴ Verrado Br. at 9, citing to Hearing Exhibit Anthem-21.

26 ³⁵ Verrado Br. at 9.

27 ³⁶ *Id.* at 3.

³⁷ *Id.* at 2.

³⁸ Verrado Reply Br. at 5.

³⁹ DMB Initial Post-Hearing Brief ("DMB Br.") at 1-2.

⁴⁰ *Id.* at 2, citing to Tr. at 42, 277-278.

1 parties in the earlier phase of this proceeding, and for the reasons cited in Decision No. 72047,
 2 including that the rate level of \$250 per acre-foot encourages the use of effluent for turf irrigation.⁴¹
 3 DMB points out that no party is proposing to change the established effluent rate.⁴²

4 6. Corte Bella

5 Corte Bella is an age-restricted community, developed by Pulte, that is completely built out
 6 and contains approximately 1,650 single family homes.⁴³ Corte Bella contends that Corte Bella
 7 residents, as well as other customers located in the three service areas of the Anthem-Agua Fria
 8 Wastewater district apart from Anthem, have been unfairly thrust into this proceeding because of the
 9 last-minute settlement agreement between Anthem, RUCO, Staff and the Company at the December
 10 2010 Open Meeting.⁴⁴ Corte Bella is opposed to deconsolidation of the Anthem-Agua Fria
 11 Wastewater district, asserting that deconsolidation is unjust, unreasonable, and unnecessary.⁴⁵ Corte
 12 Bella requests that the Commission maintain the rates implemented pursuant to Decision No.
 13 72047.⁴⁶ Corte Bella argues that the purpose of this proceeding on the Compliance Application was
 14 to consider, and not to “blindly” implement, the proposed deconsolidation of the Anthem-Agua Fria
 15 Wastewater district, and that based on the evidence now in the record, the Commission should deny
 16 the proposed deconsolidation.⁴⁷

17 7. Russell Ranch

18 Russell Ranch is a homeowners association serving a community that includes a total of 321
 19 custom lots, with 213 built lots and 108 vacant lots.⁴⁸ Russell Ranch opposes deconsolidation of the
 20 Anthem-Agua Fria Wastewater district, but if deconsolidation is approved, Russell Ranch would also
 21 like to become its own stand-alone system. Russell Ranch argues that it would be “unduly
 22 prejudiced and grossly neglected” if Anthem is allowed to have stand-alone rates without also
 23 allowing Russell Ranch to have stand-alone rates.⁴⁹ Russell Ranch argues that if the proposed

24 _____
 41 DMB Br. at 1-3, citing to Decision No. 72047 at 80-81.

25 42 DMB Br. at 3.

26 43 Hearing Exhibit CB-1, Direct Testimony of Corte Bella witness Robert Rials, at 8.

27 44 Corte Bella Post-Hearing Reply Brief (“Corte Bella Reply Br.”) at 2.

28 45 Corte Bella Initial Post-Hearing Brief (“Corte Bella Br.”) at 2, 17.

46 *Id.*

47 Corte Bella Reply Br. at 3, 4.

48 Russell Ranch Initial Post-Hearing Brief (“Russell Ranch Br.”) at 3.

49 *Id.*

1 deconsolidation is approved, which would remove Anthem customers from the Anthem-Agua Fria
 2 Wastewater district, the 213-customer Russell Ranch service area would be subsidizing the cost of
 3 service to the other Agua Fria service areas to a greater extent than it currently does.⁵⁰

4 Russell Ranch contends that an initial lack of understanding of the true geographical
 5 composition of the Anthem-Agua Fria Wastewater district, in conjunction with the fact that the
 6 Company uses only two business accounting units for the district to track costs, implied that
 7 deconsolidation would involve only two geologically separated service areas, in which one service
 8 area was subsidizing the costs of another.⁵¹ Russell Ranch states that this misconception, which was
 9 held by RUCO when its direct testimony was drafted,⁵² could not be further from the truth, as the
 10 district is clearly comprised of four geologically separated service areas.⁵³

11 Russell Ranch also raised an issue regarding the Company's tracking of hook-up fees
 12 collected from the three Agua Fria service areas pursuant to Decision No. 64746.⁵⁴ Russell Ranch
 13 did not request any relief in regard to this issue, but stated that the hook-up fee reporting
 14 requirements set in Decision No. 64746 justified establishing a separate business unit for the Russell
 15 Ranch service area.⁵⁵

16 8. Phoenix

17 Phoenix did not take a position on deconsolidation.⁵⁶ However, Phoenix requested that if the
 18 Anthem-Agua Fria Wastewater district remains intact, that the Commission re-examine the
 19 wastewater rate applicable to Phoenix.⁵⁷

20 9. RUCO

21 RUCO believes that deconsolidation is in the public interest subject to adoption of Anthem's
 22

23 ⁵⁰ Russell Ranch Br. at 5.

24 ⁵¹ *Id.* at 5-6, 8.

25 ⁵² *Id.* at 6, citing to Hearing Exhibit R-1, Direct Testimony of RUCO witness William A. Rigsby, at 5, and Tr. at 501-502.

26 ⁵³ Russell Ranch Br. at 5-6, 8.

27 ⁵⁴ *Id.* at 8. Testimony by a Company witness at the hearing established that there were no remaining hook-up fee funds to
 deposit in separate interest bearing accounts. Tr. at 220, 223-224.

28 ⁵⁵ Russell Ranch Br. at 9. The Company responded that there is no business reason or justification to expend funds to
 maintain a separate business unit to separately track expenses and revenues for such a small service area. Co. Reply Br. at
 4, citing to Tr. at 213.

⁵⁶ Phoenix Initial Post-Hearing Brief ("Phoenix Br.") at 2.

⁵⁷ *Id.* at 6; Phoenix Post-Hearing Reply Brief ("Phoenix Reply Br.") at 2.

1 phase-in proposal.⁵⁸ RUCO states that it can only support deconsolidation if an appropriate rate
2 mitigation proposal is approved.⁵⁹

3 10. Staff

4 Staff made no recommendation in this proceeding regarding deconsolidation or the Anthem
5 phase-in proposal.

6 Staff noted on brief that the parties favoring consolidation argued that rates should be set on
7 cost of service.⁶⁰ Staff also noted that witnesses for those parties acknowledged that the Commission
8 does not look solely at cost of service when setting rates,⁶¹ and that there are other factors that can be
9 considered when setting rates, such as affordability and gradualism.⁶² Staff further noted that the
10 Company's witness testified that the Commission does not look solely at cost of service when setting
11 rates,⁶³ and that the Commission has stated that cost of service studies are simply "tools" for
12 establishing revenue requirement per customer class.⁶⁴

13 With respect to the Company's filing, Staff agreed with the allocation of revenues in the
14 Company's deconsolidated schedules, but proposed a different rate design,⁶⁵ which the Company
15 accepted.⁶⁶ Staff requests that if the Commission elects to order deconsolidation, that it adopt Staff's
16 deconsolidation rate design, which includes no change to the effluent rate established in Decision No.
17 72047.⁶⁷

18 **DISCUSSION**

19 **A. Decision No. 72047 Agreement by the Company, Anthem, RUCO and Staff**

20 During the Open Meeting at which the Commission considered the rate application and

21 _____
22 ⁵⁸ RUCO Initial Post-Hearing Brief ("RUCO Br.") at 2.

23 ⁵⁹ *Id.* at 4.

24 ⁶⁰ Staff Initial Closing Brief ("Staff Br.") at 3.

25 ⁶¹ *Id.*, citing to Tr. at 340.

26 ⁶² Staff Br. at 3, citing to Tr. at 522-23.

27 ⁶³ Staff Br. at 3, citing to Tr. at 277.

28 ⁶⁴ Staff Br. at 3, citing to Decision No. 60172 (May 7, 1997) at 40, 43-44. Decision No. 60172 states:

In general, cost of service studies are tools that help determine cost causation by customer class, and what the appropriate revenue requirement for each customer class should be. Other considerations such as rate stability, fairness, conservation, etc. also are important when designing rates.

Decision No. 60172 at 40.

⁶⁵ Hearing Exhibit S-1, Direct Testimony of Staff Witness Gerald W. Becker at 7; Hearing Exhibit S-2, Surrebuttal Testimony of Staff Witness Gerald W. Becker, at Schedule GWB-6.

⁶⁶ Co. Br. at 2, citing to Tr. at 48-50 and Hearing Exhibit A-2.

⁶⁷ Staff Br. at 4.

1 adopted Decision No. 72047, the Company, Anthem, RUCO and Staff met during a recess from the
 2 Open Meeting to discuss possible resolution to a phase-in proposal for Anthem district rates and other
 3 issues, and reached an agreement.⁶⁸ The Commission found that the agreement was reasonable and
 4 appropriately balanced the interest of ratepayers and shareholders, and adopted it.

5 Anthem argues that deconsolidation was the quid pro quo for Anthem's acquiescence with
 6 respect to the ratemaking recognition of the disputed refund payments Arizona-American Water
 7 Company made to the developer Pulte.⁶⁹ Anthem asserts that the Commission envisioned
 8 deconsolidation as the ultimate regulatory result, and only intended the instant proceeding to be used
 9 to compile the necessary information to accomplish deconsolidation.⁷⁰ Anthem states that the

10 _____
 11 ⁶⁸ The agreement was set forth in Decision No. 72047 as follows:

Phase-in:

- 12 1) Three year phase-in of revenue requirement based on the 2007 and 2008 Pulte refund
 payments for both water and wastewater (as set forth in item 2).
- 13 2) As compared to the authorized revenues in the Recommended Opinion and Order, Anthem
 Water district revenues are reduced by a total of \$2.342 million as follows:
 - 14 a. In 2011 the revenue requirement is reduced \$1.561 million.
 - 15 b. In 2012 the revenue requirement is reduced \$0.781 million.
 - 16 c. In 2013 revenues equal the authorized revenues.
- 17 3) There is no recovery of the carrying costs associated with the reduced revenues.
- 18 4) There is no recovery of the foregone reduced revenues.
- 19 5) The 2007 and 2008 Pulte refunds are included in rate base in the overall authorized revenue
 requirement in the Recommended Opinion and Order.
- 20 6) The 2012 and 2013 revenue increases associated with the phase-in are implemented
 automatically effective January 1 of each year without further Commission action.

Other Matters

- 21 7) The overall revenue requirement is based on a 6.70 percent rate of return (as per Mayes
 Proposed Amendment #1)
- 22 8) Initiation of Anthem/Agua Fria Deconsolidation proceeding (as per Pierce Amendment # 1)
 - 23 a. Company to file initial application no later than April 11, 2011.
- 24 9) The Anthem/Agua Fria Wastewater district winter average residential sewer rate is not
 implemented until June 1, 2012. Prior to June 1, 2012, the Company's existing rate design for
 this tariff shall continue, but be increased based on the percentage increase in the authorized
 revenue requirement.
- 25 10) Add language to Exhibit A of Recommended Opinion and Order to reflect, "Each residential
 customer will be billed based on that customer's average water usage for the months of
 January, February, and March."
- 26 11) Support Hearing Division Amendment #2.
- 27 12) This will be full and complete resolution of the 2007 and 2008 Pulte refunds and there is no
 need for further Commission proceedings on this issue.
- 28 13) As contemplated in the Recommended Opinion and Order, the parties agree the new rates are
 effective January 1, 2011.
- 14) The Company will immediately file supporting schedules.

Decision No. 72047 at 44-45.

⁶⁹ Anthem Br. at 4.

⁷⁰ *Id.* at 6, citing Decision No. 72047 at 84.

1 Commission now has that information, and contends that it would be unfair to now deny
 2 consolidation and prevent Anthem from realizing its settlement objective, which was approved by the
 3 Commission.⁷¹

4 Verrado argues that contrary to Anthem's assertions, the Commission did not agree to
 5 deconsolidate the district in Decision No. 72047, but that the Commission did not have in front of it
 6 the information necessary to determine whether the resulting rates for the proposed deconsolidated
 7 systems would be just and reasonable.⁷² Corte Bella agrees with Verrado that the record does not
 8 support Anthem's interpretation of the language in Decision No. 72047,⁷³ asserting that the
 9 Commission did not "blindly" approve deconsolidation, and that the language in Decision No. 72047
 10 evidences that the Commission wished to consider the effects of consolidation.⁷⁴ Corte Bella states
 11 that even if Anthem's interpretation of Decision No. 72047 is correct, there are serious due process
 12 issues, because Corte Bella customers, as well as other Agua Fria customers, were not a party to the
 13 settlement agreement reached at the Open Meeting, and had no notice of the resulting rate increase
 14 until four months after Decision No. 72047 was docketed.⁷⁵ Corte Bella contends that based on the
 15 evidence now in the record, deconsolidation should not be approved.⁷⁶

16 Verrado asserts that now that evidence regarding the rate changes that would result from the
 17 proposed deconsolidation are before the Commission, it is clear that the proposed deconsolidated
 18 rates, even with Anthem's revenue transition phase-in proposal, are not just and reasonable for Agua
 19 Fria customers.⁷⁷ Verrado asserts that "quid pro quo" is not an appropriate standard for a
 20 determination on the issue of consolidation, and that Anthem's quid pro quo argument is in effect an
 21 argument that it agreed to the last-minute settlement agreement only because it thought it could push
 22 off a significant amount of the rate increase to other customers in the Anthem-Agua Fria Wastewater
 23 district.⁷⁸ Verrado states that Agua Fria residents certainly did not agree to such "quid pro quo."⁷⁹

24 ⁷¹ Anthem Br. at 6.

25 ⁷² Verrado Reply Br. at 4.

⁷³ Corte Bella Reply Br. at 3, citing to Decision No. 72047 at 84.

26 ⁷⁴ *Id.*

⁷⁵ Corte Bella Reply Br. at 3.

27 ⁷⁶ *Id.* at 4.

⁷⁷ Verrado Reply Br. at 5.

28 ⁷⁸ *Id.* at 4.

⁷⁹ *Id.*

1 **B. Cost of Service/Public Policy**

2 Anthem contends that continued consolidation of the Anthem-Agua Fria Wastewater district
3 is inconsistent with cost of service ratemaking principles and is contrary to good public policy.⁸⁰
4 Anthem argues that cost of service principles fairly dictate that those who use utility services should
5 pay for them,⁸¹ that cost of service is the single most important criterion in the development of fair
6 and reasonable revenues and related rates for a regulated utility,⁸² and that cost of service is the “very
7 essence of rate design.”⁸³ Anthem asserts that the current rates for the Anthem-Agua Fria
8 Wastewater district are not based on cost of service and do not “correctly assign cost responsibility
9 for all ratemaking components.”⁸⁴ Anthem states that under current rates, on a stand-alone basis, the
10 Anthem service area of the Anthem-Agua Fria Wastewater district would provide the Company a rate
11 of return on rate base of approximately 12.5 percent, and the combined Agua Fria service areas
12 would provide a slightly negative return on rate base.⁸⁵

13 RUCO argues that separate rates for separate systems respect the principle of traditional cost
14 of service ratemaking and ensure that those who use utility services pay for them, and that only when
15 policies in support of rate consolidation outweigh the principle of cost of service ratemaking should
16 rates be consolidated.⁸⁶ RUCO states that in the phase of this case leading to Decision No. 72047,
17 RUCO opposed rate consolidation, and that RUCO then cited among its reasons for opposing
18 consolidation bad timing due to recent rate increases in the prior rate case for some of the districts,
19 ratepayer resistance to large initial cost shifts, and lack of rate stability.⁸⁷ RUCO states that while this
20 case presents the issue of whether to deconsolidate an already-consolidated district, RUCO believes
21 the analysis for deconsolidation is the same as for consolidation of separate districts.⁸⁸

22 Russell Ranch argues that it meets the same “cost of service” argument posed by Anthem and
23 its justification to deconsolidate, and that preferential treatment cannot be given to one party when

24 _____
25 ⁸⁰ Anthem Br. at 4.

⁸¹ Anthem Reply Br. at 10.

⁸² Anthem Br. at 6, citing to Hearing Exhibit Anthem-1, Direct Testimony of Anthem witness Dan. L. Neidlinger, at 2.

⁸³ Anthem Br. at 6, citing to Tr. at 566-567 (Redirect Examination of RUCO witness William A. Rigsby).

⁸⁴ Anthem Br. at 6-7 and Anthem Reply Br. at 10, citing to Decision No. 72047 at 84.

⁸⁵ Anthem Br. at 7, citing to Tr. at 289 (Direct Examination of Anthem witness Dan L. Neidlinger).

⁸⁶ RUCO Br. at 2.

⁸⁷ *Id.* at 2-3, citing to Decision No. 72047 at 74-75.

⁸⁸ RUCO Br. at 2-3.

1 the same logic applies across the board.⁸⁹

2 Verrado and Corte Bella both note that although Anthem has proposed deconsolidation in this
3 case, Anthem earlier supported full consolidation of the Company's systems, and cited benefits of
4 rate consolidation.⁹⁰

5 Corte Bella acknowledges that full consolidation of all the Company's districts remains
6 controversial, but states that the facts and circumstances of this case, where the district has already
7 been consolidated for 10 years, are remarkably different from situations in which consolidation of
8 stand-alone districts is being considered.⁹¹ Corte Bella points out that despite RUCO's stated strong
9 belief of basing rates on cost of service, RUCO did not advocate for deconsolidation of the district
10 despite numerous opportunities to do so: not in the earlier phase of this rate case, prior to entering
11 the Open Meeting settlement agreement; not in the prior rate case involving the Anthem-Agua Fria
12 Wastewater district in 2002, which resulted in Decision No. 67093 (June 30, 2004); and not in the
13 prior rate case involving the Anthem-Agua Fria Wastewater district in 2006, which resulted in
14 Decision No. 73072.⁹² Corte Bella argues that after the district has remained consolidated for over 10
15 years with no party opposing the district's constitution, neither Anthem nor RUCO can show why
16 deconsolidation is now just and reasonable.⁹³ Corte Bella contends that deconsolidation at this point
17 in time in the name of adherence to a cost of service approach would be unfair to Corte Bella
18 residents, especially in light of the fact that Corte Bella did not have the benefit of evaluating other
19 factors that would affect their bills in the rate proceeding.⁹⁴

20 Verrado recalls that in RUCO's analysis in the prior phase of this case regarding the issue of
21 consolidation, RUCO's witness testified that a favorable consolidation proposal is one "that has the
22 least detrimental effect to the systems that are picking up costs for other systems at the initial stage of
23 consolidation. Over time, rates are stabilized and increases are minimized by spreading the costs of
24

25
26 ⁸⁹ Russell Ranch Br. at 3.

⁹⁰ Corte Bella Br. at 9 and Verrado Br. at 10-11, citing to Decision No. 74027 at 67-68.

⁹¹ Corte Bella Br. at 7.

⁹² *Id.* at 6, citing to Tr. at 514-15 and 578-79.

⁹³ Corte Bella Br. at 6-7.

⁹⁴ *Id.* at 6.

1 all systems . . .”.⁹⁵ Verrado states that in this present proceeding, because the systems are already
 2 consolidated, RUCO’s stated concern about the differences in cost at the initial stage of consolidation
 3 does not exist, and that the continued consolidation of the district will promote the rate stabilization
 4 to which RUCO’s witness referred for all customers, over time.⁹⁶

5 Corte Bella cites several reasons why Anthem and RUCO’s reliance on cost of service
 6 arguments to support deconsolidation of Anthem from the Anthem-Agua Fria Wastewater district is
 7 problematic.⁹⁷ Corte Bella states that all parties agree that cost of service is not the only factor
 8 considered when setting rates, pointing to the testimony of a Company witness who testified that
 9 some kind of balance must be established, because taken to an extreme, cost of service arguments
 10 would come down to every customer being in its own class.⁹⁸ Corte Bella states that Staff has
 11 consistently argued the importance of considering other factors such as gradualism and affordability
 12 when establishing rates,⁹⁹ that RUCO acknowledged those factors and its support for conservation-
 13 oriented rates that are not based on cost of service,¹⁰⁰ and that even Anthem acknowledges the need
 14 to use judgment to temper any result of cost of service.¹⁰¹ Corte Bella also points out that there has
 15 been no cost of service study done to justify the deconsolidated rate designs, despite the existence of
 16 the Anthem-Agua Fria Wastewater district for 10 years.¹⁰²

17 Corte Bella argues that deconsolidation of the Anthem service area from the remaining Agua
 18 Fria service area in this proceeding would deny the Agua Fria customers the opportunity to have rates
 19 established on cost of service, because this proceeding does not provide Corte Bella an opportunity to
 20 combine the Northeast Agua Fria and Sun City West service areas into one district, despite the fact
 21 that Corte Bella’s service area (the Northeast Agua Fria service area) shares the Northwest Valley
 22 Plant with the Sun City West Wastewater district.¹⁰³ Corte Bella states that if deconsolidation is
 23

24 ⁹⁵ Verrado Reply Br. at 2, citing to citing to May 3, 2010, Direct Rate Design/Rate Consolidation Testimony of RUCO
 witness Jodi Jerich (Exh.R-14) at 8-12.

25 ⁹⁶ Verrado Reply Br. at 2-3, citing to Hearing Exhibit V-2, Direct Testimony of Verrado witness Kent Simer, at 7-8.

26 ⁹⁷ Corte Bella Br. at 11-14.

27 ⁹⁸ *Id.* at 12, citing to Tr. at 277 (Company witness).

28 ⁹⁹ *Id.*, citing to Tr. at 592.

¹⁰⁰ *Id.*, citing to Tr. at 522-24.

¹⁰¹ *Id.*, citing to Tr. at 299, 325.

¹⁰² Corte Bella Br. at 13.

¹⁰³ *Id.* at 13-14.

1 approved in this proceeding, Corte Bella residents would be paying over three times the amount that
 2 Sun City West residents pay for wastewater service.¹⁰⁴ Corte Bella states that RUCO's witness
 3 agreed that it is inconsistent with the cost of service approach to not combine the Northeast Agua Fria
 4 service area where Corte Bella is located with the Sun City West Wastewater district service area,
 5 since both areas are served by the same wastewater treatment facility,¹⁰⁵ and Anthem's witness also
 6 testified that such a combination would make more sense than the current combination of service
 7 areas.¹⁰⁶

8 Verrado asserts that if the Commission gives Anthem's cost of service arguments the
 9 overriding weight that Anthem urges, the Commission will likely be asked to deconsolidate one or
 10 more of the remaining three service areas within the current Anthem-Agua Fria Wastewater district
 11 on the basis of cost of service.¹⁰⁷ Verrado states that whether or not different service areas are
 12 physically connected or share common costs, physically separate service areas will never have
 13 identical costs over time.¹⁰⁸ Verrado and Corte Bella both warn of a likely "domino effect" of
 14 deconsolidation based on cost of service, encouraging customers of other districts to seek
 15 deconsolidation based on one point in time when it is to their immediate advantage to do so.¹⁰⁹

16 C. Subsidization/ Shared Infrastructure

17 Anthem argues that deconsolidation is appropriate because the wastewater infrastructure
 18 system serving the Anthem service area serves only Anthem service area customers, and is neither
 19 physically connected nor geographically close to any of the treatment facilities used by the Company
 20 to serve other Anthem-Agua Fria Wastewater district customers.¹¹⁰ Anthem states that based on the
 21 Compliance Application schedules, on a deconsolidated basis, over \$2.4 million of the \$13.3 million
 22 in authorized revenues for the Anthem-Agua Fria Wastewater district would be transferred from the
 23 Anthem service area customers to Agua Fria service area customers,¹¹¹ and that part of this subsidy
 24

25 ¹⁰⁴ *Id.*

¹⁰⁵ Corte Bella Br. at 14, citing to Tr. at 531-34.

26 ¹⁰⁶ *Id.*, citing to Tr. at 330-31.

¹⁰⁷ Verrado Br. at 7-8.

27 ¹⁰⁸ *Id.* at 8.

¹⁰⁹ *Id.*; Corte Bella Br. at 15-16, citing to Tr. at 194-95.

¹¹⁰ Anthem Br. at 8.

28 ¹¹¹ *Id.* at 7, citing to Hearing Exhibit Anthem-1 at 4.

1 furnishes a return on the Northwest Valley Plant, which Anthem service area customers do not use.¹¹²
 2 Anthem asserts that requiring ratepayers in the Anthem service area to continue providing this
 3 subsidy to other ratepayers in the Anthem-Agua Fria Wastewater district would be unfair and
 4 unreasonable.¹¹³ Anthem states that if deconsolidation is denied, the subsidization is likely to
 5 continue, because the projected costs for carrying out the Company's projected five year capital
 6 improvement plan for the Agua Fria Wastewater service areas are higher than the projected costs for
 7 carrying out the projected five-year capital improvement plan for the Anthem wastewater system.¹¹⁴
 8 Anthem contends that lower rates, gradualism, and affordability for Agua Fria customers are being
 9 financed by Anthem's subsidy, and that any increased costs of deconsolidation are insubstantial in
 10 comparison to the \$2.4 million subsidy currently burdening Anthem.¹¹⁵

11 In response to the position of Corte Bella that deconsolidation is unjust to Corte Bella
 12 residents, Anthem responds that a substantial portion of the rate increase associated with
 13 deconsolidation is occasioned by the \$1.9 million revenue requirement allocated to the Northwest
 14 Valley Plant, which provides service to Corte Bella but not to Anthem.¹¹⁶ Anthem claims that Corte
 15 Bella is "seeking justification for someone else to bear wastewater costs of service properly
 16 attributable to Corte Bella."¹¹⁷ Anthem points out that on a deconsolidated basis, the service areas in
 17 the remainder of the Anthem-Agua Fria Wastewater district would be responsible for all of the
 18 Anthem-Agua Fria Wastewater district-allocated revenue for the Northwest Valley Plant.¹¹⁸

19 Anthem states that it recognizes that considerations other than cost can be considered, but
 20 argues that many of the benefits traditionally associated with consolidated districts have already been
 21 achieved, because the Company already operates on a consolidated basis,¹¹⁹ and that the subsidization
 22 present in current rates is of a magnitude too great to be ignored.¹²⁰ Anthem argues that the fact that
 23 the district has been consolidated for over ten years is irrelevant, and does not bar the Commission

24 ¹¹² Anthem Br. at 8.

25 ¹¹³ *Id.* at 4.

¹¹⁴ Anthem Reply Br. at 15, citing to Hearing Exhibit Anthem-10.

26 ¹¹⁵ Anthem Reply Br. at 11.

¹¹⁶ *Id.* at 4.

27 ¹¹⁷ *Id.*

¹¹⁸ Anthem Br. at 8.

28 ¹¹⁹ Anthem Reply Br. at 11, citing to Tr. at 208.

¹²⁰ Anthem Br. at 7.

1 from reviewing and modifying prior Decisions.¹²¹ Anthem believes that the fact that the Agua Fria
 2 area has not developed as was projected ten years ago, when the Anthem system's existing rate
 3 structure was applied to the new development, makes it now appropriate to deconsolidate the
 4 district.¹²² Anthem does not believe that consolidation is imminent,¹²³ and disagrees with
 5 intervenors' arguments that approving deconsolidation at this time will make future consolidation of
 6 the Company's districts more difficult in the future, citing to the testimony of a Company witness
 7 who opined that because consolidation is so difficult to achieve, deconsolidation is unlikely to make
 8 it any more difficult.¹²⁴

9 RUCO argues that the deconsolidated figures presented in the Compliance Application reveal
 10 that ratepayers in Anthem have been subsidizing the customers in the other service areas of the
 11 Anthem-Agua Fria Wastewater district.¹²⁵ RUCO also contends that it is critical to its analysis of the
 12 deconsolidation issue that the Anthem wastewater system shares no infrastructure with, and is located
 13 several miles away from, the other wastewater systems in the Anthem-Agua Fria Wastewater
 14 district.¹²⁶ RUCO contends that there is no evidence in the record to explain why the "two
 15 wastewater systems" were consolidated in the first place, and that had the district not been
 16 consolidated when the Anthem-Agua Fria Wastewater district CC&N was issued, customer rates
 17 would have more closely reflected the Company's actual cost of service and ratepayers would have
 18 had a better idea of what they could expect to pay for wastewater services when they bought
 19 homes.¹²⁷

20 In its Reply Brief, the Company clarified two of RUCO's statements on brief. First, the
 21 Company points out that in regard to RUCO's statement that the deconsolidated figures in the
 22 Compliance Application reveal that "Anthem ratepayers have been subsidizing Agua Fria
 23 customers,"¹²⁸ RUCO's statement is true only since January 1, 2011, when new rates became
 24

25 ¹²¹ Anthem Reply Br. at 5-6, 15.

¹²² *Id.* at 6.

26 ¹²³ *Id.* at 15, citing to Tr. at 323.

¹²⁴ *Id.* at 9, citing to Tr. at 199.

27 ¹²⁵ RUCO Br. at 3-4.

¹²⁶ *Id.*

¹²⁷ RUCO Br. at 3.

28 ¹²⁸ Co. Reply Br. at 3.

1 effective, based on a 2008 test year. The Company explains that, as displayed in the Compliance
 2 Application, both of the potential deconsolidated districts required a rate increase from prior existing
 3 rates, and therefore, Anthem ratepayers could not have been subsidizing other service area ratepayers,
 4 because the rates previous to 2011 were inadequate to recover Anthem's own cost of service.¹²⁹ The
 5 Company also states that there is no evidence from years prior to 2008 that supports either the view
 6 that Anthem ratepayers have been subsidizing Agua Fria ratepayers, or a contrary view that Agua
 7 Fria ratepayers have been subsidizing Anthem ratepayers.¹³⁰

8 The Company also points out that contrary to RUCO's statement that "there is no evidence in
 9 the record to explain why the two wastewater systems were consolidated in the first place," the
 10 Company's witness Ms. Murrey filed three and one half pages of testimony concerning why the four
 11 systems were consolidated.¹³¹

12 Corte Bella states that if deconsolidation is approved, the outcome will be a partially
 13 consolidated district that contains three separate wastewater systems that are not physically connected
 14 in any way, which is the very situation of partial consolidation that Anthem advocates against for
 15 itself, and which goes against the strict cost of service principles advocated by Anthem and RUCO.¹³²

16 Russell Ranch asserts that RUCO's support for the Anthem deconsolidation lacks merit and
 17 credibility due to its admitted flawed interpretations and its failure to validate the cost of service for
 18 the individual Agua Fria service areas.¹³³ Russell Ranch states that RUCO's witness acknowledged
 19 that the deconsolidated rates RUCO is recommending do not represent the cost of service to those
 20 communities, and that there may be cross-subsidization between the three service areas.¹³⁴ Russell
 21 Ranch contends that it is irresponsible for RUCO, as a consumer advocate, to establish a policy
 22 position in support of the Anthem deconsolidation in the absence of a full knowledge of the Anthem-
 23 Agua Fria Wastewater district's composition and a complete understanding of the impact on all
 24 service areas, communities and ratepayers within the district.¹³⁵ Russell Ranch and Verrado both

25 ¹²⁹ *Id.*

26 ¹³⁰ *Id.*

27 ¹³¹ Co. Reply Br. at 4, citing to Hearing Exhibit A-1 at 3-6.

¹³² Corte Bella Br. at 15; Corte Bella Reply Br. at 6.

¹³³ Russell Ranch Br. at 7.

¹³⁴ *Id.*, citing to Tr. at 543-544.

28 ¹³⁵ *Id.*, citing to Tr. at 543-544.

1 point out that the direct testimony of RUCO's witness in this hearing indicated an early
 2 misunderstanding of the physical layout of the Anthem-Agua Fria Wastewater district, and that the
 3 witness admitted at the hearing he did not understand at the time he drafted his direct testimony that
 4 the Agua Fria portion of the district included three physically separate wastewater infrastructure
 5 systems.¹³⁶ RUCO chose not to file a Reply Brief in response to the criticisms of its analysis and
 6 recommendations in this case.¹³⁷

7 Verrado states that although the parties to this proceeding focused a great deal on the lack of
 8 physical connection between the four service areas in the Anthem-Agua Fria Wastewater district, it is
 9 important to note that all four service areas are connected in other significant ways, in that they are all
 10 within the Phoenix metropolitan area, and they share significant costs, including labor costs and
 11 service company costs.¹³⁸ Verrado points out that given the distances between all four service areas
 12 in the current district, RUCO's heavy reliance on the physical separation and cost of service
 13 differences between only one of four separate systems is arbitrary.¹³⁹ Verrado states that the
 14 Commission and parties to the cases in which the new rates were established for the Anthem-Agua
 15 Fria Wastewater district have been reviewed repeatedly, in prior Commission Decision Nos. 69671,
 16 63455, 68854, and 67015 (CC&N extension Decisions), and in Decision Nos. 67093 and 73072 (rate
 17 case Decisions), and the consolidated status of the district was not an issue.¹⁴⁰ Verrado and Corte
 18 Bella each argue that this prior ratemaking treatment of the consolidated district is well-established,
 19 and consistent with the Commission's more recent focus on encouraging consolidation.¹⁴¹

20 Verrado asserts that ratemaking principles should be applied in a manner that avoids rate
 21 volatility, and that in considering cost of service principles in the context of consolidation
 22 determinations, a longer view should be taken than data from one test year, in order to consider what
 23

24 ¹³⁶ Russell Ranch Br. at 6; Verrado Reply Br. at 3, citing to Hearing Exhibit R-1 at 5 and Tr. at 501-503.

¹³⁷ See RUCO's Notice of Filing docketed February 7, 2012.

25 ¹³⁸ Verrado Br. at 11, citing to Tr. at 196-198.

¹³⁹ Verrado Br. at 3-4.

26 ¹⁴⁰ *Id.* at 7.

27 ¹⁴¹ Corte Bella Br. at 5-6; Verrado Br. at 7 and Corte Bella Br. at 7-9, citing to Decision No. 71410 (December 8, 2009) at
 28 51. Corte Bella also pointed to the Commission's recent Decision No. 71845 (August 25, 2010), which consolidated
 Arizona Water Company's Lakeside and Overgaard systems and its Casa Grande Coolidge and Stanfield systems, where
 the Commission stated that partial consolidation moved toward the possibility of a future single-tariff pricing structure
 without the substantial rate impacts of consolidation being accomplished all at once.

1 is likely to happen over time.¹⁴² Corte Bella asserts that Anthem's position in favor of
 2 deconsolidation at this time is shortsighted, because the current subsidy is temporary.¹⁴³ Verrado and
 3 Corte Bella point out that while Anthem argues that it is "subsidizing" other Anthem-Agua Fria
 4 Wastewater district customers now, that over time, as the built-out Anthem service area infrastructure
 5 ages and the Agua Fria service areas grow, the tables will likely turn and the Anthem customers will
 6 be "subsidized" by the other Anthem-Agua Fria Wastewater district customers in the future, as the
 7 Agua Fria service areas customer base continues to increase, with "subsidization" passing back and
 8 forth as infrastructure replacements become necessary over time in different service areas.¹⁴⁴ Corte
 9 Bella states that the current subsidy will likely zero out, and even shift in favor of the Anthem service
 10 area over time, as Anthem's witness acknowledged.¹⁴⁵ Verrado and Corte Bella both argue that
 11 despite periodic "subsidies" from service area to service area, over the long term, all customers in a
 12 consolidated district should enjoy more stable rates with the ability to spread new costs over a larger
 13 customer base.¹⁴⁶

14 Corte Bella points out that despite Anthem's claims to the contrary, consolidation remains an
 15 open issue following Decision No. 72047.¹⁴⁷ Verrado states that Decision No. 72047 rejected a full
 16 consolidation for the Company due to the large disparity in rates among the Company's districts, and
 17 because not all of the Company's districts were being considered, ordered the Company to develop a
 18 consolidation proposal in a future rate application which includes all of its systems.¹⁴⁸ Verrado
 19 asserts that deconsolidation in this proceeding will worsen the rate disparity problem noted in
 20 Decision No. 72047, and for that reason it would be better to defer a decision on the proposed
 21 deconsolidation until that future rate case.¹⁴⁹ Corte Bella contends that just as the large disparity in
 22 rates was too great an impediment to support full consolidation in Decision No. 72047, the large
 23 disparity that would result if deconsolidation is approved is also an insurmountable impediment to
 24

25 ¹⁴² Verrado Br. at 10.

26 ¹⁴³ Corte Bella Reply Br. at 5.

27 ¹⁴⁴ Verrado Br. at 10; Corte Bella Br. at 4.

28 ¹⁴⁵ Corte Bella Reply Br. at 4, citing to Tr. at 303-304.

¹⁴⁶ Verrado Br. at 10, citing to Hearing Exhibit V-2 at 11; Corte Bella Br. at 5.

¹⁴⁷ Corte Bella Br. at 11.

¹⁴⁸ Verrado Br. at 11, citing Decision No. 72047 at 84-85, 123.

¹⁴⁹ Verrado Br. at 9-10.

1 deconsolidation in this proceeding.¹⁵⁰

2 **D. Anthem Revenue Transition Phase-in Proposal**

3 Anthem states that it is sensitive to the concerns expressed by intervenors in this proceeding
4 regarding the significant transfer of revenue responsibility from Anthem service area customers to
5 customers in the remaining service areas in the Anthem-Agua Fria Wastewater district.¹⁵¹ Anthem
6 states that it is for this reason that Anthem has agreed to phase in the revenue transition to
7 deconsolidation over a three year period.¹⁵² Anthem also states that because Anthem is willing to pay
8 more over the three-year period in order to allow for smoother implementation of deconsolidated
9 rates, the Commission should not deny deconsolidation simply because there would be some
10 resulting rate shock to Agua Fria ratepayers.¹⁵³ Under the Anthem phase-in proposal, annual
11 adjustments of approximately \$800,000 would be made progressively decreasing the rates of
12 Anthem-Agua Fria Wastewater district customers in the Anthem service area while correspondingly
13 increasing the rates of Anthem-Agua Fria Wastewater district customers not in the Anthem service
14 area.¹⁵⁴ Under Anthem's phase-in proposal, adjustments would be made to the revenue levels
15 authorized in Decision No. 72047, with no overall change to revenue levels to the Company.¹⁵⁵ At
16 the end of three years, the final rate impacts of the phase-in on customers would be those proposed by
17 the Company and Staff in the event of deconsolidation.

18 RUCO states that it shares the concerns of the intervenors regarding the potential rate shock
19 that will result if deconsolidation is approved, and that it can only support deconsolidation if a rate
20 mitigation proposal is approved.¹⁵⁶ RUCO asserts that Anthem's phase-in plan is fair and appropriate
21 for this case, and that it is a generous plan from the standpoint of Anthem ratepayers.¹⁵⁷

22 Corte Bella states that it is undisputed that deconsolidation would result in rate shock;
23 characterizes the approximately \$60 increase in average monthly wastewater rates from 2010 rates
24

25 ¹⁵⁰ Corte Bella Br. at 10.

¹⁵¹ Anthem Br. at 8-9; Anthem Reply Br. at 20.

¹⁵² Anthem Br. at 9.

¹⁵³ Anthem Reply Br. at 20.

¹⁵⁴ Anthem Br. at 9.

¹⁵⁵ *Id.*

¹⁵⁶ RUCO Br. at 4.

¹⁵⁷ *Id.* at 4-5.

1 that would result under the proposed deconsolidation plan for customers in the Agua Fria service
 2 areas as “astonishing;” and argues that it is unfair to those customers to deconsolidate the district at
 3 this time.¹⁵⁸

4 Verrado contends that rate shock will result if the rates proposed for a stand-alone Agua Fria
 5 Wastewater district are implemented, and Anthem’s proposed phase-in is only a mitigation of that
 6 rate shock.¹⁵⁹ Russell Ranch states that one becomes desensitized to the meaning of the term rate
 7 shock because it has been discussed so much over the duration of this case, but since the formation of
 8 the Anthem-Agua Fria Wastewater district in 1998, the accumulated rate increase for the three Agua
 9 Fria service areas, if Anthem is allowed to deconsolidate, would be in excess of 316 percent.¹⁶⁰ Corte
 10 Bella characterizes the Anthem phase-in plan as “death by a thousand cuts,” and Verrado and Corte
 11 Bella both point out that the Anthem phase-in proposal would apply only to the additional rate
 12 increase in excess of the 54 percent increase already granted for the district in Decision No. 72047.¹⁶¹
 13 Verrado and Corte Bella also point out that in pending Docket No. W-1303A-10-0448, Agua Fria
 14 Water district customers are also facing an increase in their water rates.¹⁶² Verrado states that the
 15 Agua Fria Water district customers expect an increase of 63.22 percent by the third year of the phase-
 16 in under the parties’ settlement agreement that is being considered in that docket.¹⁶³ Verrado believes
 17 the Commission should consider the potential additional impact of the pending water rate case
 18 increase on Agua Fria customers when making a determination on deconsolidation in this case.¹⁶⁴

19 **E. Notice to Customers of the Potential Increase**

20 Corte Bella states that Agua Fria customers were not put on notice of the proposed
 21 deconsolidation of the Anthem-Agua Fria Wastewater district, and the resulting 133.90 percent rate
 22 increase, until the Company filed the Compliance Application, four months after Decision No. 72047
 23

24 ¹⁵⁸ Corte Bella Br. at 2, 5; Corte Bella Reply Br. at 6.

25 ¹⁵⁹ Verrado Br. at 5, citing to Hearing Exhibit V-1 at 8-9 and Hearing Exhibit CB-1, Direct Testimony of Corte Bella
 witness Robert Rials, at 9-10.

26 ¹⁶⁰ Russell Ranch Br. at 3.

27 ¹⁶¹ Corte Bella Br. at 3-4; Verrado Br. at 5, citing to Tr. at 315.

28 ¹⁶² Corte Bella Br. at 3; Verrado Br. at 6.

¹⁶³ Verrado Br. at 6, citing to Settlement Agreement docketed December 15, 2011, in Docket No. WS-01303A-10-0448,
 Ex. Settlement H-4 (Step 3).

¹⁶⁴ Verrado Br. at 6, citing to Tr. at 310.

1 was docketed.¹⁶⁵ Corte Bella notes that, as Anthem's witness acknowledged at the hearing, there
 2 were determinations made in the proceeding leading to Decision No. 72047 that will now have a
 3 great impact if deconsolidation takes place.¹⁶⁶

4 Verrado states that at the inception of this rate case, the Company published notice of a
 5 potential 81.8 percent rate increase over test year revenues, and notes that public comments in this
 6 case and in Docket No. W-01303A-10-0448 indicate that some customers believe they did not
 7 receive the required notice of the rate increase request, or were confused about whether they were
 8 included in the affected districts.¹⁶⁷ Verrado states that Agua Fria customers were not notified until
 9 after Decision No. 72047 was issued, and after the Company submitted the Compliance Application,
 10 that they could instead be facing the increase of approximately 134 percent over test year rates that
 11 would result from deconsolidation, which constitutes an approximately 53 percent greater rate impact
 12 than was originally noticed.¹⁶⁸ Verrado points out that because the rate base and revenue requirement
 13 were already determined in Decision No. 72047, Agua Fria customers in this compliance proceeding
 14 no longer have the ability to reopen those determinations.¹⁶⁹ Verrado states that it is too late now to
 15 know whether the substantial difference in the noticed rate impact would have caused Agua Fria
 16 customers to have become more involved earlier in the main rate case, but that they became
 17 substantially involved when they were notified after Decision No. 72047 of the potential for the
 18 133.90 percent overall increase.¹⁷⁰ Verrado states that Agua Fria customers were not represented in
 19 the Open Meeting settlement negotiations that led to this proceeding, and for this reason, Verrado
 20 requests that the determination on potential deconsolidation be delayed until a future rate case where
 21 Agua Fria residents are assured of having a full opportunity to investigate the reasons for the
 22 significant cost of service in the Agua Fria areas.¹⁷¹

23 Anthem argues that the fact that the Agua Fria intervenors were not represented in the
 24 previous phase of this rate case and in the settlement discussions is a direct result of their own

25 ¹⁶⁵ Corte Bella Br. at 3. (Corte Bella states that the rate increase would be 139.7 percent.)

26 ¹⁶⁶ Corte Bella Br. at 3-4, citing to Tr. at 318-19.

27 ¹⁶⁷ Verrado Br. at 4.

¹⁶⁸ *Id.*

¹⁶⁹ Verrado Br. at 5.

¹⁷⁰ *Id.* at 4-5.

28 ¹⁷¹ *Id.* at 5.

1 respective choices not to participate,¹⁷² and that Anthem ratepayers should not now be required to
 2 wait until a future rate proceeding for deconsolidation to occur.¹⁷³ Anthem contends that delaying
 3 reconsideration of deconsolidation until a future rate case is not warranted, because it would not
 4 provide the Agua Fria intervenors any meaningful opportunity that they have not already been
 5 afforded,¹⁷⁴ and that despite the intervenors' participation in this proceeding, the only solution they
 6 suggest is that Anthem continue to subsidize them.¹⁷⁵

7 **F. Phoenix OWU Rate**

8 On June 23, 2011, Phoenix docketed a filing titled "Motion to Intervene and Notice of Errors
 9 in Exhibit 'A' to Decision No. 72047." Attached to the filing were the direct testimonies of Andy
 10 Terrey and Tammy Ryan. The Motion indicated that Phoenix wished to intervene in the proceeding
 11 on the Compliance Application.

12 On July 5, 2005, a Procedural Order was issued granting intervention to Phoenix. The
 13 Procedural Order noted that Phoenix did not intervene in, and was not a party to, the proceeding that
 14 resulted in Decision No. 72047, but that in addition to requesting intervention in the proceeding on
 15 the Compliance Application, Phoenix's June 23, 2011 Motion made a further request as follows:

16 Phoenix requests that the Commission set a limited rehearing [of Decision No. 72047]
 17 for the sole purpose to clarify pages ii, iv and vi to "Exhibit A" to set out a Wholesale
 18 Potable Water Rate of \$2.32 per one thousand gallons delivered and a Wheeling Water
 19 Rate of \$0.30 / Kgal delivered unless Arizona American can support a change in either
 rate by submitting an analysis to Phoenix of the actual costs paid or incurred by
 Arizona American with respect to providing the respective services under the Anthem
 Wholesale Water/Wastewater Service Agreement.

20 The Procedural Order noted that the Commission had not acted on the above-quoted request, and that
 21 Rehearing of Decision No. 72047 has not been granted.

22 On October 11, 2011, Phoenix filed the surrebuttal testimonies of its witnesses Allen Eneboe,
 23 Andy Terrey and Denise Olson. On October 18, 2011, Phoenix filed an additional copy of Exhibit A
 24 to the surrebuttal testimony of its witness Denise Olsen.

25 On October 20, 2011, Anthem filed a Motion to Exclude Issue from Hearing. On October 25,

26 ¹⁷² Anthem Reply Br. at 16-18, citing to Tr. at 415 (DMB was an intervenor in the previous hearing and did not
 27 participate in the Open Meeting settlement discussions.)

¹⁷³ Anthem Reply Br. at 19.

¹⁷⁴ *Id.* at 18.

¹⁷⁵ *Id.* at 18-19.

1 2011, Verrado filed a Joinder in Anthem's Motion to Exclude Issue from Hearing. On November 3,
2 2011, Phoenix filed its Response to Motion to Exclude Issue from Hearing.

3 At the November 7, 2011 prehearing conference, Anthem's Motion to Exclude Issue from
4 Hearing was discussed. After hearing argument from the parties, the Motion was denied, with the
5 caveats that this proceeding would not be a rehearing of Decision No. 72047, that the overall revenue
6 requirement determined in Decision No. 72047 will not change in this proceeding, and that the issues
7 in this proceeding are limited to the schedules filed in the Compliance Application. With those
8 caveats, it was ruled that Phoenix would be allowed to participate in the hearing and present factual
9 evidence and legal argument to support its position in regard to the schedules filed by the Company
10 in the Compliance Application. Phoenix was reminded, and recognized on the record, that the
11 Commission had not granted its request to reopen Decision No. 72047, and that if it wished to pursue
12 its request as stated in its intervention request to reopen Decision No. 72047, that it would need to
13 pursue that request separately, and not in this proceeding.

14 Phoenix participated in the Compliance Application hearing through counsel. Phoenix did not
15 offer evidence, and withdrew its witnesses.¹⁷⁶

16 Phoenix pays the Company for wastewater treatment services it receives in Anthem under the
17 Company's tariffed Other Wholesale User ("OWU") rate. Phoenix contends that the OWU rate of
18 \$5.57 per 1,000 gallons established by Decision No. 72047 is unsupported, as it was based on a cost
19 of service study conducted in a 2006 rate case.¹⁷⁷ Phoenix asserts that testimony at the hearing
20 establishes that the OWU rate established in Decision No. 72047 is incorrect.¹⁷⁸

21 Phoenix requests that the Commission re-examine the wastewater treatment services rate
22 applicable to Phoenix.¹⁷⁹

23 The Company states on brief that Decision No. 72047 left this docket open to consider just
24 one issue, whether to deconsolidate the Anthem-Agua Fria Wastewater district, and contends that
25

26 ¹⁷⁶ See Tr. at 479. Counsel for Phoenix stated that it had the opportunity to present the case it wanted to within the
27 confines of the Procedural Order.

¹⁷⁷ Phoenix Br. at 4-5.

¹⁷⁸ *Id.* at 5, citing to Tr. at 606 and 631.

28 ¹⁷⁹ Phoenix Br. at 6; Phoenix Post-Hearing Reply Brief ("Phoenix Reply Br." at 2).

1 Phoenix's request to re-examine the OWU rate is outside the scope of this proceeding.¹⁸⁰ The
 2 Company further contends that Phoenix's request is essentially a redundant and improper request for
 3 rehearing of Decision No. 72047, which is already before the Commission.¹⁸¹

4 The Company objects to Phoenix's issue being evaluated in an additional phase of this case.
 5 The Company states that this case is based on a 2008 test year, and that because every cost and
 6 revenue has most likely changed materially, further re-examination of the data would consume most
 7 of 2012, with any rate change not likely until late 2012 or 2013.¹⁸² The Company also states that a
 8 reduction to the OWU rate without any consideration of offsetting changes to other customers' rates
 9 would result in the establishment of rates which would not allow the Company to recover its
 10 authorized revenue requirement and, argues that this would be contrary to Decision No. 72047 and
 11 would result in rates that are no longer just and reasonable.¹⁸³

12 G. Conclusions

13 Anthem contends that deconsolidation of the Anthem-Agua Fria Wastewater district is
 14 consistent with the determination in Decision No. 72047 to reject consolidation of the Company's
 15 districts, and that it would be "completely arbitrary" for the district to remain consolidated, when the
 16 Anthem Water district and Agua Fria Water district are separate,¹⁸⁴ and the Company maintains two
 17 separate business units for the Anthem-Agua Fria Wastewater district.¹⁸⁵ We agree.

18 Maintaining the Anthem-Agua Fria Wastewater District as a consolidated district would not
 19 result in just and reasonable rates for Anthem residents. This is so for at least two reasons. First, it is
 20 undisputed that the large disparity in deconsolidated rates is due to the Northwest Valley Plant, the
 21 Verrado Reclamation Facility and its expansion as well as the Russell Ranch Reclamation Facility.
 22 By virtue of geographic separation and no interconnection facilities, Anthem residents do not and
 23 cannot use these facilities, whereas Agua Fria wastewater customers do. Thus, in order to more
 24 accurately allocate costs to the cost-causers, we will deconsolidate Anthem from the Anthem/Agua

25 ¹⁸⁰ Co. Reply Br. at 2.

26 ¹⁸¹ *Id.*

27 ¹⁸² Co. Br. at 2-3.

28 ¹⁸³ *Id.* at 3.

¹⁸⁴ Anthem Reply Br. at 7-8, citing to RUCO Br. at 4 ("RUCO finds it persuasive that the Commission kept the Anthem and Agua Fria water systems as stand alone systems.")

¹⁸⁵ Anthem Reply Br. at 8, citing to Tr. at 82-83.

1 Fria Wastewater District at this time.

2 Some have argued against deconsolidating Anthem from the Agua Fria Wastewater District
3 by pointing out that the Agua Fria district itself is made up of three distinct wastewater systems that
4 are not interconnected and do not share infrastructure with one another. Accordingly, these parties
5 argue that the deconsolidation of Anthem, will not result in a pure assignment of cost causation
6 among the three separate systems within the Agua Fria wastewater district. We are not persuaded by
7 this line of argument. First, we do not believe the perfect (a complete allocation of costs to each
8 system within the Agua Fria wastewater district) should be the enemy of the good (a more accurate
9 allocation of costs between the Anthem and Agua Fria wastewater districts). Second, no party has
10 actively sought to deconsolidate the separate systems within the Agua Fria wastewater district as
11 Anthem has done in this one. If parties believe that fairness requires the Commission to consider
12 further deconsolidation of the Agua Fria district they are free to advocate for such a result in future
13 Commission proceedings.

14 Moreover, even if we were to set aside our desire to establish rates on cost causation
15 principles, we believe deconsolidation of the Anthem wastewater district would be appropriate in this
16 case in order to preserve the integrity of settlement negotiations that occur in Commission
17 proceedings. In our December 15, 2010 Open Meeting, we encouraged the parties to negotiate the
18 settlement of contentious legal and equitable issues involving the disputed refund payments that the
19 Company paid to Pulte. As part of the settlement agreement that was ultimately reached, Anthem
20 surrendered several arguments against recognizing the disputed refund payments to Pulte for
21 ratemaking purposes. Anthem's willingness to do so was based on the gains Anthem would make in
22 other areas under the settlement agreement, including the timely deconsolidation of the Anthem/Agua
23 Fria Wastewater District. The record suggests that deconsolidation of the Anthem/Agua Fria
24 Wastewater District was vital to Anthem's willingness to support the settlement as a complete
25 package. Therefore, in order to preserve the integrity of the settlement negotiations that occur in
26 Commission proceedings, we believe it is in the public interest to deconsolidate Anthem from the
27 Anthem/Agua Fria Wastewater District at this time.

28 We recognize that our decision to deconsolidate Anthem from Agua Fria will result in a

1 significant shift in revenue responsibility from Anthem to Agua Fria. While we agree with Anthem
 2 that it is appropriate to eliminate the current subsidy that exists, we are mindful of the impact this
 3 revenue shift will have on Agua Fria ratepayers. In order to mitigate the impacts of the revenue shift,
 4 we will adopt the revenue transition plan proposed by Anthem, with one modification. In order to
 5 give Agua Fria customers additional time to prepare for this change, we will require the Company to
 6 begin the initial phase of the three-year revenue transition plan on January 1, 2013, instead of
 7 immediately as proposed by Mr. Neidlinger.

8 The evidence in this proceeding, including but not limited to the OWU tariff issue raised by
 9 Phoenix, demonstrates the need for the Company to file an updated cost of service study, and we will
 10 require it to do so. We will require the cost of service studies and other information supporting
 11 consolidation that are provided by the Company in its filing to be sufficient for all parties to make
 12 their own reasoned proposals either for or against consolidation or deconsolidation, consistent with
 13 sound ratemaking principles. At that time, with a cost of service study in hand, the Company can
 14 address the issues Phoenix raised in this proceeding regarding the OWU tariffed rate applicable to
 15 wastewater treatment services provided to Phoenix under their agreement.

16 * * * * *

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

19 **FINDINGS OF FACT**

20 1. On July 2, 2009, the Company filed with the Commission an application for rate
 21 increases for its Anthem Water District, Sun City Water District, Anthem-Agua Fria Wastewater
 22 District, Sun City Wastewater District, and Sun City West Wastewater District.

23 2. Intervention in this matter was granted to RUCO; Anthem; PORA; W.R. Hansen; the
 24 WUAA; the Resorts; the Town of Paradise Valley; the Anthem Golf and Country Club; Marshall
 25 Magruder; DMB; Mashie, LLC dba Corte Bella Golf Club; Larry D. Woods; and Philip H. Cook.

26 3. On January 6, 2011, the Commission issued Decision No. 72047 in these dockets.
 27 Decision No. 72047 left the dockets open for the sole purpose of considering the design and
 28 implementation of stand-alone revenue requirements and rate designs for separate Anthem

1 Wastewater and Agua Fria Wastewater districts as provided in the settlement reached by the
2 Company, Anthem, RUCO and Staff during the Open Meeting at which Decision No. 72047 was
3 considered. Decision No. 72047 ordered the Company to file, by April 1, 2011, an application
4 supporting consideration of stand-alone revenue requirements and rate designs for separate Anthem
5 Wastewater and Agua Fria Wastewater districts, and made the rates approved for the Anthem-Agua
6 Fria Wastewater district interim, subject to change pursuant to a Commission determination on the
7 Company's April 1, 2011 filing.¹⁸⁶

8 4. On April 1, 2011, the Company complied with Decision No. 72047 by filing its
9 Compliance Application. The filing included direct testimony and exhibits concerning the separate
10 revenue requirements and separate rate designs for new Anthem Wastewater and Agua Fria
11 Wastewater districts on a stand-alone basis using the combined revenue authorizations in Decision
12 No. 72047.

13 5. On April 4, 2011, a Procedural Order was issued setting a procedural conference to
14 commence on April 19, 2011, in order to provide an opportunity for discussion of a procedural
15 schedule, public notice of the Compliance Application, and other procedural issues prior to the
16 issuance of a Procedural Order governing the processing of the Compliance Application.

17 6. On April 8, 2011, the Company filed a Notice of Filing Certified Mail Receipt.

18 7. On April 13, 2011, the Company filed a Correction Concerning Certified Mail
19 Receipt.

20 8. On April 19, 2011, DMB filed a Notice of Substitution of Counsel.

21 9. On April 19, 2011, the procedural conference convened as scheduled. Appearances
22 were entered through counsel for the Company, Anthem, Anthem Golf and Country Club, DMB,
23 RUCO, and Staff. The parties discussed public notice issues and the timing of discovery and pre-
24 filing testimony.

25 10. On April 27, 2011, the Commission issued a Procedural Order Setting Hearing for
26 Consideration of Compliance Application. The Procedural Order set the hearing to commence on
27

28 ¹⁸⁶ Decision No. 72047 at 121.

1 October 17, 2011, and set associated procedural deadlines, including a deadline for publication of
2 notice of the Compliance Application and Hearing. The Procedural Order directed the Company to
3 mail to each of its customers in the Anthem-Agua Fria Wastewater district, and to each of the
4 homeowners' associations located in the Anthem-Agua Fria Wastewater district, a copy of the
5 required notice by First-Class U.S. Mail, with mailing to be completed no later than May 20, 2011.

6 11. On April 28, 2011, Verrado filed a Motion to Intervene.

7 12. On May 11, 2011, a Procedural Order was issued granting intervention to Verrado.

8 13. On May 24, 2011, the Company filed an Affidavit of Mailing.

9 14. On June 21, 2011, Corte Bella filed a Motion/Application to Intervene.

10 15. On June 23, 2011, John Luke, Managing Member, Russell Ranch, LLC filed a Motion
11 to Intervene.

12 16. On June 23, 2011, Frederick G. Botha filed a Motion to Intervene.

13 17. On June 24, 2011, a Procedural Order was issued indicating that the intervention
14 request of Russell Ranch, LLC would be considered once an intervention request was filed in this
15 docket by counsel representing Russell Ranch, LLC in this proceeding on the Compliance
16 Application.

17 18. On June 24, 2011, Russell Ranch filed a Motion to Intervene. Russell Ranch is an
18 Arizona non-profit corporation. Attached to the June 24, 2011, Motion was a copy of a June 20,
19 2011, Russell Ranch Board of Directors Resolution authorizing its President, Pauline A. Harris
20 Henry, to represent it in this proceeding.

21 19. On June 30, 2011, a Procedural Order was issued granting intervention to Corte Bella,
22 Frederick G. Botha, and Russell Ranch. The Procedural Order authorized Pauline A. Harris Henry to
23 represent Russell Ranch in this proceeding before the Commission.

24 20. On June 23, 2011, Phoenix docketed a filing titled "Motion to Intervene and Notice of
25 Errors in Exhibit 'A' to Decision No. 72047." The Motion indicated that Phoenix wished to
26 intervene in the proceeding on the Compliance Application.

27 21. On July 5, 2011, a Procedural Order was issued granting intervention to Phoenix. The
28 Procedural Order noted that Phoenix did not intervene in, and was not a party to, the proceeding that

1 resulted in Decision No. 72047, but that in addition to requesting intervention in the proceeding on
2 the Compliance Application, the City's June 23, 2011 Motion made a further request as follows:

3
4 Phoenix requests that the Commission set a limited rehearing [of Decision No. 72047]
5 for the sole purpose to clarify pages ii, iv and vi to "Exhibit A" to set out a Wholesale
6 Potable Water Rate of \$2.32 per one thousand gallons delivered and a Wheeling Water
7 Rate of \$0.30 / Kgal delivered unless Arizona American can support a change in either
8 rate by submitting an analysis to Phoenix of the actual costs paid or incurred by
9 Arizona American with respect to providing the respective services under the Anthem
10 Wholesale Water/Wastewater Service Agreement.

11 22. The Procedural Order noted that the Commission had not acted on the above-quoted
12 request. Rehearing of Decision No. 72047 has not been granted.

13 23. On July 11, 2011, Marshall Magruder filed a Request to Withdraw, indicating his wish
14 to withdraw from the remaining matters in these dockets.

15 24. On July 12, 2011, Corte Bella docketed a Stipulated Motion to Continue Deadline for
16 Filing Direct Testimony. The Motion requested the issuance of a Procedural Order extending the
17 date for Staff and Intervenors to file their direct testimony on the Compliance Application from July
18 26, 2011 to August 9, 2011, and indicated that the Company, Anthem, Verrado, RUCO and Staff did
19 not object to the request.

20 25. On July 13, 2011, The Company filed a Response to the July 12, 2011 Motion.
21 Therein, The Company stated that while it did not oppose Corte Bella's request for a two week
22 extension to file direct testimony, it could not agree to the request unless all other procedural dates,
23 including the hearing date, were extended for at least the same amount of time. The Company stated
24 that an equal extension of time for the remaining deadlines was necessary in order to allow it
25 sufficient time to review the direct testimony and to prepare and file its responsive testimony.

26 26. On July 14, 2011, Frederick Botha filed a data request in the docket.

27 27. On July 15, 2011, the Commission issued a Procedural Order Modifying Procedural
28 Schedule. The Procedural Order continued the hearing on the Compliance Application to November
14, 2011, and reserved the noticed October 17, 2011 hearing date for public comment only. The
Procedural Order also granted Marshall Magruder's request to withdraw, and ordered removal of
Marshall Magruder from the service list in the docket.

- 1 28. Also on July 15, 2011, Anthem filed a Response to the July 12, 2011 Motion.
- 2 29. On July 22, 2011, Corte Bella filed a Notice of Appearance of Co-Counsel.
- 3 30. On August 16, 2011, RUCO filed the direct testimony of its witnesses William A.
- 4 Rigsby and Rodney L. Moore.
- 5 31. On August 16, 2011, Corte Bella filed the direct testimony of its witness Robert Rials.
- 6 32. On August 16, 2011, Russell Ranch filed the direct testimony of its witness Daniel
- 7 O'Connor.
- 8 33. On August 16, 2011, DMB filed the direct testimony of its witness David Nilsen.
- 9 34. On August 16, 2011, Anthem filed the direct testimony of its witness Dan L.
- 10 Neidlinger.
- 11 35. On August 16, 2011, Frederick Botha filed copies of responses to his data requests.
- 12 36. On August 16, 2011, Verrado filed the direct testimony of its witnesses Melinda
- 13 Gulick and Kent Simer.
- 14 37. On August 16, 2011, Staff filed the direct testimony of its witness Gerald W. Becker.
- 15 38. On August 18, 2011, Russell Ranch refiled the direct testimony of its witness Daniel
- 16 O'Connor.
- 17 39. On August 18, 2011, RUCO filed a Notice of Disclosure, to which was attached the
- 18 Notice of Disclosure originally filed in these dockets on February 24, 2010, prior to the hearing on
- 19 the rate application which culminated in the Commission's issuance of Decision No. 72047.
- 20 40. On August 29, 2011, Marshall Magruder docketed a filing in these dockets.
- 21 41. On September 8, 2011, the Company filed its Response to Mr. Marshall Magruder.
- 22 42. On September 13, 2011, Anthem Golf and Country Club filed the rebuttal testimony
- 23 of its witness Desi Howe.
- 24 43. On September 13, 2011, the Company filed the rebuttal testimony of its witness
- 25 Sandra L. Murrey.
- 26 44. On September 15, 2011, Phoenix filed a Notice of Appearance of Co-Counsel.
- 27 45. On October 11, 2011, Staff filed the surrebuttal testimony of its witness Gerald W.
- 28 Becker.

- 1 46. On October 11, 2011, RUCO filed the surrebuttal testimony of its witness William A.
2 Rigsby.
- 3 47. On October 11, 2011, Corte Bella filed the surrebuttal testimony of its witness Robert
4 Rials.
- 5 48. On October 11, 2011, Anthem filed the surrebuttal testimony of its witness Dan L.
6 Neidlinger.
- 7 49. On October 11, 2011, Phoenix filed the surrebuttal testimony of its witnesses Allen
8 Eneboe, Andy Terrey and Denise Olson.
- 9 50. On October 12, 2011, Frederick Botha filed his testimony.
- 10 51. On October 17, 2011, a public comment meeting on the Compliance Application was
11 held at the Commission's offices before a duly authorized Administrative Law Judge of the
12 Commission. Appearances were entered through counsel for the Company, Anthem, Corte Bella,
13 Verrado, DMB, RUCO and Staff. Numerous members of the public provided their comments, both
14 in favor of and in opposition to deconsolidation.
- 15 52. On October 18, 2011, Phoenix filed an additional copy of Exhibit A to the surrebuttal
16 testimony of its witness Denise Olsen.
- 17 53. On October 20, 2011, Anthem filed a Motion to Exclude Issue from Hearing.
- 18 54. On October 25, 2011, Verrado filed a Joinder in Anthem's Motion to Exclude Issue
19 from Hearing.
- 20 55. On October 31, 2011, the Company filed copies of its Wheeled Water Rate tariffs
21 approved in Decision No. 72047.
- 22 56. On November 1, 2011, the Company filed the rejoinder testimony of its witness
23 Sandra L. Murrey.
- 24 57. On November 3, 2011, Phoenix filed its Response to Motion to Exclude Issue from
25 Hearing.
- 26 58. On November 4, 2011, Anthem Golf and Country Club filed a Request to Excuse
27 Appearance of Witness.
- 28 59. On November 7, 2011, Russell Ranch filed a Notice of Substitution. Attached to the

1 filing was a copy of a Board Resolution authorizing its newly elected President, George Turner, to
2 appear on behalf of Russell Ranch before the Commission in this proceeding.

3 60. The prehearing conference convened as scheduled on November 7, 2011, before a
4 duly authorized Administrative Law Judge of the Commission. Appearances were entered through
5 counsel for the Company, Anthem, Anthem Golf and Country Club, Corte Bella, Verrado, DMB,
6 Phoenix, RUCO and Staff. Russell Ranch appeared through its representative Mr. George Turner.

7 61. At the November 7, 2011 prehearing conference, the Motion filed by Anthem Golf
8 and Country Club to excuse its witness from appearing at the hearing was granted. Numerous
9 members of the public provided their comments, both in favor of and in opposition to
10 deconsolidation.

11 62. At the November 7, 2011 prehearing conference, Anthem's Motion to Exclude Issue
12 from Hearing was discussed. The Motion was denied, with the caveats that this proceeding would
13 not be a rehearing of Decision No. 72047, that the overall revenue requirement determined in
14 Decision No. 72047 will not change in this proceeding, and that the issues in this proceeding are
15 limited to the schedules filed in the Compliance Application. With those caveats, it was ruled that
16 Phoenix would be allowed to participate in the hearing and present factual evidence and legal
17 argument to support its position in regard to the schedules filed by the Company in the Compliance
18 Application. Phoenix was reminded, and recognized on the record, that the Commission had not
19 granted its request to reopen Decision No. 72047, and that if it wished to pursue its request as stated
20 in its intervention request to reopen Decision No. 72047, that it would need to pursue that request
21 separately, and not in this proceeding.

22 63. On November 8, 2011, the Company filed a Notice of Filing Testimony Summaries.

23 64. On November 8, 2011, RUCO, filed a Notice of Filing Testimony Summaries.

24 65. On November 9, 2011, Frederick Botha filed a letter in the docket indicating that his
25 testimony needed to be postponed to a later hearing,

26 66. On November 9, 2011, Verrado and DMB filed Witness Testimony Summaries.

27 67. On November 9, 2011, Russell Ranch filed its Testimony Summary.

28 68. On November 10, 2011, Staff filed its Witness Summary.

1 69. On November 10, 2011, Corte Bella filed its Witness Testimony Summary.

2 70. On November 10, 2011, Anthem filed its Summaries of Witness Testimony.

3 71. On November 10, 2011, Phoenix filed a Notice of filing Witness Summary.

4 72. On November 14, 2011, RUCO filed a Notice of Errata.

5 73. On November 14, 2011, Frederick Botha refiled his November 9, 2011 filing.

6 74. On November 14, 2011, the hearing on the Compliance Application convened as
7 scheduled before a duly authorized Administrative Law Judge of the Commission. Appearances
8 were entered through counsel for the Company, Anthem, Corte Bella, Verrado, DMB, Phoenix,
9 RUCO and Staff. Russell Ranch appeared through its representative Mr. George Turner. The parties
10 presented evidence through witnesses and were provided an opportunity to cross-examine witnesses.
11 At the close of the evidentiary hearing, the parties agreed to a post-hearing briefing schedule.

12 75. On January 17, 2012, the Company, Anthem, Verrado, DMB, Corte Bella, Phoenix,
13 RUCO and Staff filed Initial Post-Hearing Briefs.

14 76. On January 18, 2012, Russell Ranch filed its Initial Post-Hearing Brief.

15 77. On February 7, 2012, the Company, Anthem, Corte Bella, Verrado, and Phoenix filed
16 Post-Hearing Reply Briefs, and this matter was taken under advisement.

17 78. Written public comments on the issue of deconsolidation of the Anthem-Agua Fria
18 Wastewater district have been filed by approximately 1,180 members of the public. Approximately
19 594 of those comments are in favor of deconsolidation, and approximately 586 of those comments
20 are opposed to deconsolidation.

21 79. The evidence at the hearing on the Compliance Application brought to light the fact
22 that there are four, and not just two, non-contiguous service areas in the Anthem-Agua Fria
23 Wastewater district, and that one of the Agua Fria service areas shares the Northwest Valley Plant
24 infrastructure with the Sun City West Wastewater district. Based on the evidence presented, we find
25 that deconsolidation of the Anthem-Agua Fria Wastewater district as proposed in the Compliance
26 Application would not correctly assign cost responsibility for all ratemaking components, and is
27 therefore not in the public interest at this time.

28 80. In order to address the issue of deconsolidation/consolidation in the most expeditious

1 and fair manner possible, we will require the Company to make the system-wide rate filing as ordered
2 by Decision No. 72047 that includes all of the affected districts, including the Sun City West
3 Wastewater district, as soon as possible, so that all affected parties will receive notice of, and will
4 have a full opportunity to address, all the issues affecting the Company's revenue requirement, and
5 can make proposals either for or against consolidation or deconsolidation for Commission
6 consideration.

7 81. The required system-wide rate filing should include full cost of service studies and
8 other information supporting consolidation sufficient for all parties to make their own reasoned
9 proposals either for or against consolidation or deconsolidation, consistent with sound ratemaking
10 principles.

11 82. In the required system-wide rate filing, the Company can address the issues Phoenix
12 raised in this proceeding regarding the OWU tariffed rate applicable to wastewater treatment services
13 provided to Phoenix under their agreement.

14 CONCLUSIONS OF LAW

15 1. The Company is a public service corporation pursuant to Article XV of the Arizona
16 Constitution and A.R.S. §§ 40-250 and 40-251.

17 2. The Commission has jurisdiction over The Company and the subject matter of the
18 application.

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

20 4. Based on the evidence in this proceeding, we find that deconsolidation of the
21 Anthem-Agua Fria Wastewater district as proposed in the Compliance Application is in the public
22 interest.


23 5. It is reasonable and in the public interest to require the Company to make the system-
24 wide rate filing as ordered by Decision No. 72047 that includes all of the affected districts, including
25 the Sun City West Wastewater district, as soon as possible, so that all affected parties will receive
26 notice of, and will have a full opportunity to address, all the issues affecting the Company's revenue
27 requirement, and can make proposals either for or against consolidation or deconsolidation for
28 Commission consideration.

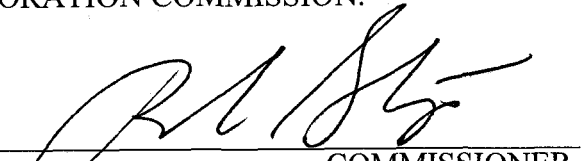
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IT IS FURTHER ORDERED that EPCOR Water (USA), shall, in the above-ordered system-wide rate filing, address the issues the City of Phoenix raised in this proceeding regarding the OWU tariffed rate applicable to wastewater treatment services provided to the City of Phoenix under their agreement.


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

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

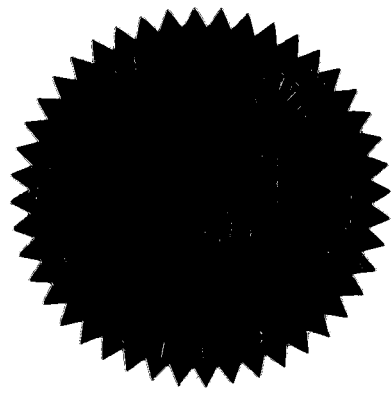

CHAIRMAN


COMMISSIONER

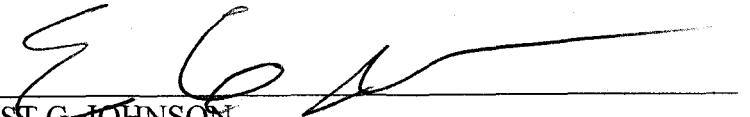
COMMISSIONER

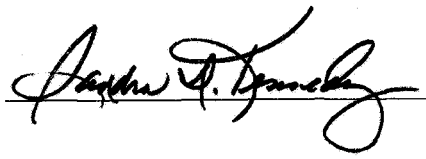

COMMISSIONER


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 5th day of June 2012.


ERNEST G. JOHNSON
EXECUTIVE DIRECTOR

DISSENT 

DISSENT 

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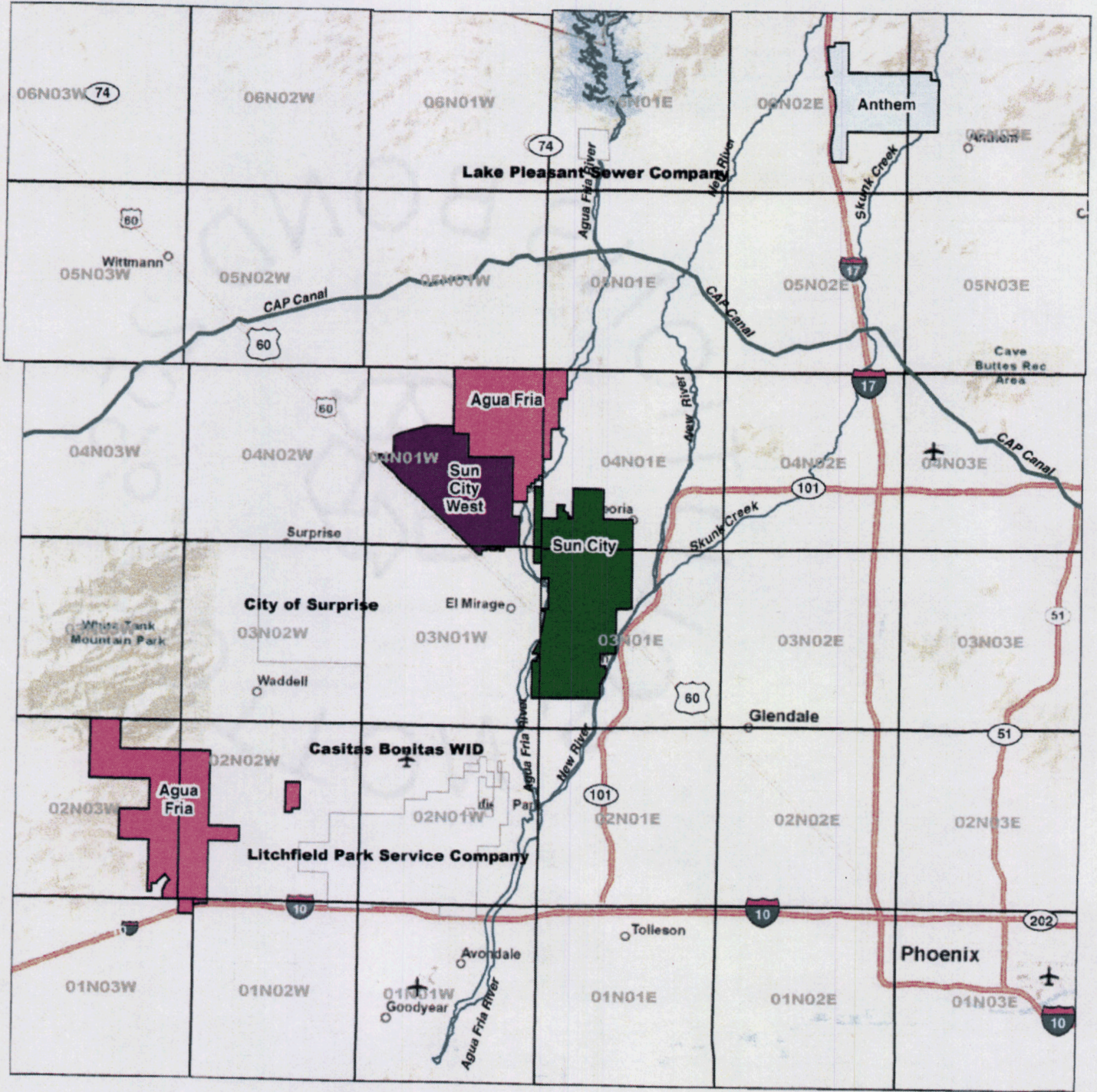
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EXHIBIT A



Maricopa County

Arizona American Water Company (Sewer)

Maricopa County

Arizona American Water Company (Water)

