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OPEN MEETING AGENDA ITEM



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BEFORE THE ARIZONA CORPORATION COMMISSION

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2012 JUL 17 A 10: 38

Arizona Corporation Commission

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AZ CORP COMMISSION
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JUL 17 2012

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IN THE MATTER OF THE COMMISSION'S
GENERIC EVALUATION OF THE
REGULATORY IMPACT FROM THE USE OF
ARRANGEMENTS BY WATER UTILITIES
AND THEIR AFFILIATES NON-TRADITIONAL
FINANCING

DOCKET NO. W-00000C-06-0149

**Comments of Sunrise Water Co. in
Support of Chairman Pierce's
Proposed Policy Statement Concerning
Income Tax Recovery**

1 Sunrise Water Co. ("Sunrise") supports Chairman Pierce's Proposed Policy Statement on
2 Income Tax Expense for Tax Pass-Through Entities.

3 Sunrise's interest is not just academic. In its 2008 rate case (Docket No. W-02069A-08-
4 0406) Sunrise was one of the first water utilities to bring to the Commission's attention how its
5 income-tax recovery policy discriminated against small water utilities. The Commission allowed
6 large pass-through entities such as Arizona Public Service Company, Tucson Electric Power
7 Company, and Southwest Gas Corporation, to recover income tax expenses but did not allow
8 small pass-through water companies to recover such expenses. Then, on December 23, 2009, in
9 Decision No. 71445, the Commission set rates that denied Sunrise's recovery of any income tax
10 expense.

11 Three years ago, in its brief in Docket No. W-02069A-08-0406, Sunrise argued as
12 follows (in part):

13 Sunrise agrees with the policy behind the New Mexico Supreme Court case cited
14 by Mr. Jones – technical distinctions are not sufficient grounds to reject Sunrise's request
15 for income tax expense.¹ Since the Arizona commission uses hypothetical income tax
16 calculations when determining the amount of income tax to include in the expenses of
17 consolidated C-Corps, it has effectively agreed with the New Mexico Supreme Court's

¹ *Moyston v. New Mexico Public Service Commission*, 76 N.M. 146, 160; 412 P.2d 840, 850 (1966).

1 statement “that the fundamental inquiry is not limited to technical distinctions, but is
2 determined by practical economic facts.” Sunrise simply requests that it not be
3 discriminated against relative to the numerous C-Corps that are part of consolidated
4 groups receiving income tax recovery in Arizona. The *practical economic fact* is that the
5 regulated activities of both S-Corps and C-Corps generate income-tax liabilities that must
6 be paid by the ultimate shareholder(s).

7 The net income generated by Sunrise through the provision of regulated water
8 services is subject to State and Federal income tax. The passed-through tax liability
9 would not exist absent the provision of regulated water services by Sunrise. Using the
10 words of the Texas Supreme Court, the taxes paid by Mr. Campbell on the income of
11 Sunrise are “inescapable business outlays and are directly comparable with similar
12 corporate taxes.”² Like any other expense prudently incurred in the operation of a
13 regulated entity, the income-tax expense should be recovered in rates of the regulated
14 entity, unless circumstances particular to the regulated entity warrant a disallowance of
15 the income tax expense.³

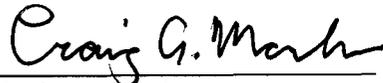
16 Three years have passed since Sunrise first briefed the issue of whether income-tax
17 expenses should be consistently recovered by all pass-through entities. Sunrise has closely
18 followed the arguments raised by the various parties in subsequent rate cases and workshops.
19 Sunrise is now even more convinced that its position is correct. The fundamental point is that it
20 is discriminatory to allow pass-through entities such as APS, SW Gas, and TEP to recover
21 income tax-expenses in rates, but not to allow small water pass-through entities such as Sunrise
22 Water to recover income tax expenses.

23 Chairman Pierce’s proposed policy statement properly resolves the issue. Sunrise urges
24 the Commission to approve Chairman Pierce’s proposed policy statement.

² *Suburban Utility Corp. v. Public Utility Com'n of Texas*, 652 S.W.2d 358, 364 (Tex. 1983).

³ Sunrise Brief dated July 23, 2009, at pp. 13-14.

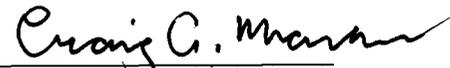
1 RESPECTFULLY SUBMITTED on July 17, 2012.
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