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BEFORE THE ARIZONA CORPORATION COMMISSION

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Arizona Corporation Commission

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AZ CORP COMMISSION
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IN THE MATTER OF THE APPLICATION OF
LAGO DEL ORO WATER COMPANY, AN
ARIZONA CORPORATION, FOR A
DETERMINATION OF THE FAIR VALUE OF ITS
UTILITY PLANT AND PROPERTY AND FOR
INCREASES IN ITS WATER RATES AND
CHARGES FOR UTILITY SERVICE BASED
THEREON.

DOCKET NO. W-01944A-13-0215

**STAFF'S NOTICE OF FILING
SURREBUTTAL TESTIMONY**

The Utilities Division ("Staff") of the Arizona Corporation Commission ("Commission") hereby files the Surrebuttal Testimony of Staff witnesses Mary J. Rimback, John A. Cassidy and Michael Thompson in the above-captioned matter.

RESPECTFULLY SUBMITTED this 7th day of March, 2014.

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ORIGINAL

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BEFORE THE ARIZONA CORPORATION COMMISSION

BOB STUMP
Chairman
GARY PIERCE
Commissioner
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BOB BURNS
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IN THE MATTER OF THE APPLICATION OF) DOCKET NO W-01944A-13-0215
LAGO DEL ORO WATER COMPANY, AN)
ARIZONA CORPORATION FOR A)
DETERMINATION OF THE)
FAIR VALUE OF ITS UTILITY PLANT AND)
PROPERTY AND FOR INCREASES IN ITS)
WATER RATES AND CHARGES FOR UTILITY)
SERVICE BASED THEREON)
_____)

SURREBUTTAL
TESTIMONY
OF
MARY J. RIMBACK
PUBLIC UTILITIES ANALYST
UTILITIES DIVISION
ARIZONA CORPORATION COMMISSION

MARCH 7, 2014

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EXECUTIVE SUMMARY
LAGO DEL ORO WATER COMPANY
DOCKET NO. W-01944A-13-0215

The surrebuttal testimony of Staff witness Mary J. Rimback addresses the issues of rate base, operating income, revenue requirement and rate design for Lago Del Oro Water Company ("LDO" or "Company").

The Company's rebuttal testimony requests an increase in revenue of \$1,148,253 (61.00 percent) over test year revenue of \$1,882,238. The total annual revenue of \$3,030,491 produces operating income of \$647,208 to provide an 8.79 percent rate of return ("ROR") on a proposed \$7,363,846 fair value rate base ("FVRB") which is also the proposed original cost rate base ("OCRB").

The Utilities Division ("Staff") recommends an increase in revenue of \$1,029,215 (54.68 percent) over test year revenue of \$1,882,238. The total annual revenue of \$2,911,453 produces operating income of \$604,049 to provide an 8.20 percent ROR on the Staff adjusted OCRB of \$7,366,456.

1 **I. INTRODUCTION**

2 **Q. Please state your name, occupation, and business address.**

3 A. My name is Mary J. Rimback. I am a Public Utilities Analyst with the Arizona
4 Corporation Commission (“ACC” or “Commission”) in the Utilities Division (“Staff”).
5 My business address is 1200 West Washington Street, Phoenix, Arizona 85007.

6

7 **Q. Are you the same Mary J. Rimback who previously submitted direct testimony in**
8 **this case?**

9 A. Yes, I am.

10

11 **Q. How is your testimony organized?**

12 A. My testimony is presented in four Sections. Section I is this introduction. Section II
13 provides the purpose of the testimony. Section III is a summary of recommendations.
14 Section IV presents Staff’s response to the rebuttal testimony of Mr. Thomas J. Bourassa
15 (“Bourassa Rebuttal”).

16

17 **II. PURPOSE OF THE SURREBUTTAL TESTIMONY**

18 **Q. What is the purpose of your surrebuttal testimony in this proceeding?**

19 A. The purpose of my surrebuttal testimony in this proceeding is to respond, on behalf of
20 Staff, to the rebuttal testimony of Mr. Thomas J. Bourassa and to present Staff’s
21 surrebuttal position regarding rate base, operating income, revenue requirement and rate
22 design issues.

1 **Q. Do you attempt to address every issue raised by the Company in its rebuttal**
2 **testimony?**

3 A. No. My silence on any particular issue raised in the Company's rebuttal testimony does
4 not indicate that Staff agrees with the Company's rebuttal position on that issue. I rely on
5 my direct testimony unless modified by this surrebuttal testimony.

6
7 **Q. What issues will you address?**

8 A. My surrebuttal addresses the following issues.

- 9 1) Plant-in-Service ("PIS") and Accumulated Depreciation on Plant Purchased from
10 Affiliate
11 2) Fully Depreciated Plant
12 3) Contributions-in Aid of Construction ("CIAC")
13 4) Accumulated Deferred Income Taxes
14 5) Contractual Services Water Testing
15 6) Contractual Services annual audit costs
16 7) Rate Design
17

18 **III. SUMMARY OF RECOMMENDATIONS**

19 **Q. What rebuttal revenue requirement is LDO proposing?**

20 A. The Company's rebuttal testimony requests total operating revenue of \$3,030,491 a
21 \$1,148,253 (61.00 percent) increase over the test year revenue of \$1,882,238. This
22 provides a \$647,208 operating income and an 8.79 percent ROR on a proposed \$7,363,846
23 fair value rate base ("FVRB") which is also the proposed original cost rate base
24 ("OCRB").

1 **Q. Please summarize Staff's recommended revenue requirement.**

2 A. Staff recommends total operating revenue of \$2,911,453, a \$1,029,215 (54.68 percent)
3 increase over the test year revenue of \$1,882,238. This provides a \$604,049 operating
4 income and an 8.20 percent ROR on an OCRB of \$7,366,456. (In Staff's direct
5 testimony, Staff recommended total operating revenue of \$2,829,778, a \$947,540 or 50.34
6 percent increase over the test year revenue of \$1,882,238 to provide a \$580,094 operating
7 income and a 7.9 percent ROR on an OCRB of \$7,342,962.)
8

9 **Q. Has the ROR used to develop the revenue requirement in Staff's surrebuttal**
10 **testimony changed from the ROR in Staff's direct testimony?**

11 A. Yes. Staff's recommended ROR is increased from the 7.90 percent reflected in my direct
12 testimony filed on January 17, 2014, to 8.20 percent in this filing. The ROR change is
13 supported by Staff witness Mr. John Cassidy.
14

15 **IV. RESPONSE TO REBUTTAL TESTIMONY OF MR. THOMAS J. BOURASSA**
16

17 *Plant-in-Service ("PIS") and accumulated depreciation of plant purchased from affiliate*

18 **Q. Is the Company disputing the Staff adjustment to the value of PIS included for**
19 **ratemaking purposes?**

20 A. Yes. The Company cites in its rebuttal testimony the National Association of Regulatory
21 Commissioners Uniform System of Accounts ("NARUC USOA") Accounting Instruction
22 No. 21, subsection B(1) which requires purchased plant to be recorded at its original cost
23 and subsection B(2) which requires that accumulated depreciation associated with the
24 original cost be recorded for utility plant, purchased or sold.

1 **Q. Did the Company, in its original application follow instruction No. 21?**

2 A. No, the Company valued the assets at original cost but recognized depreciation as if the
3 assets were placed in service at the beginning of 2012. The assets were actually placed in
4 service over a period beginning in 1997 and continuing on through 2009. The
5 depreciation recognized by the Company did not reflect the reduction in useful life of the
6 assets.

7
8 **Q. What was the value placed on this purchased plant in the Company's original
9 application?**

10 A. The Company valued the transaction at the original cost of the underlying asset without
11 regard to the reduction in useful life of the assets that has occurred since this plant was
12 first placed into service. The original cost was \$3,887,998. This value was utilized in
13 both the rate application and the related financing application.

14
15 **Q. Did Staff effectively adjust this \$3,887,998 downward, recognizing the loss in
16 economic value associated with accumulated depreciation?**

17 A. Yes, Staff originally valued these assets at \$2,751,411. This was the remaining economic
18 value of these assets at the point in time when they were transferred to LDO.

19
20 **Q. Did the Company accept Staff's valuation of plant transferred in the financing
21 docket?**

22 A. Yes, the Company has agreed to Staff's recommendation that the financing be limited to
23 the remaining economic value of these assets or \$2,751,411.

1 **Q. Has the value of plant to be recognized for purposes of the rate application been in**
2 **dispute by the Company?**

3 A. Yes. The Company has argued that these assets should be recorded in a manner that
4 makes clear both the original cost and accumulated depreciation from the point the assets
5 were first devoted to utility service. Effectively this would be accomplished by recording
6 the assets at the original \$3,887,998 value and also recognize an accumulated depreciation
7 reserve on these assets of \$1,233,787. The Company has made a compelling argument,
8 since it is important to acknowledge that these assets have been providing utility service
9 for a number of years.

10
11 **Q. Does Staff now agree with the position advocated by LDO?**

12 A. Yes, Staff recommends recognition of the original cost of the assets of \$3,887,998 and
13 also recognition of an additional accumulated depreciation reserve of \$1,136,587. The net
14 of these two entries is \$2,751,411.

15
16 **Q. Did the Company include an accumulated depreciation reserve adjustment of**
17 **\$97,200 in its original application?**

18 A. Yes, the Company reflected one-half year's depreciation on these assets being purchased.
19

20 **Q. What adjustment to accumulated depreciation is still needed for the assets purchased**
21 **from an affiliate?**

22 A. The required adjustment is \$1,136,587, which is the net of the \$1,233,787 discussed above
23 less the \$97,200 adjustment already in the Company's application.

1 ***Fully Depreciated Plant***

2 **Q. Do Staff and the Company dispute the amount of fully depreciated plant?**

3 A. Yes, the Company states that all fully depreciated plant has been properly included in its
4 original application. Staff continues to disagree with this Company position.

5
6 **Q. Did Staff review the Company- provided information as to additions, retirements
7 and adjustments?**

8 A. Yes.

9
10 **Q. Did Staff record retirements as stated in the Company's rebuttal testimony?¹**

11 A. No, Staff did not record retirements, Staff performed an audit analysis of the plant and
12 accumulated depreciation balances presented by the Company. Plant is considered retired
13 when it is removed from service, not when the recordkeeping reflects that it is fully
14 depreciated. Property retired is defined by both NARUC USoA and the Arizona
15 Administrative Code ("AAC"):

16 1) According to the NARUC USoA definition No. 12, "Property retired," as applied to
17 utility plant, means property which has been removed, sold, abandoned, destroyed,
18 or which for any cause has been permanently withdrawn from service.

19 2) According to the AAC R-14-2-102 Subsection A(7) "Property retired" means assets
20 which have been removed, sold, abandoned, destroyed, or which for any cause have
21 been withdrawn from service and books of account.

22
23 **Q. Did Staff adjust accumulated depreciation values and modify the Company's on-
24 going depreciation expense based on this analysis?**

25 A. Yes.

¹¹ Company Rebuttal of Thomas J. Bourassa "(Bourassa Rt." at 11

1 **Q. Please explain the basis of Staff's depreciation adjustments.**

2 A. The Company presented the application as required by the Commission, that is the plant
3 balances were traced from the last rate case, additions, retirements and adjustments were
4 shown for each of the twenty-four years since the last rate case. Staff analyzed the year-
5 by-year transactions and notes that once the original cost of the plant was fully expensed
6 for depreciation, some plant continued to be depreciated.

7
8 **Q. Does Staff take issue with this practice?**

9 A. Yes, as stated in AAC R14-2-102 (3) "Depreciation" means an accounting process which
10 will permit the recovery of the original cost of an asset less its net salvage over the service
11 life". As such recovering beyond the original cost of the plant in service does not comply
12 with AAC R14-2-103 (3).

13
14 **Q. Does the accumulated depreciation reserve adjustment proposed by Staff increase
15 the Company's rate base by \$371,263 as shown in Surrebuttal Schedule MJR-W6?**

16 A. Yes, continuing to depreciate PIS beyond the original cost negatively impacts rate base, so
17 reversing this depreciation reserve item increases rate base.

18
19 **Q. Does this adjustment affect any other ratemaking calculations?**

20 A. Yes, this removes fully depreciated plant from the going forward calculation of
21 depreciation expense.

1 ***Contributions in Aid of Construction (“CIAC”)***

2 **Q. Does Staff’s position with regards to vintage year depreciation impact the**
3 **Company’s CIAC balance as proposed in the Company’s rebuttal²?**

4 A. No, Staff notes that the CIAC balances in the last rate case were fully amortized by 1995.
5 Staff found that the Company provided calculations in the rate application (Schedule B-2
6 page 5.1) which continued to amortize CIAC that was completely amortized in 1995.

7
8 ***Accumulated Deferred Income Taxes (“ADIT”)***

9 **Q. Did Staff adjust the ADIT calculation based on the Company’s calculation of the**
10 **effects of not taking bonus depreciation on the entire \$3,887,000 of plant purchased**
11 **from an affiliate?**

12 A. No. Staff does not understand the rebuttal points raised by the Company regarding bonus
13 depreciation. No mention of bonus depreciation was included in the original rate
14 application. The plant purchased from an affiliate was placed in service over a period of
15 many years. If applicable, bonus depreciation would have been an issue for the affiliate in
16 the years the various assets were placed in service. These would not have resulted in
17 bonus depreciation implications only in 2012, as the Company seems to be suggesting.
18 Staff believes this rebuttal point is irrelevant and should be disregarded.

19
20 ***Contractual Services Testing for water testing costs***

21 **Q. Does Staff accept the adjustment for mandated water testing costs of \$5,940?**

22 A. Yes, this represents one-fifth of 92.0 percent of the total costs of \$32,280, allowing the
23 Company to recover the LDO portion over five years.
24

² Bourassa Rt at 14

1 ***Contractual Services Annual Audit***

2 **Q. Does Staff recommend inclusion of \$8,000 to prepare annual financial audits as a**
3 **condition of its proposed new debt?**

4 A. No. No support has been given for this \$8,000 amount, and both the amount of any
5 ultimate auditing costs and the timing regarding when any such auditing costs will be
6 incurred are not known and measurable at the present time. Further, Staff notes there are a
7 number of specific requirements included in the term sheet provided in the financing
8 application and an additional annual audit was not one of the terms of the loan.

9
10 ***Rate Design***

11 **Q. Did Staff change the rate design from its direct testimony?**

12 A. No, Staff left the fundamental rate design as in its direct testimony, adjusting for the
13 change in recommended revenues.

14
15 **Q. Did Staff include the rate design and typical bill analysis in surrebuttal schedules?**

16 A. Yes.

17
18 **Q. Does this conclude your testimony?**

19 A. Yes, it does.

REVENUE REQUIREMENT

LINE NO.	DESCRIPTION	(A) COMPANY FAIR VALUE	(B) STAFF FAIR VALUE
1	Adjusted Rate Base	\$ 8,287,733	\$ 7,366,456
2	Adjusted Operating Income (Loss)	\$ (3,470)	\$ (28,182)
3	Current Rate of Return (L2 / L1)	-0.04%	-0.38%
4	Required Rate of Return	8.65%	8.20%
5	Required Operating Income (L4 * L1)	\$ 716,971	\$ 604,049
6	Operating Income Deficiency (L5 - L2)	\$ 720,441	\$ 632,232
7	Gross Revenue Conversion Factor	1.6560	1.6279
8	Required Revenue Increase (L7 * L6)	\$ 1,193,033	\$ 1,029,215
9	Adjusted Test Year Revenue	\$ 1,882,238	\$ 1,882,238
10	Proposed Annual Revenue	\$ 3,075,271	\$ 2,911,453
11	Required Increase in Revenue (%)	63.38%	54.68%

References:

Column (A): Company Schedule A-1

Column (B): Staff Schedules MJR-W3 and MJR-W9

GROSS REVENUE CONVERSION FACTOR

LINE NO.	DESCRIPTION	(A)	(B)	(C)	(D)
<u>Calculation of Gross Revenue Conversion Factor:</u>					
1	Revenue	100.0000%			
2	Uncollectible Factor	0.0000%			
3	Revenues (L1 - L2)	100.0000%			
4	Combined Federal and State Income Tax and Property Tax Rate (Line 18)	38.5714%			
5	Subtotal (L3 - L4)	61.4286%			
6	Revenue Conversion Factor (L1 / L5)	1.627907			
<u>Calculation of Uncollectible Factor:</u>					
7	Unity	100.0000%			
8	Combined Federal and State Tax Rate (Line 17)	37.5028%			
9	One Minus Combined Income Tax Rate (L7 - L8)	62.4972%			
10	Uncollectible Rate	0.0000%			
11	Uncollectible Factor (L9 * L10)	0.0000%			
<u>Calculation of Effective Tax Rate:</u>					
12	Operating Income Before Taxes (Arizona Taxable Income)	100.0000%			
13	Arizona State Income Tax Rate	6.5000%			
14	Federal Taxable Income (L12 - L13)	93.5000%			
15	Applicable Federal Income Tax Rate (Line 48)	33.1581%			
16	Effective Federal Income Tax Rate (L9 x L10)	31.0028%			
17	Combined Federal and State Income Tax Rate (L13 + L16)		37.5028%		
<u>Calculation of Effective Property Tax Factor</u>					
18	Unity	100.0000%			
19	Combined Federal and State Income Tax Rate (L17)	37.5028%			
20	One Minus Combined Income Tax Rate (L13-L14)	62.4972%			
21	Property Tax Factor (MJR-W13, L27)	1.7099%			
22	Effective Property Tax Factor (L20*L21)		1.0686%		
23	Combined Federal and State Income Tax and Property Tax Rate (L17+L22)			38.5714%	
24	Required Operating Income (Schedule MJR-W1, Line 5)	\$ 604,049			
25	Adjusted Test Year Operating Income (Loss) (MJR-W10, L40)	(28,182)			
26	Required Increase in Operating Income (L24 - L25)		\$ 632,232		
27	Income Taxes on Recommended Revenue (Col. [C], L52)	\$ 315,382			
28	Income Taxes on Test Year Revenue (Col. [C], L52)	(64,002)			
29	Required Increase in Revenue to Provide for Income Taxes (L27 - L28)		379,384		
30	Recommended Revenue Requirement (Schedule MJR-W1, Line 10)	\$ 2,911,453			
31	Uncollectible Rate	0.0000%			
32	Uncollectible Expense on Recommended Revenue (L30*L31)	\$ -			
33	Adjusted Test Year Uncollectible Expense	\$ -			
34	Required Increase in Revenue to Provide for Uncollectible Exp. (L32-L33)				
35	Property Tax with Recommended Revenue (Schedule MJR-W18, L21)	\$ 111,267			
36	Property Tax on Test Year Revenue (Schedule MJR-W13, Line 17)	93,668			
37	Increase in Property Tax Due to Increase in Revenue (L30-31)		17,599		
38	Total Required Increase in Revenue (L21 + L24 + L29 + L32)		\$ 1,029,215		
<u>Calculation of Income Tax:</u>					
39	Revenue (Schedule MJR-W1, Col. [B], Line 9 & Sch. MJR-W1, Col. [B] Line 10)	\$ 1,882,238	\$ 1,029,215	\$ 2,911,453	
40	Operating Expenses Excluding Income Taxes	\$ 1,974,422		\$ 1,992,021	
41	Synchronized Interest (L57)	\$ 95,764		\$ 95,764	
42	Arizona Taxable Income (L34 - L35 - L36)	\$ (187,948)		\$ 823,668	
43	Arizona State Income Tax Rate	6.5000%		6.5000%	
44	Arizona Income Tax (L37 x L38)	\$ (12,217)		\$ 53,538	
45	Federal Taxable Income (L37- L39)	\$ (175,732)		\$ 770,130	
46	Federal Tax on First Income Bracket (\$1 - \$50,000) @ 15%	\$ (7,500)		\$ 7,500	
47	Federal Tax on Second Income Bracket (\$51,001 - \$75,000) @ 25%	\$ (6,250)		\$ 6,250	
48	Federal Tax on Third Income Bracket (\$75,001 - \$100,000) @ 34%	\$ (8,500)		\$ 8,500	
49	Federal Tax on Fourth Income Bracket (\$100,001 - \$335,000) @ 39%	\$ (29,535)		\$ 91,650	
50	Federal Tax on Fifth Income Bracket (\$335,001 - \$10,000,000) @ 34%	\$ -		\$ 147,944	
51	Total Federal Income Tax	\$ (51,785)		\$ 261,844	
52	Combined Federal and State Income Tax (L43 + L51)	\$ (64,002)		\$ 315,382	
53	Applicable Federal Income Tax Rate [Col. [C], L51 - Col. [A], L51] / [Col. [C], L45 - Col. [A], L45]			33.1581%	
54	Synchronized Interest Calculation				
55	Rate Base			\$ 7,366,456	
56	Weighted Average Cost of Debt			1.30%	
57	Synchronized Interest			\$ 95,764	

RATE BASE - ORIGINAL COST

LINE NO.	(A) COMPANY AS FILED	(B) STAFF ADJUSTMENTS	(C) STAFF AS ADJUSTED
1	Plant in Service	\$ 18,200,198	\$ 18,200,199
2	Less: Accumulated Depreciation	8,840,798	9,606,122
3	Net Plant in Service	<u>\$ 9,359,400</u>	<u>\$ 8,594,077</u>
<i>LESS:</i>			
4	Contributions in Aid of Construction (CIAC)	\$ 852,693	\$ 753,535
5	Less: Accumulated Amortization	469,879	282,997
6	Net CIAC	<u>\$ 382,814</u>	<u>\$ 470,538</u>
7	Advances in Aid of Construction (AIAC)	297,640	297,640
8	Customer Deposits	111,854	111,854
9	Accumulated Deferred Income Tax	279,359	347,588
<i>ADD:</i>			
10	Working Capital Allowance	-	-
11	Deferred Regulatory Assets	-	-
12	Original Cost Rate Base	<u>\$ 8,287,733</u>	<u>\$ 7,366,456</u>

References:

Column [A]: Company Application Schedule B-1
Column [B]: Testimony MJR
Column [C]: Column [A] + Column [B]

SUMMARY OF ORIGINAL COST RATE BASE ADJUSTMENTS

LINE NO.	ACCT. NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] ADJ.#1 2012 Affiliate Purchase Ref. Sch MJR-WS	[C] ADJ.#2 Accum Deprec Fully Deprec Plant Ref. Sch MJR-W6	[D] ADJ.#3 CIAC and Accum Amort of CIAC Ref. Sch MJR-W7	[E] ADJ.#4 ADIT Accum Def Inc Txs Ref. Sch MJR-W8	[F] STAFF ADJUSTED
1	301.0	Organization Cost						
2	302.0	Franchise Cost						
3	303.0	Land and Land Rights	42,608					42,608
4	304.0	Structures and Improvements	359,681					359,681
5	305.0	Collecting and Impounding Res.						
6	306.0	Lake River and Other Intakes		0				0
7	307.0	Wells and Springs	2,164,423					2,164,423
8	308.0	Infiltration Galleries and Tunnels						
9	309.0	Supply Mains						
10	310.0	Power Generation Equipment	187,864					187,864
11	311.0	Electric Pumping Equipment	3,585,660					3,585,660
12	320.0	Water Treatment Equipment						
13	320.2	Chemical Solution Feeders	24,640					24,640
14	330.0	Distribution Reservoirs & Standpipe						
15	330.1	Storage Tanks	1,758,175					1,758,175
16	330.2	Pressure Tanks	321,969					321,969
17	331.0	Transmission and Distribution Mains	6,083,805					6,083,805
18	333.0	Services	1,888,741					1,888,741
19	334.0	Meters	504,321					504,321
20	335.0	Hydrants	718,857					718,857
21	336.0	Backflow Prevention Devices						
22	339.0	Other Plant and Miscellaneous Equipment						
23	340.0	Office Furniture and Fixtures	36,758					36,758
24	340.1	Computers and Software						
25	341.0	Transportation Equipment	89,569					89,569
26	342.0	Stores Equipment						
27	343.0	Tools and Work Equipment						
28	344.0	Laboratory Equipment						
29	345.0	Power Operated Equipment	55,787					55,787
30	346.0	Communications Equipment	351,219					351,219
31	347.0	Miscellaneous Equipment	26,122					26,122
32	348.0	Other Tangible Plant						
33		Total Plant in Service - Actual	\$ 18,200,198					\$ 18,200,199
34		Post Test-Year Plant						
35		Total Plant in Service	\$ 18,200,198	0				\$ 18,200,199
36		Less: Accumulated Depreciation	8,940,798	1,136,587	(371,263)			9,606,122
37		Net Plant in Service	\$ 9,359,400	(1,136,587)	371,263			\$ 8,594,077
38		LESS:						
39		Contributions in Aid of Construction (CIAC)	\$ 852,693					753,535
40		Less: Accumulated Amortization	469,879			(99,158)		282,997
41		Net CIAC (L42 - L43)	\$ 382,814			(87,724)		470,538
42		Advances in Aid of Construction (AIAC)	297,640					297,640
43		Customer Meter Deposits	111,854					111,854
44		Deferred Income Tax	279,359				68,229	347,588
45		Working Capital Allowance						
46		Deferred Regulatory Assets						
47		Original Cost Rate Base	\$ 8,287,733	(1,136,587)	371,263	(87,724)	(68,229)	\$ 7,366,456

RATE BASE ADJUSTMENT NO. 1 - Staff adjusted value of plant purchased from affiliated company

LINE NO.	DESCRIPTION	[A]	[B]	[C]
		STAFF AS ADJ NO. 1	STAFF ADJUSTMENTS	STAFF AS ADJUSTED
1	304 Structures and Improvements	\$ 110,051	\$ -	\$ 110,051
2	307 Wells and Springs	496,541	-	496,541
3	310 Power Generation Equipment	62,481	-	62,481
4	311 Electric Pumping Equipment	547,976	-	547,976
5	330.1 Storage Tanks	323,184	-	323,184
6	330.2 Pressure Tanks	89,247	-	89,247
7	331 Transmission and Distribution Mains	1,774,780	-	1,774,780
8	333 Services	270,250	-	270,250
9	335 Hydrants	189,964	-	189,964
10	346 Communications Equipment	23,525	-	23,525
11				
12	Subtotal	<u>\$ 3,887,998</u>	<u>\$ -</u>	<u>\$ 3,887,998</u>
13				
14	Accumulated Depreciation	\$ 97,200	\$ 1,136,587	\$ 1,233,787

References:

Column [A]: Company Schedule B-2, Page 3.29
Column [B]: Testimony MJR
Column [C]: Column [A] + Column [B]

RATE BASE ADJUSTMENT NO. 1 - Accumulated depreciation - fully depreciated plant

LINE NO.	DESCRIPTION	[A]	[B]	[C]
		COMPANY AS FILED	STAFF ADJUSTMENTS	STAFF AS ADJUSTED
1	Accumulated Depreciation	\$ 8,840,798	\$ (371,263)	\$ 8,469,535

References:

Column [A]: Company Schedule B-2, Page 3.29

Column [B]: Testimony MJR

Column [C]: Column [A] + Column [B]

RATE BASE ADJUSTMENT NO. 3 - CIAC and accumulated amortization of CIAC

LINE NO.	DESCRIPTION	[A]	[B]	[C]
		COMPANY AS FILED	STAFF ADJUSTMENTS	STAFF AS ADJUSTED
1	CIAC	\$ 852,693	\$ (99,158)	\$ 753,535
2	AMORTIZATION OF CIAC	469,879	(186,882)	282,997
3	NET CIAC	<u>\$ 382,814</u>	<u>\$ 87,724</u>	<u>\$ 470,538</u>

References:

Columns [A]: Company Schedule B-2, Page 5.1 thru 5.3

Column [B]: Column [C] less Column [A]

Column [C]: Testimony MJR

RATE BASE ADJUSTMENT NO. 4 - Adit adjustment

LINE NO.	DESCRIPTION	[A]	[B]	[C]
		COMPANY AS FILED	STAFF ADJUSTMENTS	STAFF AS ADJUSTED
1	ADIT	\$ 279,359	\$ 68,229	\$ 347,588

References:

Column [A]: Company Schedule B.1, Page 1

Column [B]: Column [C] less Column [A]

Column [C]: Column [A] + Column [B]

OPERATING INCOME STATEMENT - ADJUSTED TEST YEAR AND STAFF RECOMMENDED

LINE NO.	DESCRIPTION	[A] COMPANY ADJUSTED TEST YEAR AS FILED	[B] STAFF TEST YEAR ADJUSTMENTS	[C] STAFF TEST YEAR AS ADJUSTED	[D] STAFF PROPOSED CHANGES	[E] STAFF RECOMMENDED
1	<u>REVENUES:</u>					
2	Metered Water Sales	\$ 1,865,121	\$ -	\$ 1,865,121	\$ 1,029,215	\$ 2,894,336
3	Water Sales-Unmetered	-	-	-	-	-
4	Other Water Revenue	17,117	-	17,117	-	17,117
5	Intentionally Left Blank	-	-	-	-	-
6	Total Operating Revenues	\$ 1,882,238	\$ -	\$ 1,882,238	\$ 1,029,215	\$ 2,911,453
7				##		
8	<u>OPERATING EXPENSES:</u>					
9	Salaries and Wages	\$ 169,991	\$ -	\$ 169,991	\$ -	\$ 169,991
10	Employee Benefits and Pensions	35,228	-	35,228	-	35,228
11	Purchased Water	-	-	-	-	-
12	Purchased Power	442,823	-	442,823	-	442,823
13	Fuel for Power Production	-	-	-	-	-
14	Chemicals	21,969	-	21,969	-	21,969
15	Materials and Supplies	80,299	-	80,299	-	80,299
16	Office Supplies and Expense	66,431	-	66,431	-	66,431
17	Contractual Services-Engineering	-	-	-	-	-
18	Contractual Services -Accounting	533	-	533	-	533
19	Contractual Services- Legal	166	-	166	-	166
20	Contractual Services-Other	57,785	-	57,785	-	57,785
21	Contractual Services-Testing	22,433	5,392	27,825	-	27,825
22	Rents	9,435	-	9,435	-	9,435
23	Rents-Equipment	-	-	-	-	-
24	Transportation Expenses	42,440	-	42,440	-	42,440
25	Insurance - Vehicle	5,165	-	5,165	-	5,165
26	Insurance - General Liability	20,083	-	20,083	-	20,083
27	Regulatory Commission Expense-Other	855	-	855	-	855
28	Regulatory Commission Expense - Rate Case	55,000	-	55,000	-	55,000
29	Bad Debt Expense	4,922	-	4,922	-	4,922
30	Miscellaneous Expense	19,274	-	19,274	-	19,274
31	Depreciation and Amortization Expense	861,127	(40,597)	820,530	-	820,530
33	Taxes Other than Income	-	-	-	-	-
34	Property Taxes	98,597	(4,929)	93,668	17,599	111,267
35	Income Taxes	(128,849)	64,847	(64,002)	379,384	315,382
36	Interest on Customer Deposits	-	-	-	-	-
37	Total Operating Expenses	\$ 1,885,708	\$ 24,713	\$ 1,910,420	\$ 396,983	\$ 2,307,403
38	Operating Income (Loss)	\$ (3,470)	\$ (24,713)	\$ (28,182)	\$ 632,232	\$ 604,049
39						
40	Other Income(Expense)					
	Interest Income	\$ -	\$ -	\$ -	-	-
	Other Income(Expense)	-	-	-	-	-
	Interest Expense	(204,322)	108,558	(95,764)	-	(95,764)
	Other Expense	-	-	-	-	-
	Total Other Income (Expense)	\$ (204,322)	\$ 108,558	\$ (95,764)	\$ -	\$ (95,764)
	Net Profit (Loss)	\$ (207,792)	\$ 83,845	\$ (123,946)	\$ 632,232	\$ 508,285

References:

- Column (A): Company Schedule C-1
- Column (B): Schedule MJR-W10
- Column (C): Column (A) + Column (B)
- Column (D): Schedules MJR-W1, MJR-W2 and MJR-W13
- Column (E): Column (C) + Column (D)

SUMMARY OF OPERATING INCOME STATEMENT ADJUSTMENTS - TEST YEAR

LINE NO.	DESCRIPTION	[A] COMPANY AS FILED	[B] Water Testing Expenses ADJ #1 Ref: Sch MJR-W11	[C] Depreciation Expense ADJ #2 Ref: Sch MJR-W12	[D] Property Tax Expense ADJ #3 Ref: Sch MJR-W13	[E] Income Tax Expense ADJ #4 Ref: Sch MJR-W14	[F] STAFF ADJUSTED
1	REVENUES:						
2	Metered Water Sales	\$ 1,865,121	-	-	-	-	1,865,121
3	Water Sales-Unmetered	-	-	-	-	-	-
4	Other Water Revenue	17,117	-	-	-	-	17,117
5	Intentionally Left Blank	-	-	-	-	-	-
6	Total Operating Revenues	\$ 1,882,238	\$ -	\$ -	\$ -	\$ -	\$ 1,882,238
7							
8	OPERATING EXPENSES:						
9	Salaries and Wages	\$ 169,991	0	-	-	-	169,991
	Employee Benefits and Pensions	\$ 35,228	-	-	-	-	35,228
10	Purchased Water	-	-	-	-	-	-
11	Purchased Power	442,823	-	-	-	-	442,823
12	Fuel for Power Production	-	-	-	-	-	-
13	Chemicals	21,969	-	-	-	-	21,969
14	Materials and Supplies	80,299	-	-	-	-	80,299
15	Office Supplies and Expense	66,431	-	-	-	-	66,431
16	Contractual Services-Engineering	-	-	-	-	-	-
17	Contractual Services-Accounting	533	-	-	-	-	533
18	Contractual Services-Legal	166	-	-	-	-	166
19	Contractual Services-Other	57,785	-	-	-	-	57,785
20	Contractual Services-Testing	22,433	5,392	-	-	-	27,825
24	Rents	9,435	-	-	-	-	9,435
25	Rents-Equipment	-	-	-	-	-	-
26	Transportation Expenses	42,440	-	-	-	-	42,440
27	Insurance - Vehicle	5,165	-	-	-	-	5,165
28	Insurance - General Liability	20,083	-	-	-	-	20,083
29	Regulatory Commission Expense-Other	855	-	-	-	-	855
30	Regulatory Commission Expense - Rate Case	55,000	-	-	-	-	55,000
31	Bad Debt Expense	4,922	-	-	-	-	4,922
32	Miscellaneous Expense	19,274	-	-	-	-	19,274
33	Depreciation and Amortization Expense	861,127	-	(40,597)	-	-	820,530
35	Taxes Other than Income	-	-	-	(4,929)	-	-
36	Property Taxes	98,597	-	-	-	64,847	93,668
37	Income Taxes	(128,849)	-	-	-	-	(64,002)
38	Interest on Customer Deposits	-	-	-	-	-	-
39	Total Operating Expenses	\$ 1,885,708	\$ (5,392)	\$ (40,597)	\$ (4,929)	\$ 64,847	\$ 1,910,420
40	Operating Income (Loss)	\$ (3,470)	\$ (5,392)	\$ 40,597	\$ 4,929	\$ (64,847)	\$ (28,182)
	Other Income(Expense)						
	Interest Income	\$ -	-	-	-	-	-
	Other Income(Expense)	(204,322)	-	-	-	-	(95,764)
	Interest Expense	-	-	-	-	-	-
	Other Expense	-	-	-	-	-	-
	Total Other Income (Expense)	\$ (204,322)	\$ -	\$ -	\$ -	\$ -	\$ (95,764)
	Net Profit (Loss)	\$ (207,792)	\$ (5,392)	\$ 40,597	\$ 4,929	\$ (64,847)	\$ (123,946)

OPERATING ADJUSTMENT NO. 1 - Water testing expense

Line No.	Description	[A]	[B]	[C]
		COMPANY PROPOSED	STAFF ADJUSTMENTS	STAFF RECOMMENDED
1	Contractual Services-Testing	\$ 22,433	\$ (548)	\$ 21,885
2	UCMR 3	\$ -	\$ 5,940	\$ 5,940
3		<u>\$ 22,433</u>	<u>\$ 5,392</u>	<u>\$ 27,825</u>

¹ Unregulated Contaminant Monitoring Rules

References:

Column [A]: Company Schedule C-1, Page 1 and Company Rebuttal Testimony
Column [B]: Testimony Staff Engineering Testimony
Column [C]: Column [A] + Column [B]

OPERATING ADJUSTMENT NO. 3 - Depreciation expense

LINE NO.	ACCT NO.	DESCRIPTION	[A] PLANT In SERVICE Per Staff	[B] NonDepreciable or Fully Depreciated PLANT	[C] DEPRECIABLE PLANT (Col A - Col B)	[D] DEPRECIATION RATE	[E] DEPRECIATION EXPENSE (Col C x Col D)
1	301.0	Organization Cost	\$ -	\$ -	\$ -	0.00%	\$ -
2	302.0	Franchise Cost	-	-	-	0.00%	-
3	303.0	Land and Land Rights	42,608	42,608	-	0.00%	-
4	304.0	Structures and Improvements	359,681	11,667	348,014	3.33%	11,589
5	305.0	Collecting and Impounding Res.	-	-	-	2.50%	-
6	306.0	Lake River and Other Intakes	0	-	0	2.50%	0
7	307.0	Wells and Springs	2,164,423	134,725	2,029,698	3.33%	67,589
8	308.0	Infiltration Galleries and Tunnels	-	-	-	6.67%	-
9	309.0	Supply Mains	-	-	-	2.00%	-
10	310.0	Power Generation Equipment	187,864	-	187,864	5.00%	9,393
11	311.0	Electric Pumping Equipment	3,585,660	-	3,585,660	12.50%	448,208
12	320.1	Water Treatment Equipment	-	-	-	3.33%	-
13	320.2	Chemical Solution Feeders	24,640	-	24,640	20.00%	4,928
14	330.0	Distribution Reservoirs & Standpipe	-	-	-	2.22%	-
15	330.1	Storage Tanks	1,758,175	222,970	1,535,205	2.22%	34,082
16	330.2	Pressure Tanks	321,969	-	321,969	5.00%	16,098
17	331.0	Transmission and Distribution Mains	6,083,805	805,218	5,278,587	2.00%	105,572
18	333.0	Services	1,888,741	247,045	1,641,696	3.33%	54,668
19	334.0	Meters	504,321	80,024	424,297	8.33%	35,344
20	335.0	Hydrants	718,857	148,034	570,823	2.00%	11,416
21	336.0	Backflow Prevention Devices	-	-	-	6.67%	-
22	339.0	Other Plant and Miscellaneous Equipment	-	-	-	6.67%	-
23	340.0	Office Furniture and Fixtures	36,758	-	36,758	6.67%	2,452
24	340.1	Computers and Software	-	-	-	20.00%	-
25	341.0	Transportation Equipment	89,569	-	89,569	20.00%	17,914
26	342.0	Stores Equipment	-	-	-	4.00%	-
27	343.0	Tools and Work Equipment	-	-	-	5.00%	-
28	344.0	Laboratory Equipment	-	-	-	10.00%	-
29	345.0	Power Operated Equipment	55,787	-	55,787	5.00%	2,789
30	346.0	Communications Equipment	351,219	-	351,219	10.00%	35,122
31	347.0	Miscellaneous Equipment	26,122	-	26,122	10.00%	2,612
32	348.0	Other Tangible Plant	-	-	-	10.00%	-
33		Total Plant	\$ 18,200,199	\$ 1,692,291	\$ 16,507,908		\$ 859,776
38		CIAC = Depreciation Expense/Depreciable Plant		5.21%			
39		CIAC Balance	\$ 753,535				
40		Depreciation Expense Before Amortization of CIAC:	\$ 859,776				
41		Less Amortization of CIAC:	\$ 39,246				
42		Test Year Depreciation Expense - Staff:	\$ 820,530				
43		Depreciation Expense - Company:	\$ 861,127				
44		Staff's Total Adjustment:	\$ (40,597)				

Note:

* Indicates items that were fully depreciated per Company Schedule C-2.

References:

- Column [A]: Schedule MJR-W4
- Column [B]: Testimony MJR From Column [A]
- Column [C]: Column [A] - Column [B]
- Column [D]: Staff Engineering Testimony
- Column [E]: Column [C] x Column [D]

OPERATING INCOME ADJUSTMENT NO. 4- Property tax expense

LINE NO.	Property Tax Calculation	[A] STAFF AS ADJUSTED	[B] STAFF RECOMMENDED
1	Staff Adjusted Test Year Revenues	\$ 1,882,238	\$ 1,882,238
2	Weight Factor	2	2
3	Subtotal (Line 1 * Line 2)	3,764,476	\$ 3,764,476
4	Staff Recommended Revenue, Per Schedule MJR-1	1,882,238	\$ 2,911,453
5	Subtotal (Line 4 + Line 5)	5,646,714	6,675,929
6	Number of Years	3	3
7	Three Year Average (Line 5 / Line 6)	1,882,238	\$ 2,225,310
8	Department of Revenue Mutilplier	2	2
9	Revenue Base Value (Line 7 * Line 8)	3,764,476	\$ 4,450,619
10	Plus: 10% of CWIP -	-	-
11	Less: Net Book Value of Licensed Vehicles	112,728	\$ 112,728
12	Full Cash Value (Line 9 + Line 10 - Line 11)	3,651,748	\$ 4,337,891
13	Assessment Ratio	19.0%	19.0%
14	Assessment Value (Line 12 * Line 13)	693,832	\$ 824,199
15	Composite Property Tax Rate (Per Company Schedule)	13.5000%	13.5000%
16			\$ -
17	Staff Test Year Adjusted Property Tax (Line 14 * Line 15)	\$ 93,668	
18	Company Proposed Property Tax	98,597	
19			
20	Staff Test Year Adjustment (Line 17-Line 18)	\$ (4,929)	
21	Property Tax - Staff Recommended Revenue (Line 14 * Line 15)		\$ 111,267
22	Staff Test Year Adjusted Property Tax Expense (Line 17)		\$ 93,668
23	Increase in Property Tax Expense Due to Increase in Revenue Requirement		\$ 17,599
24			
25	Increase to Property Tax Expense		\$ 17,599
26	Increase in Revenue Requirement		1,029,215
27	Increase to Property Tax per Dollar Increase in Revenue (Line 25/Line 26)		1.709903%

References:

Column [A]: Company Schedule C-2, Page 3

Column [B]: Testimony MJR

Column [C]: Column [A] + Column [B]

Lago Del Oro Water Company
 Docket No. W-01944A-13-0215
 Test Year Ended December 31, 2012

Surrebuttal Schedule MJR-W14

MENT NO. 5 - Test year income taxes RATE BASE ADJUSTMENT NO. 1 - Staff adjusted value of plant purc

LINE NO.	DESCRIPTION	[A]	[B]	[C]
		COMPANY TEST YEAR	STAFF ADJUSTMENTS	STAFF RECOMMENDED
1	Income Tax Expense	\$ (128,849)	\$ 64,847	\$ (64,002)

References:
 Column (A): Company Schedule C-1
 Column (B): Column [C] - Column [A]
 Column (C): Schedule MJR-W2

Monthly Usage Charge	Present	Company Proposed Rates	Staff Recommended Rates ¹
Meter Size (All Classes):			
5/8 x 3/4 Inch	12.40	14.80	14.15
3/4 Inch	12.40	14.80	14.15
1 Inch	18.00	24.67	23.59
1 1/2 Inch	28.00	49.33	47.16
2 Inch	40.00	78.93	75.46
3 Inch	62.00	157.87	150.94
4 Inch	84.00	246.67	235.84
5 Inch	106.00	Remove	NT
6 Inch	128.00	493.33	471.66
8 Inch	150.00	789.33	754.66
Golf Course Irrigation	-	200.00	200.00
Construction Hydrant	NT	NT	NT
Gallons in Minimum	2,000	-	-
Commodity Charge - Per 1,000 Gallons All Classes			
5/8" x 3/4" Meter			
All classes over Minimum	1.80	N/A	N/A
First 4,000 gallons	N/A	1.80	1.55
4,001 to 10,000 gallons	N/A	3.09	3.00
Over 10,000 gallons	N/A	4.38	4.08
Commercial, Irrigation (except golf course irrigation)			
First 10,000 gallons			
Over 10,000 gallons			
3/4" Meter			
All classes over Minimum	1.80	N/A	N/A
Residential:			
First 4,000 gallons	N/A	1.80	1.55
4,001 to 10,000 gallons	N/A	3.09	3.00
Over 10,000 gallons	N/A	4.38	4.08
Commercial, Irrigation (except golf course irrigation)			
First 10,000 gallons	N/A	3.09	3.00
Over 10,000 gallons	N/A	4.38	4.08
1" Meter			
All classes over Minimum	1.80	N/A	N/A
All Classes except golf course irrigation, hydrant			
First 17,000 gallons	N/A	3.09	3.00
Over 17,000 gallons	N/A	4.38	4.08
1 1/2" Meter			
All classes over Minimum	1.80	N/A	N/A
All Classes except golf course irrigation, hydrant			
First 34,000 gallons	N/A	3.09	3.00
Over 34,000 gallons	N/A	4.38	4.08
2" Meter			
All classes over Minimum	1.80	N/A	N/A
All Classes except golf course irrigation, hydrant			
First 54,000 gallons	N/A	3.09	3.00
Over 54,000 gallons	N/A	4.38	4.08
3" Meter			
All classes over Minimum	1.80	N/A	N/A
All Classes except golf course irrigation, hydrant			
First 107,000 gallons	N/A	3.09	3.00
Over 107,000 gallons	N/A	4.38	4.08
4" Meter			
All classes over Minimum	1.80	N/A	N/A
All Classes except golf course irrigation, hydrant			
First 167,000 gallons	N/A	3.09	3.00
Over 167,000 gallons	N/A	4.38	4.08
6" Meter			
All classes over Minimum	1.80	N/A	N/A
All Classes except golf course irrigation, hydrant			
First 334,000 gallons	N/A	3.09	3.00

Over 334,000 gallons	N/A	4.38	4.08
8" Meter			
All classes over Minimum	1.80	N/A	N/A
All Classes except golf course irrigation, hydrant			
First 534,000 gallons	N/A	3.09	3.00
Over 534,000 gallons	N/A	4.38	4.08
Golf Course Irrigation			
All Gallons	0.37	0.85	0.85
Hydrant/Construction			
All Gallons	N/T	4.38	4.08
Monthly Service Charge for Fire Sprinkler Up to 8"	NT	NT	Per Rule*
*2% of monthly minimum for a comparable size meter connection, but no less than \$10.00 per month. The service charge for fire sprinklers is only applicable for service lines separate and distinct for the primary water service line.			

Other Service Charges:

Establishment	\$ 25.00	\$ 25.00	\$ 25.00
Establishment (After Hours)	\$ 30.00	N/T	N/T
Reconnection (Delinquent)	\$ 25.00	\$ 25.00	\$ 25.00
Meter Reread (If Correct)	\$ 15.00	\$ 15.00	\$ 15.00
Meter Test (If Correct)	\$ 30.00	\$ 30.00	\$ 30.00
Deposit	**	**	**
Deposit Interest	**	***	***
Reestablishment (within 12 months)	***	***	***
NSF Check	\$ 10.00	\$ 10.00	\$ 10.00
Late Payment Penalty	N/T	1.5% per month	1.5% per month
Deferred Payment	1.5% per month	1.5% per month	1.5% per month
Moving Meter at Customer Request	N/T	N/T	N/T
Service Calls - Per Hour	N/T	N/T	N/T
After Hours Service Charge	N/T	\$ 30.00	30.00

* Per Commission Rule A.A.C. R-14-2-403(B)

** Per Commission Rule A.A.C. R-14-2-403(B)

*** Per Commission Rule A.A.C. R-14-2-403(D) - Months off the system times the monthly minimum.

(a) No charge for service calls during normal working hours.

In addition to the collection of regular rates, the utility will collect from its customers a proportionate share of any privilege, sales, use, and franchise tax. Per commission rule 14-2-409D(5).

Service and Meter Installation Charges

	Total Present Charge	Proposed Service Line	Proposed Meter	Total Proposed Charge	Recommended Service Line	Recommended Meter Installation	Total Recommended
5/8 x 3/4-inch	\$ 250.00	\$ 385.00	\$ 135.00	\$ 520.00	\$ 415.00	\$ 155.00	\$ 570.00
3/4-inch	\$ 275.00	\$ 415.00	\$ 205.00	\$ 620.00	\$ 415.00	\$ 205.00	\$ 620.00
1-inch	\$ 300.00	\$ 465.00	\$ 265.00	\$ 730.00	\$ 465.00	\$ 265.00	\$ 730.00
1-1/2-inch	\$ 450.00	520.00	475.00	995.00	520.00	475.00	995.00
2-inch	625.00	-	-	-	-	-	-
2-inch Turbine	-	\$ 800.00	995.00	\$ 1,795.00	\$ 800.00	\$ 995.00	\$ 1,795.00
2-inch Compound	\$ -	800.00	1,840.00	2,640.00	800.00	1,840.00	2,640.00
3-inch	800.00	-	-	-	-	-	-
3-inch Turbine	-	\$ 1,015.00	\$ 1,620.00	\$ 2,635.00	\$ 1,015.00	\$ 1,620.00	\$ 2,635.00
3-inch Compound	\$ -	1,135.00	2,495.00	3,630.00	1,135.00	2,495.00	3,630.00
4-inch	975.00	-	-	-	-	-	-
4-inch Turbine	-	\$ 1,430.00	\$ 2,570.00	\$ 4,000.00	\$ 1,430.00	\$ 2,570.00	\$ 4,000.00
4-inch Compound	\$ -	1,610.00	3,545.00	5,155.00	1,610.00	3,545.00	5,155.00
5-inch	\$ 1,150.00	-	-	-	-	-	-
6-inch	1,325.00	-	-	-	-	-	-
6-inch Turbine	-	2150	\$ 4,925.00	\$ 7,075.00	\$ 2,150.00	4925	\$ 7,075.00
6-inch Compound	\$ -	2,270.00	6,820.00	9,090.00	2,270.00	6,820.00	9,090.00
8-inch	-	-	-	-	-	-	-
8-inch or Larger	\$ 1,500.00	ICB*	ICB*	ICB*	ICB*	ICB*	ICB*

*ICB Indicates Individual Case Basis Cost.

Typical Bill Analysis
 General Service 5/8 x 3/4-Inch Meter

Company Proposed	Gallons	Present Rates	Proposed Rates	Dollar Increase	Percent Increase
Average Usage	7,024	\$ 21.44	\$ 31.34	\$ 9.90	46.17%
Median Usage	5,500	18.70	26.64	\$ 7.94	42.43%
Staff Recommended					
Average Usage	7,024	\$ 21.44	\$ 29.42	\$ 7.98	37.21%
Median Usage	5,500	18.70	24.85	\$ 6.15	32.89%

Present & Proposed Rates (Without Taxes)
 General Service 5/8 x 3/4-Inch Meter

Gallons	Present Rates	Company Proposed Rates	% Increase	Staff Recommended Rates	% Increase
-	\$ 12.40	\$ 14.80	19.35%	\$ 14.15	14.11%
1,000	12.40	16.60	33.87%	15.70	26.61%
2,000	12.40	18.40	48.39%	17.25	39.11%
3,000	14.20	20.20	42.25%	18.80	32.39%
4,000	16.00	22.00	37.50%	20.35	27.19%
5,000	17.80	25.09	40.96%	23.35	31.18%
5,500	18.70	26.64	42.43%	24.85	32.89%
6,500	20.50	29.73	45.00%	27.85	35.85%
7,024	21.44	31.34	46.17%	29.42	37.21%
7,500	22.30	32.82	47.15%	30.85	38.34%
8,000	23.20	34.36	48.10%	32.35	39.44%
8,500	24.10	35.91	48.98%	33.85	40.46%
9,500	25.90	39.00	50.56%	36.85	42.28%
10,500	27.70	42.73	54.26%	40.39	45.81%
11,500	29.50	47.11	59.69%	44.47	50.75%
12,500	31.30	51.49	64.50%	48.55	55.11%
13,500	33.10	55.87	68.79%	52.63	59.00%
14,500	34.90	60.25	72.64%	56.71	62.49%
15,500	36.70	64.63	76.10%	60.79	65.64%
16,500	38.50	69.01	79.25%	64.87	68.49%
17,500	40.30	73.39	82.11%	68.95	71.09%
18,500	42.10	77.77	84.73%	73.03	73.47%
19,500	43.90	82.15	87.13%	77.11	75.65%
20,500	45.70	86.53	89.34%	81.19	77.66%
25,500	54.70	108.43	98.23%	101.59	85.72%
30,500	63.70	130.33	104.60%	121.99	91.51%
35,500	72.70	152.23	109.39%	142.39	95.86%
40,500	81.70	174.13	113.13%	162.79	99.25%
45,500	90.70	196.03	116.13%	183.19	101.97%
50,500	99.70	217.93	118.59%	203.59	104.20%
75,500	144.70	327.43	126.28%	305.59	111.19%
100,500	189.70	436.93	130.33%	407.59	114.86%

BEFORE THE ARIZONA CORPORATION COMMISSION

BOB STUMP
Chairman
GARY PIERCE
Commissioner
BRENDA BURNS
Commissioner
SUSAN BITTER SMITH
Commissioner
BOB BURNS
Commissioner

IN THE MATTER OF THE APPLICATION OF)
LAGO DEL ORO WATER COMPANY, AN)
ARIZONA CORPORATION, FOR A)
DETERMINATION OF THE FAIR VALUE OF)
ITS UTILITY PLANT AND PROPERTY AND)
FOR INCREASES IN ITS WATER RATES AND)
CHARGES FOR UTILITY SERVICE BASED)
THEREON.)

DOCKET NO. W-01944A-13-0215

SURREBUTTAL

TESTIMONY

OF

JOHN A. CASSIDY

PUBLIC UTILITIES ANALYST

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

MARCH 7, 2014

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**EXECUTIVE SUMMARY
LAGO DEL ORO WATER COMPANY
DOCKET NO. W-01944A-13-0215**

The surrebuttal testimony of Staff witness John A. Cassidy addresses the following issues:

Capital Structure – Staff continues to recommend that the Commission adopt a capital structure for Lago Del Oro Water Company (“Company”) for this proceeding consisting of 29.0 percent debt and 71.0 percent equity.

Cost of Equity – Staff recommends that the Commission adopt a 9.7 percent return on equity (“ROE”) for the Company, which is an increase from the 9.3 percent ROE Staff recommended in its direct testimony. Staff’s estimated ROE for the Company is based on the 9.1 percent average of its discounted cash flow method (“DCF”) cost of equity methodology estimates for the sample companies of 8.7 percent for the constant-growth DCF model and 9.5 percent for the multi-stage DCF model. Staff’s recommended ROE includes an upward economic assessment adjustment of 60 basis points (0.6 percent).

Cost of Debt – Staff continues to recommend that the Commission adopt a 4.6 percent cost of debt for the Company.

Overall Rate of Return – Staff recommends that the Commission adopt an 8.2 percent overall rate of return. In direct testimony, Staff had recommended an overall rate of return of 7.9 percent.

Mr. Bourassa’s Testimony – The Commission should reject the Company’s proposed 10.5 percent ROE for the following reasons:

Mr. Bourassa’s primary Future Growth DCF estimates rely exclusively on analysts’ forecasts of earnings per share growth. Effectively, Mr. Bourassa’s overall DCF estimate is weighted 75 percent by his Future Growth DCF estimates. Mr. Bourassa’s proposed ROE has been inflated by an implicit upward adjustment for financial risk and small company risk premium.

1 **I. INTRODUCTION**

2 **Q. Please state your name, occupation, and business address.**

3 A. My name is John A. Cassidy. I am a Public Utilities Analyst employed by the Arizona
4 Corporation Commission (“Commission”) in the Utilities Division (“Staff”). My business
5 address is 1200 West Washington Street, Phoenix, Arizona 85007.

6
7 **Q. Are you the same John A. Cassidy who filed direct testimony in this case?**

8 A. Yes, I am.

9
10 **Q. What is the purpose of your surrebuttal testimony in this rate proceeding?**

11 A. The purpose of my surrebuttal testimony is to update Staff’s cost of capital
12 recommendations and to respond to the cost of capital rebuttal testimony of Lago Del Oro
13 Water Company (“LDO” or “Company”) witness, Thomas J. Bourassa (“Mr. Bourassa’s
14 Rebuttal”).

15
16 **Q. Please explain how Staff’s surrebuttal testimony is organized.**

17 A. Staff’s surrebuttal testimony is presented in three sections. Section I is this introduction.
18 Section II presents Staff’s comments on the rebuttal testimony of the Company’s cost of
19 capital witness, Mr. Bourassa. Lastly, Section III presents Staff’s recommendations.

1 **II. STAFF RESPONSE TO COMPANY'S COST OF CAPITAL WITNESS MR.**
2 **THOMAS J. BOURASSA**

3 **Q. Please summarize the capital structure, cost of debt, cost of equity, and overall rate**
4 **of return proposed in Mr. Bourassa's rebuttal.**

5 A. In his rebuttal testimony, Mr. Bourassa has adopted Staff's recommended 29.0 percent
6 debt / 71.0 percent equity capital structure, and Staff's recommended 4.6 percent cost of
7 debt. Mr. Bourassa continues to recommend a 10.5 percent cost of equity for the
8 Company. Mr. Bourassa's cost of capital recommendations result in an overall rate of
9 return ("ROR") for LDO of 8.79 percent.

10
11 **Q. Mr. Cassidy, in his rebuttal testimony Mr. Bourassa suggests that your direct**
12 **testimony criticized him for relying exclusively on analysts' forecasts of earnings**
13 **per share ("EPS") growth in the discounted cash flow ("DCF") model.¹ Do you**
14 **consider this to be a proper characterization of your criticism of his DCF**
15 **methodology?**

16 A. No. In direct testimony, I fully acknowledge that while Mr. Bourassa's primary
17 Future Growth DCF model relies exclusively on analysts' forecasts of EPS growth to
18 estimate the dividend growth (g) component, his secondary Past and Future Growth
19 DCF model does *not* so rely (instead, it gives a 50 percent weighting to historical
20 measures of growth and a 50 percent weight to the dividend growth rate obtained
21 from his primary Future Growth DCF model).² My criticism of his exclusive reliance
22 on analysts' forecasts of EPS growth in the DCF model relates solely to his primary
23 Future Growth DCF model. It is worth repeating, however, that Mr. Bourassa's

¹ See Bourassa Rebuttal, p.11, lines 3-5.

² See Cassidy Direct, pp. 33-34, lines 22:8.

1 overall DCF estimate effectively gives a 75 percent weight to analysts' forecasts of
2 EPS growth.³

3
4 **Q. In his rebuttal testimony,⁴ Mr. Bourassa employs a recent 3-year historical total**
5 **return statistic for the water utility industry as “evidence” that the dividend growth**
6 **(g) rates used in Staff’s constant growth DCF model are significantly understated.**
7 **How does Staff respond?**

8 A. Mr. Bourassa’s assertion is without merit, as the “evidence” he provides is predicated on
9 logic which erroneously assumes that realized, historical returns represent the cost of
10 equity (K) in the constant growth DCF model. Specifically, Mr. Bourassa presents a
11 calculation based upon a realized 11.9 percent 3-year historical annualized total return for
12 water utility stocks, as reported by *Value Line*. Using the constant growth DCF equation
13 (i.e., $K = (D_1/P_0) + g$), he then solves for the dividend growth (g) rate by mistakenly
14 assuming the 11.9 percent total return figure to be the estimated cost of equity (K), and
15 substituting Staff’s 2.9 percent expected dividend yield as the value for (D_1/P_0) . Based
16 upon this calculation, Mr. Bourassa states “[t]his indicated return would *imply* a
17 [dividend] growth rate for the DCF model of 9.0 percent (emphasis added).”⁵ To
18 demonstrate that Staff’s DCF dividend growth (g) rate is “significantly understated,” Mr.
19 Bourassa then compares his *implied* 9.0 percent growth rate to Staff’s actual 5.2 percent
20 dividend growth rate.

³ See Cassidy Direct, p. 34, lines 8-11.

⁴ See Bourassa Rebuttal, p. 13, lines 4-13.

⁵ See Bourassa Rebuttal, p. 13, lines 7-8; and p.13, footnote 21.

1 **Q. Does Mr. Bourassa employ this same logic in his effort to justify his use of analysts'**
2 **forecasts of EPS growth as a proxy for the dividend growth (g) component in the**
3 **constant growth DCF model?**

4 A. Yes. In doing so, he points out that even his 6.07 percent dividend growth rate derived
5 from analysts' forecasts of EPS growth used in his primary Future Growth DCF model
6 "falls far short of the implied [9.0 percent] growth rate investors have realized over the
7 last three years." Mr. Bourassa concludes with the observation, "[w]hat this shows is
8 that when using forecasts of earnings growth, the indicated cost of equity can vastly
9 understate the cost of equity."⁶

10

11 **Q. Do realized returns represent the cost of equity?**

12 A. No, as stated in my direct testimony, the cost of equity represents investors' expected
13 returns.⁷ As such, the cost of equity is prospective (i.e., forward looking) in nature,
14 whereas realized returns represent historical (i.e., backward looking) measures of
15 performance.

16

17 **Q. In light of the above, and given Mr. Bourassa's discussion in this regard, does his**
18 **rebuttal testimony provide support for a conclusion that reliance on analysts'**
19 **forecasts of EPS growth in the DCF model can vastly understate the cost of equity?**

20 A. No, it does not.

⁶ See Bourassa Rebuttal, p. 13, lines 12-13.

⁷ See Cassidy Direct, p. 14, line 22.

1 **Q. Mr. Cassidy, in his rebuttal testimony Mr. Bourassa takes exception to comments**
2 **made by Staff in direct testimony concerning the market risk premium (“MRP”)**
3 **employed by Mr. Bourassa in his Current Market Risk Premium CAPM analysis.**
4 **How does Staff respond?**

5 A. In direct testimony, I pointed out that due to strength in the equity markets, *Value Line’s*
6 3-5 year stock price appreciation estimate had fallen considerably since the filing of Mr.
7 Bourassa’s direct testimony, and that as a consequence the 9.31 percent MRP utilized in
8 his Current MRP CAPM model was no longer reflective of current market conditions.⁸ As
9 evidenced by the filing of Mr. Bourassa’s rebuttal testimony, Staff’s observation in this
10 regard has proven correct, for as shown in TJB Rebuttal Schedule D-4.12, Mr. Bourassa
11 now reports the updated MRP in his current MRP CAPM to be 5.74 percent, a figure 357
12 basis points *lower* than that used in his direct testimony (9.31% - 5.74% = 3.57%).
13 Coincidentally, this change has resulted in Mr. Bourassa’s Current MRP CAPM estimated
14 cost of equity (K) falling from 10.4 percent in direct testimony (*See* TJB Schedule D-4.12)
15 to 8.3 percent in rebuttal (*See* TJB Rebuttal Schedule D-4.12).

16
17 **III. STAFF RECOMMENDATIONS**

18 **Q. In updating its cost of capital analysis for the Company, did Staff’s recommended**
19 **ROE and overall ROR change from the levels recommended by Staff in direct**
20 **testimony?**

21 A. Yes. Staff now recommends a ROE of 9.7 percent instead of 9.3 percent. As a
22 consequence of this change, Staff’s recommended overall ROR increased from 7.9 percent
23 in direct testimony to 8.2 percent in surrebuttal.

24

⁸ See Cassidy Direct, pp. 40-41, lines 8:2.

1 **Q. What factors contributed to this upward change to Staff's estimated cost of equity**
2 **for LDO?**

3 A. On January 17, 2014, *Value Line* issued its quarterly update for the publicly-traded water
4 utility companies under its review, providing annual financial data for each of Staff's
5 seven sample companies through the year ending December 31, 2013. Utilizing this
6 information, Staff updated its model in order to calculate historical measures of growth in
7 dividends per share ("DPS"), EPS and Sustainable Growth over the 10-year period, 2003-
8 2013. As a consequence, Staff's overall average DCF cost of equity estimate increased
9 from 8.7 percent in direct testimony to an updated 9.1 percent in surrebuttal. The
10 increases to Staff's DCF cost of equity estimates are due, in part, to a change in the 10-
11 year period over which historical measures of growth are calculated and, in part, to the
12 expected dividend yield (D_1/P_0) component in Staff's constant growth DCF model having
13 risen from 2.9 percent in direct testimony to 3.1 percent in surrebuttal.

14
15 **Q. Based on Staff's review of Mr. Bourassa's rebuttal testimony, and given its updated**
16 **cost of capital analysis, what are Staff's recommendations for the Company?**

17 A. Staff recommends the following for LDO's cost of capital:
18 1. A capital structure of 29.0 percent debt and 71.0 percent equity.
19 2. A 4.6 percent cost of debt.
20 3. A 9.7 percent return on equity (a figure which includes an upward 60 basis point (0.6
21 percent) economic assessment adjustment).
22 4. An 8.2 percent overall rate of return.

23
24 **Q. Does this conclude your surrebuttal testimony?**

25 A. Yes, it does.

Lago Del Oro Water Company Cost of Capital Calculation
 Capital Structure
 And Weighted Average Cost of Capital
 Staff Recommended and Company Proposed

[A]	[B]	[C]	[D]
<u>Description</u>	<u>Weight (%)</u>	<u>Cost</u>	<u>Weighted Cost</u>
Staff Recommended Structure			
Debt	29.0%	4.6%	1.3%
Common Equity	71.0%	9.7%	6.9%
Weighted Average Cost of Capital			8.2%
Company Proposed Structure			
Debt	29.0%	4.6%	1.33%
Common Equity	71.0%	10.50%	7.46%
Weighted Average Cost of Capital			8.79%

[D] : [B] x [C]

Supporting Schedules: JAC-2, JAC-3 and JAC-4.

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Lago Del Oro Water Company Cost of Capital Calculation
Average Capital Structure of Sample Water Utilities

[A]	[B]	[C]	[D]
<u>Company</u>	<u>Debt</u>	<u>Common Equity</u>	<u>Total</u>
American States Water	43.3%	56.7%	100.0%
California Water	54.2%	45.8%	100.0%
Aqua America	55.2%	44.8%	100.0%
Connecticut Water	55.3%	44.7%	100.0%
Middlesex Water	43.1%	56.9%	100.0%
SJW Corp	56.2%	43.8%	100.0%
York Water	<u>45.0%</u>	<u>55.0%</u>	<u>100.0%</u>
 Average Sample Water Utilities	50.3%	49.7%	100.0%
 Chaparral City - Actual Capital Structure	29.0%	71.0%	100.0%

Source:

Sample Water Companies from Value Line

Lago Del Oro Water Company Cost of Capital Calculation
Growth in Earnings and Dividends
Sample Water Utilities

[A]	[B]	[C]	[D]	[E]
<u>Company</u>	Dividends Per Share 2003 to 2013 <u>DPS¹</u>	Dividends Per Share Projected <u>DPS¹</u>	Earnings Per Share 2003 to 2013 <u>EPS¹</u>	Earnings Per Share Projected <u>EPS¹</u>
American States Water	5.6%	7.1%	14.8%	3.8%
California Water	1.3%	8.9%	4.5%	10.2%
Aqua America	7.6%	10.2%	9.6%	6.0%
Connecticut Water	1.7%	3.4%	3.7%	2.9%
Middlesex Water	1.5%	1.5%	5.1%	3.6%
SJW Corp	4.1%	5.4%	2.8%	7.5%
York Water	4.1%	6.1%	4.8%	8.8%
Average Sample Water Utilities	3.7%	6.1%	6.5%	6.1%

¹ Value Line

Lago Del Oro Water Company Cost of Capital Calculation
Sustainable Growth
Sample Water Utilities

[A]	[B]	[C]	[D]	[E]	[F]
Company	Retention Growth 2002 to 2012 <u>br</u>	Retention Growth Projected <u>br</u>	Stock Financing Growth <u>vs</u>	Sustainable Growth 2002 to 2012 <u>br + vs</u>	Sustainable Growth Projected <u>br + vs</u>
American States Water	3.8%	5.2%	1.5%	5.3%	6.8%
California Water	2.6%	3.4%	1.6%	4.2%	5.1%
Aqua America	4.0%	5.2%	1.8%	5.8%	7.1%
Connecticut Water	2.0%	3.6%	4.0%	6.0%	7.6%
Middlesex Water	1.3%	2.8%	2.7%	4.0%	5.5%
SJW Corp	3.3%	3.8%	0.1%	3.5%	3.9%
York Water	<u>2.2%</u>	<u>3.7%</u>	<u>4.4%</u>	<u>6.6%</u>	<u>8.2%</u>
Average Sample Water Utilities	2.7%	4.0%	2.3%	5.1%	6.3%

[B]: Value Line

[C]: Value Line

[D]: Value Line, MSN Money, and Form 10-Ks filed with the Securities and Exchange Commission (<http://www.sec.gov/>)

[E]: [B]+[D]

[F]: [C]+[D]

Lago Del Oro Water Company Cost of Capital Calculation
 Selected Financial Data of Sample Water Utilities

[A]	[B]	[C]	[D]	[E]	[F]	[G]
<u>Company</u>	<u>Symbol</u>	<u>Spot Price</u> <u>2/5/2014</u>	<u>Book Value</u>	<u>Mkt To</u> <u>Book</u>	<u>Value Line</u> <u>Beta</u> β	<u>Raw</u> <u>Beta</u> β_{raw}
American States Water	AWR	27.15	12.01	2.3	0.65	0.45
California Water	CWT	21.93	11.81	1.9	0.60	0.37
Aqua America	WTR	23.31	8.10	2.9	0.60	0.37
Connecticut Water	CTWS	32.04	14.10	2.3	0.75	0.60
Middlesex Water	MSEX	19.51	12.17	1.6	0.75	0.60
SJW Corp	SJW	27.92	15.41	1.8	0.85	0.75
York Water	YORW	19.76	8.30	2.4	0.70	0.52
Average				2.2	0.70	0.52

[C]: Msn Money

[D]: Value Line

[E]: [C] / [D]

[F]: Value Line

[G]: $(-0.35 + [F]) / 0.67$

Lago Del Oro Water Company Cost of Capital Calculation
Calculation of Expected Infinite Annual Growth in Dividends
Sample Water Utilities

[A]	[B]
<u>Description</u>	<u>g</u>
DPS Growth - Historical ¹	3.7%
DPS Growth - Projected ¹	6.1%
EPS Growth - Historical ¹	6.5%
EPS Growth - Projected ¹	6.1%
Sustainable Growth - Historical ²	5.1%
<u>Sustainable Growth - Projected²</u>	<u>6.3%</u>
Average	5.6%

1 Schedule JAC-5

2 Schedule JAC-6

Lago Del Oro Water Company Cost of Capital Calculation
Multi-Stage DCF Estimates
Sample Water Utilities

[A]	[B]	[C]	[D]	[E]	[F]	[G]	[H]
<u>Company</u>	Current Mkt. Price (P_0) ¹ 2/5/2014	Projected Dividends ² (Stage 1 growth) (D_t)				Stage 2 growth ³ (g_n)	Equity Cost Estimate (K) ⁴
		d_1	d_2	d_3	d_4		
American States Water	27.2	0.78	0.82	0.87	0.92	6.5%	9.3%
California Water	21.9	0.68	0.71	0.75	0.80	6.5%	9.5%
Aqua America	23.3	0.60	0.63	0.67	0.71	6.5%	9.0%
Connecticut Water	32.0	1.01	1.06	1.12	1.19	6.5%	9.6%
Middlesex Water	19.5	0.78	0.83	0.88	0.92	6.5%	10.4%
SJW Corp	27.9	0.77	0.81	0.86	0.91	6.5%	9.2%
York Water	19.8	0.58	0.61	0.65	0.68	6.5%	9.4%

Average 9.5%

$$P_0 = \sum_{t=1}^n \frac{D_t}{(1+K)^t} + \frac{D_n(1+g_n)}{K-g_n} \left[\frac{1}{(1+K)} \right]^n$$

Where : P_0 = current stock price
 D_t = dividends expected during stage 1
 K = cost of equity
 n = years of non - constant growth
 D_n = dividend expected in year n
 g_n = constant rate of growth expected after year n

1 [B] see Schedule JAC-7

2 Derived from Value Line Information

3 Average annual growth in GDP 1929 - 2012 in current dollars.

4 Internal Rate of Return of Projected Dividends

BEFORE THE ARIZONA CORPORATION COMMISSION

BOB STUMP
Chairman
GARY PIERCE
Commissioner
BRENDA BURNS
Commissioner
BOB BURNS
Commissioner
SUSAN BITTER SMITH
Commissioner

IN THE MATTER OF THE APPLICATION OF) DOCKET NO. W-01944A-13-0215
LAGO DEL ORO WATER COMPANY FOR, AN)
ARIZONA CORPORATION, FOR A)
DETERMINATION OF THE FAIR VALUE OF ITS)
UTILITY PLANT AND PROPERTY AND FOR)
INCREASES IN ITS WATER RATES AND)
CHARGES FOR UTILITY SERVICE BASED)
THEREON.)

SURREBUTTAL TESTIMONY

OF

MICHAEL THOMPSON, P. E.

UTILITIES ENGINEER

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

MARCH 7, 2014

**SURREBUTTAL TESTIMONY
LAGO DEL ORO WATER COMPANY
DOCKET NO. W-01944A-13-0215**

RECOMMENDATIONS

1. Staff recommends that Lago Del Oro Water Company (“LDO” or “Company”) file with Docket Control, as a compliance item in this docket and within 90 days of the effective date of a decision in this proceeding, at least seven (7) BMPs in the form of tariffs that substantially conform to the templates created by Staff for Commission’s review and consideration. The templates created by Staff are available on the Commission’s website at <http://www.azcc.gov/Divisions/Utilities/forms.asp>. LDO may request cost recovery of the actual costs associated with the BMPs implemented in its next general rate application.
2. Staff recommends that any increase in rates approved by the Commission not become effective until ADWR has determined that LDO is in compliance with departmental requirements governing water providers and/or community water systems.

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1 **INTRODUCTION**

2 **Q. Please state your name and business address.**

3 A. My name is Michael Thompson. My business address is 1200 West Washington Street,
4 Phoenix, Arizona 85007.

5
6 **Q. By whom and in what position are you employed?**

7 A. I am employed by the Arizona Corporation Commission (“Commission” or “ACC”) as a
8 Utilities Engineer - Water/Wastewater in the Utilities Division.

9
10 **Q. Did you submit Direct Testimony on behalf of the Utilities Division in this case?**

11 A. Yes.

12
13 **PURPOSE OF TESTIMONY**

14 **Q. What is the purpose of your Surrebuttal Testimony?**

15 A. To respond to the Rebuttal Testimony filed by Ray L. Jones on behalf of LDO. My
16 testimony addresses LDO’s compliance status with ADWR, and LDO’s position on Best
17 Management Practices (“BMPs”).

18
19 **ADWR COMPLIANCE STATUS**

20 **Q. Does ADWR consider LDO to be in compliance with respect to LDO’s Water
21 System Plan?**

22 A. Yes. Prior to my direct testimony, LDO had not submitted its Water System Plan to
23 ADWR for approval. Therefore, ADWR considered LDO to be non-compliant with
24 departmental requirements governing water providers and/or community water systems at
25 that time. Staff recommended that any increase in rates approved by the Commission not

1 become effective until ADWR has determined that LDO is in compliance with
2 departmental requirements governing water providers and/or community water systems.
3 Since my direct testimony, LDO has submitted its Water System Plan to ADWR and
4 ADWR currently considers LDO to be in compliance with respect to its Water System
5 Plan.

6
7 **Q. Is LDO currently in compliance with ADWR with regards to its Well Permits?**

8 A. No. Since my direct testimony, a recent ADWR Water Provider Compliance Report,
9 dated January 14, 2014, indicates that LDO is now non-compliant with departmental
10 requirements governing water providers and/or community water systems for a different
11 reason. LDO's well No. 55-573651 (LDO Well No. 19) has not been permitted as a
12 service well by ADWR.

13
14 **Q. Does Staff have a recommendation regarding LDO's current Compliance Status?**

15 A. Yes. Because of the recent non-compliance regarding LDO Well No. 19, Staff continues
16 to recommend that any increase in rates approved by the Commission not become
17 effective until ADWR has determined that LDO is in compliance with departmental
18 requirements governing water providers and/or community water systems.

19
20 **BMPS**

21 **Q. What is LDO's position on BMPs?**

22 A. Mr. Jones stated that LDO does not agree with Staff's recommendation because it is
23 excessive and duplicative, taking LDO beyond what is required by the Arizona
24 Department of Water Resources' ("ADWR"). Mr. Jones also stated the Company is
25 already enrolled with ADWR's Modified Non-Per Capita Conservation Program

1 (“Modified NPCCP”) that requires LDO to implement the Public Education Program
2 (“PEP”) and one additional BMP. Staff recommends that LDO file at least seven BMPs
3 in the form of tariffs that substantially conform to the templates created by Staff for
4 Commission review and approval.

5
6 **Q. First, could you provide a brief background of the BMPs?**

7 **A.** Yes. In 2008, ADWR added a new regulatory program for the ADWR Third
8 Management Plan for Active Management Areas (“AMAs”). The new program, called
9 Modified NPCCP, addresses large municipal water providers (cities, towns and private
10 water companies serving more than 250 acre-feet per year) and was developed in
11 conjunction with stakeholders from all AMAs. Participation in the program is required
12 for all large municipal water providers in AMAs that do not have a Designation of
13 Assured Water Supply and that are not regulated as a large untreated water provider or an
14 institutional provider.

15
16 The Modified NPCCP is a performance-based program that requires participating
17 providers to implement water conservation measures that result in water use efficiency in
18 their service areas. A water provider regulated under the program must implement a
19 required PEP and choose one or more additional BMPs based on its size, as defined by its
20 total number of water service connections. The provider must select the additional BMPs
21 from the list included in the Modified NPCCP Program. The BMPs are a mix of
22 technical, policy, and information conservation efforts.
23

1 Although the implementation of the Modified NPCCP is required of large municipal
2 water providers within an AMA, the Staff has recommended adoption of the BMPs for
3 implementation by Commission-regulated water companies.
4

5 **Q. Could you also provide a background on how Staff decided on the number of BMPs**
6 **it is recommending in this case?**

7 A. Yes. In April of 2011, Staff had in-house discussions regarding the implementation of
8 BMPs. Based on the knowledge of ADWR's requirements to implement the Modified
9 NPCCP (a PEP and one or more additional BMPs based on the customer base size) and
10 the understanding of some Commissioners' desire for additional BMPs above a water
11 company's ADWR requirements, it was decided by the Utilities Director to recommend
12 the number of BMPs based on the size of a water utility as follows:

13 Class A – 10 BMPs

14 Class B – 7 BMPs

15 Class C – 5 BMPs

16 Class D & E – 3 BMPs
17

18 With the adoption of this guideline, Staff was primarily looking for consistency when
19 recommending the number of BMPs to be implemented for a water utility.
20

21 **Q. Do you agree that filing the BMPs with the Commission is duplication of State**
22 **regulatory oversight?**

23 A. No, I do not. Basically, the difference between the ADWR and ACC filing is the ACC
24 requires the BMPs to be filed in tariff form. The ACC requires the BMPs be filed in
25 tariff form for implementation, notification of water company/customer requirements,

1 and notification of steps for service termination, if needed. The ADWR filing does not
2 address these issues. Having ACC approved BMP tariffs gives water companies more
3 tools to prevent water loss, at a little to no extra cost to the Company. BMPs also assist
4 customers in using water more efficiently and not wasting it, thereby preventing
5 excessively high bills.
6

7 **Q. Are you aware of another State regulation under the terms of which the**
8 **Commission requires water utilities to file a tariff with the ACC for**
9 **implementation?**

10 A. Yes, the Backflow Prevention Tariff. The backflow prevention program falls under the
11 Arizona Department of Environment Quality (“ADEQ”) regulation and, if a water utility
12 is to implement this ADEQ requirement, the water utility must file this Backflow
13 Prevention Tariff for implementation, notification of water company/customer
14 requirements, and notification of steps for service termination, if needed.
15

16 **Q. Based on the Company’s Rebuttal Testimony, has Staff’s recommendation**
17 **regarding the BMPs changed?**

18 A. No. Staff still recommends that the Company file with Docket Control, as a compliance
19 item in this docket, within 90 days of the effective date of a decision in this proceeding,
20 at least seven BMPs in the form of tariffs that substantially conform to the templates
21 created by Staff for Commission review and approval. These BMP templates are
22 available on the Commission’s website. The Company may submit the two approved
23 ADWR BMPs as part of the seven and may request recovery of the actual costs
24 associated with the implemented BMPs in its next general rate application.
25

1 **Q. Does this conclude your Surrebuttal Testimony?**

2 **A. Yes, it does.**