

ORIGINAL



0000152505

RECEIVED

2014 JAN 31 P 3 39

ARIZONA CORPORATION COMMISSION
DOCKET CONTROL

1 FENNEMORE CRAIG, P.C.
 Jay L. Shapiro (No. 014650)
 2 Todd Wiley (No. 015358)
 2394 E. Camelback Road
 3 Suite 600
 Phoenix, Arizona 85016
 4 Attorneys for Liberty Utilities (Litchfield Park Water & Sewer) Corp.

BEFORE THE ARIZONA CORPORATION COMMISSION

5
 6
 7
 8
 9 IN THE MATTER OF THE
 APPLICATION OF LITCHFIELD PARK
 10 SERVICE COMPANY, AN ARIZONA
 CORPORATION, FOR A
 DETERMINATION OF THE FAIR
 11 VALUE OF ITS UTILITY PLANTS AND
 PROPERTY AND FOR INCREASES IN
 12 ITS WATER RATES AND CHARGES
 FOR UTILITY SERVICE BASED
 13 THEREON.

DOCKET NO: W-01427A-13-0043

14 IN THE MATTER OF THE
 APPLICATION OF LITCHFIELD PARK
 15 SERVICE COMPANY, AN ARIZONA
 CORPORATION, FOR A
 DETERMINATION OF THE FAIR
 16 VALUE OF ITS UTILITY PLANTS AND
 PROPERTY AND FOR INCREASES IN
 17 ITS WASTEWATER RATES AND
 18 CHARGES FOR UTILITY SERVICE
 BASED THEREON.

DOCKET NO: SW-01428A-13-0042

REPLY BRIEF

January 31, 2014

Arizona Corporation Commission

DOCKETED

JAN 31 2014

DOCKETED BY	<i>nr</i>
-------------	-----------

Table of Contents

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26

I. BRIEF SUMMARY OF THE ISSUE. 1

II. RATEPAYERS AND THE COMPANY DERIVE SUBSTANTIAL BENEFITS FROM THE PROPOSED SIBS..... 4

A. Regulatory Lag Is Not in the Public Interest..... 4

B. The SIBs Promote Safe and Reliable Utility Service, Including Needed Plant Improvements and Upgrades. 6

C. The Proposed Water and Wastewater SIBs Benefit Customers Through Rate Gradualism. 7

D. The Proposed Water and Wastewater SIBs Benefit Customers Through Rate Stability. 8

E. The Efficiency Credit Is a Direct Monetary Benefit to Both Water and Wastewater Customers. 9

F. The Proposed SIBs Benefit Water and Wastewater Customers Through Financial Stability and Increased Utility Ability to Attract Capital. 11

III. THE PROPOSED SIBS ARE LEGAL AND COMPLY WITH ARIZONA’S FAIR VALUE REQUIREMENT..... 12

A. The SIB is A Lawful Adjuster Mechanism..... 12

B. Plant- Based Adjusters Are Legal In Arizona and the Commission Has Approved and RUCO Has Supported Numerous Plant-Based Adjusters for Other Utilities..... 14

C. The Proposed SIBs Comply With Arizona’s Fair Value Requirement..... 16

D. The SIB Is Not Single Issue Ratemaking. 19

E. Alternatively, the SIB Is a Valid and Lawful Surcharge Mechanism. 21

F. RUCO Does Not State Any Persuasive Reason for Rejecting the Wastewater SIB. 23

G. The RAPA Report Is Nothing More Than Consumer Advocacy and Should Be Summarily Ignored..... 26

IV. RUCO’S OTHER RED HERRINGS SHOULD BE IGNORED..... 27

A. RUCO’s Extraordinary Circumstances Argument Is Meritless..... 27

B. The LPSCO SIBs and the AWC SIB Are Virtually Identical..... 28

V. CONCLUSION..... 30

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26

TABLE OF ABBREVIATIONS AND CONVENTIONS

LPSCO uses the following abbreviations in citing to the pre-filed testimony and hearing transcripts in this brief. Other documents that were admitted as exhibits during the hearing are cited by hearing exhibit number. The final schedules will be cited as "Final Schedule XXX." Other citations to testimony and documents are provided in full, including (where applicable) the Commission's docket number and filing date.

DEFINED TERMS

Full Name/Description	Abbreviated term
Alaska Department of Law Regulatory Affairs and Public Advocacy	RAPA
Arizona Corporation Commission	Commission
Arizona Corporation Commission Utilities Division Staff	Staff
Arizona Public Service Company, Docket No. E-01345A-11-0224, Proposed Settlement Agreement, dated January 6, 2012	APS Settlement Agreement
Arizona Water Company	AWC
Arizona Water Company-Eastern Group, Docket No. W-01445A-11-0310	AWC Rate Case
Arizona Water Company-Eastern Group, Docket No. W-01445A-11-0310, Phase 2	AWC SIB Settlement
Arizona Water Company-Eastern Group, Docket No. W-01445A-11-0310, Phase 2, Settlement Agreement Regarding Distribution System Improvement Charge and Other DSIC-Like Proposals, dated April 1, 2013	AWC Settlement Agreement
Arsenic Cost Recovery Mechanism	ACRM
Construction Work in Progress	CWIP
Distribution System Improvement Charge	DSIC
Energy Efficiency/Demand Side Management	EE/DSM
Environmental Improvement Surcharge	EIS

* The Final Schedules are attached to the Proposed Settlement Agreement Between LPSCO and RUCO (filed December 11, 2013) (Ex. A-17).

1	Full Name/Description	Abbreviated term
2	Fair Value Rate Base	FVRB
3	Fire Flow Cost Recovery Mechanism	FCRM
4	Liberty Utilities (Litchfield Park Water & Sewer Corp.)	LPSCO or the Company
5	Liberty Utilities (Litchfield Park Water & Sewer Corp.), Arizona Corporation	Parties
6	Commission Utilities Division Staff and Residential Utility Consumer Office	
7		
8	Plan of Administration	POA
9	Plant Replacement Surcharge Mechanism	PRISM
10	Proposed Settlement Agreement Between LPSCO and RUCO in the LPSCO Rate Case, dated December 11, 2013	Settlement
11		
12	Purchased Power Adjustment Mechanism	PPAM
13	Renewable Energy Surcharge	RES
14	Residential Utility Consumer Office	RUCO
15	System Improvement Benefit	SIB
16	Valencia Water Company, Inc., Global Water – Palo Verde Utilities Company, Water Utility of Northern Scottsdale, Water Utility of Greater Tonopah, Inc., Valencia Water Company – Greater Buckeye Division, Global Water – Santa Cruz Water Company and Willow Valley Water Co., Inc., Docket No. W-01212A-12-0309, et al., Recommended Opinion and Order, dated January 21, 2014	Global ROO
17		
18		
19		
20	Weighted Average Cost of Capital	WACC
21		
22		
23		
24		
25		
26		

LPSCO PRE-FILED TESTIMONY

	Pre-Filed Testimony	Hearing Exhibit	Abbreviation
1			
2			
3	Direct Testimony of Greg Sorensen	A-1	Sorensen Dt.
4	Direct Testimony of Christopher Krygier	A-2	Krygier Dt.
5			
6	Direct Testimony of Thomas J. Bourassa (Rate Base)	A-3	Bourassa Dt.
7	Direct Testimony of Thomas J. Bourassa (Cost of Capital)	A-4	Bourassa COC Dt.
8			
9	Rebuttal Testimony of Christopher Krygier	A-5	Krygier Rb.
10	Rebuttal Testimony of Thomas J. Bourassa (Rate Base)	A-6	Bourassa Rb.
11	Rebuttal Testimony of Greg Sorensen	A-7	Sorensen Rb.
12	Rebuttal Testimony of Thomas J. Bourassa (Cost of Capital)	A-8	Bourassa COC Rb.
13			
14	Rebuttal Testimony of Wendell Licon	A-9	Licon Rb.
15	Rejoinder Testimony of Christopher Krygier	A-12	Krygier Rj.
16	Rejoinder Testimony of Thomas J. Bourassa (Rate Base)	A-13	Bourassa Rj.
17			
18	Rejoinder Testimony of Greg Sorensen	A-14	Sorensen Rj.
19	Rejoinder Testimony of Thomas J. Bourassa (Cost of Capital)	A-15	Bourassa COC Rj.
20			
21	Rejoinder Testimony of Wendell Licon	A-16	Licon Rj.
22			
23			
24			
25			
26			

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26

RUCO PRE-FILED TESTIMONY

Pre-Filed Testimony	Hearing Exhibit	Abbreviation
Direct Testimony of Robert Mease	R-1	Mease Dt.
Surrebuttal Testimony of Robert Mease	R-2	Mease Sb.
Direct Testimony of Robert Mease (Rate Design)	R-3	Mease RD Dt.

STAFF PRE-FILED TESTIMONY

Pre-Filed Testimony	Hearing Exhibit	Abbreviation
Direct Testimony of James Armstrong	S-1	Armstrong Dt.
Direct Testimony of Dorothy Hains	S-2	Hains Sb.
Surrebuttal Testimony of Dorothy Hains	S-3	Hains Sb.
Direct Testimony of John Cassidy	S-4	Cassidy Dt.
Surrebuttal Testimony of John Cassidy	S-5	Cassidy Sb.
Direct Testimony of Darron Carlson	S-6	Carlson Dt.
Surrebuttal Testimony of Darron Carlson	S-7	Carlson Sb.
Direct Testimony of Darron Carlson (Rate Design)	S-8	Carlson RD Dt.

OTHER PORTIONS OF THE RECORD

Document	Hearing Exhibit
Notice of Errata (Rebuttal Schedule H-3, page 4)	A-10
Notice of Errata (Rebuttal Schedule D-1)	A-11

1	Document	Hearing Exhibit
2	Final Settlement Agreement and Schedules	A-17
3		
4	Direct Testimony of Greg Sorensen (Arizona Water Company Rate Case)	A-18
5	Settlement Agreement (Arizona Water Company Rate Case)	A-19
6	Engineering Report (Wastewater)	A-20
7	Engineering Report (Water)	A-21
8	Draft Plan of Administration (Wastewater)	A-22
9		
10	Draft Plan of Administration (Water)	A-23
11	RUCO's Response to DR 2.8	A-24
12	Finalized Plan of Administration (Wastewater)	A-25
13	Finalized Plan of Administration (Water)	A-26
14		
15	Plan of Administration (Wastewater), dated December 10, 2013	R-4
16	Decision No. 73938	judicial notice
17	Testimony of Patrick Quinn (Arizona Water Company Rate Case)	R-8
18	Testimony of William Rigsby Quinn (Arizona Water Company Rate Case)	R-9
19		
20	RAPA Comments	R-10
21	Oct. 16, 2013 Errata	S-9
22	Oct. 21, 2013 Errata	S-10

8852404.1/035227.0022

23
24
25
26

1 LPSCO hereby submits this Reply Brief in support of its application for rate
2 increases for its water and wastewater utility divisions. The only disputed issue relates to
3 LPSCO's request for approvals of the SIB mechanisms for LPSCO's water and
4 wastewater divisions.¹ Staff and LPSCO support approval of the SIBs on the terms set
5 forth in the SIB POAs.² RUCO, however, opposes approval of the SIBs. Here, LPSCO
6 responds to RUCO's opening brief relating to the SIB approvals.

7 **I. BRIEF SUMMARY OF THE ISSUE.**

8 In Decision No. 73938 (June 27, 2013), the Commission recognized the needs for
9 the SIB mechanism and the clear public benefits of this new adjuster mechanism in terms
10 of rate gradualism, rate stability and access to capital for utilities. The Commission has
11 determined that the SIB mechanism is "compliant with the Commission's constitutional
12 requirements, as well as the case law interpreting the Commission's authority and
13 discretion in setting rates."³ Based on overwhelming evidence, the Commission
14 determined that the SIB mechanism is in the best interests of ratepayers and utilities.

15 In turn, LPSCO modeled its water and wastewater SIBs here on the AWC SIB
16 approved by the Commission in Decision No. 73938. LPSCO's SIBs are mirror images of
17 the AWC SIB and the Commission should approve the LPSCO SIBs for the same reasons
18 stated by the Commission in Decision No. 73938.⁴

19
20
21 ¹ In this reply brief, LPSCO uses the same citation format, abbreviations and conventions as utilized in its
22 initial closing brief dated January 17, 2014. Additionally, the parties' initial closing briefs will be
23 identified as "Staff Br.," "RUCO Br.," and "LPSCO Br.," respectively.

24 ² Ex. A-25; Ex. A-26; Staff Br. at 6-14.

25 ³ Decision No. 73938 at 53.

26 ⁴ Notably, ALJ Nodes recently issued the Global ROO on January 21, 2014 in which he recommends
approval of a SIB for Global Water's Willow Valley division as follows: "Consistent with our findings in
Decision Nos. 73938 and 74081, we believe that the proposed SIB mechanism incorporated therein,
together with the financial information and analysis required herein, satisfies the fair value concerns
addressed by various court decisions." Global ROO at 55. The Commission should make the same
finding for LPSCO here.

1 The record reflects that LPSCO needs over \$25 million of capital improvements to
2 its water and wastewater systems.⁵ The evidence clearly shows that the SIBs will
3 (i) enable LPSCO to meet the challenge of replacing aging infrastructure; (ii) result in
4 more gradual rate increases, as strongly preferred by ratepayers; (iii) reduce the
5 complexity of rate cases; (iv) provide a direct monetary benefit to ratepayers through the 5
6 percent efficiency credit, something that no other SIB-like mechanism has in the country,
7 and (v) keep LPSCO financially healthy with better access to capital to continue providing
8 safe and reliable water and wastewater utility services.⁶

9 In the words of author Laurence J. Peter, “[b]ureaucracy defends the status quo
10 long past the time when the quo has lost its status.” Here, RUCO continues to defend the
11 status quo by railing against the SIB mechanism as new and untraditional, and because it
12 will change rates outside of a full, general rate case.⁷ Faced with the clear and
13 unequivocal public benefits of the SIBs, RUCO resorts to its mantra that the SIB is illegal
14 and violates traditional principles of ratemaking in Arizona. RUCO regurgitates the same
15 arguments about regulatory lag, matching of operating expenses and ratepayer benefits
16 that RUCO made in the AWC Rate Case. RUCO’s own witness—Mr. Mease—
17 acknowledged that RUCO is not making any new arguments relating to the LPSCO SIBs
18 and that the Commission considered and rejected all of the arguments RUCO is making
19 here in Decision No. 73938.⁸ RUCO also didn’t make these arguments in prior cases for
20 other utilities approving adjusters similar to the proposed SIBs here.⁹

21 ⁵ Krygier Dt. at 9; Ex. A-20; Ex. A-21.

22 ⁶ Krygier Dt. at 9-15; Krygier Rb. at 21-25; Tr. at 81:1-83:5 (Krygier). In his direct and rebuttal
23 testimonies, Mr. Krygier cited an October 3, 2012 poll that showed that over 89 percent of customers
24 prefer smaller, frequent rate increases instead of larger, less frequent increases. Krygier Dt. at 4-5, Exhibit
25 CDK-DT1; Krygier Rb. at 22.

24 ⁷ RUCO Br. at 3.

25 ⁸ Tr. at 227-231. On page 231 of the transcript, Mr. Mease testified: “Q. And you would agree with me
26 that the Commission, in approving the SIB in 73938, rejected all of those arguments by RUCO,
27 didn’t they? A. Yes.”

26 ⁹ Krygier Rb. at 23-24.

1 In its brief, RUCO hopes that the Commission will change its mind and be swayed
2 by use of catch phrases like “fair value,” “regulatory lag” or “single issue” ratemaking.
3 The SIB mechanism, however, complies with all requirements under Arizona law,
4 including clearly meeting the fair value standard set forth in Article 15, § 14 of the
5 Arizona Constitution. In fact, the SIBs are specifically tailored to comply with applicable
6 Arizona legal requirements regarding ratemaking, including the fair value requirement—
7 a fact that RUCO concedes in its opening brief.¹⁰ The record demonstrates clearly that the
8 SIB is a ratemaking adjuster mechanism using FVRB to provide for the timely recovery of
9 capital costs invested by LPSCO in water and wastewater system improvement projects
10 meeting the specific criteria set forth in the POAs.¹¹ It is legal under Arizona law.

11 Henry David Thoreau once said that “it’s not what you look at that matters, it’s
12 what you see.” Here, when looking at the SIBs for LPSCO, the Commission should see
13 an adjustment mechanism benefiting both water and wastewater customers and the utility
14 through rate gradualism, improved infrastructure, improved service quality, a five percent
15 efficiency credit, and improved utility ability to attract necessary capital investment,
16 while being specifically designed to comply with all applicable Arizona ratemaking
17 laws.¹² That’s what the Commission saw in Decision No. 73938, that’s what Judge Nodes
18 saw in the Global ROO, and that’s what the Commission should see here.

19
20
21
22 ¹⁰ RUCO Br. at 10 (RUCO acknowledges that SIB Schedule D “will show an analysis of the impact of the
23 SIB/CSIB plant on the fair value rate base, revenue, and the fair value rate of return,” and further contends
24 that SIB Schedule D “was obviously put in to satisfy *Scates*, but it does not go far enough.”). *See also*
25 Krygier Rb. at 21; Staff Br. at 12.

24 ¹¹ Krygier Dt. at 4-11; Krygier Rb. at 21-25; Tr. at 84-86 (Krygier); Ex. A-25 at 5, § III(C)(6); Ex. A-26 at
25 5, § III(C)(6). The SIBs also qualify as a fair value based surcharge, another means of establishing these
26 types of rate setting mechanisms. *Residential Util. Consumer Office v. Arizona Corp. Comm’n*, 199 Ariz.
588, 589, 20 P.3d 1169, 1170 (App. 2001).

¹² Krygier Dt. at 4-11; Krygier Rb. at 21-25; Ex. A-25; Ex. A-26; Tr. at 74-77, 88-90 (Krygier).

1 **II. RATEPAYERS AND THE COMPANY DERIVE SUBSTANTIAL**
2 **BENEFITS FROM THE PROPOSED SIBS.**

3 In its brief, RUCO “opposes the SIB/CSIB mechanism because ratepayers are not
4 adequately compensated for the additional risk associated with the SIB/CSIB and because
5 it is illegal.”¹³ RUCO is not talking about business or financial risk. Rather, RUCO is
6 talking about increased rates to be paid by customers given that the SIB “reduces
7 regulatory lag in favor of LPSCO because the Company will not have to wait until new
8 rates go into effect to recover a return on SIB/CSIB eligible plant...”¹⁴ This argument
9 distorts the issue before the Commission.

10 **A. Regulatory Lag Is Not in the Public Interest.**

11 In making the argument that ratepayers lose the benefits of regulatory lag, RUCO
12 applies a distorted view of risks and benefits under the SIB mechanism. To RUCO, the
13 sole focus is manipulating regulatory lag to achieve the lowest possible water or sewer
14 rate for customers—even to the exclusion of quality service, necessary plant investment
15 and rate gradualism. For example, RUCO claims that “[r]atepayers will be paying for the
16 recovery of and return on routine plant placed into rate base in between rate cases that the
17 ratepayer would not otherwise pay until the next rate case.”¹⁵ RUCO even claims that
18 “[e]limination of regulatory lag is not in the best interests of ratepayers.”¹⁶
19 These arguments not only seek to preserve a status quo that RUCO knows benefits
20 ratepayers at the utility’s expense, but RUCO also ignores the overwhelming benefits of
21 the SIB mechanism based on the evidence in this record.

22 Unfortunately, the SIB mechanism does not eliminate regulatory lag; it only
23 partially mitigates some of its negative effects. Even with the SIB, the replaced plant is

24 ¹³ RUCO Br. at 3.

25 ¹⁴ *Id.*

25 ¹⁵ *Id.*

26 ¹⁶ RUCO Br. at 17.

1 subject to review in the utility's next general rate case, in turn forcing the utility to operate
2 efficiently and control costs. RUCO's argument that regulatory lag is beneficial seeks to
3 continue the downward spiral of impeding the Company's ability to recover its cost of
4 providing service in the misguided name of protecting the ratepayer. That position is
5 especially unjustified given the \$25 million in infrastructure needs facing LPSCO. In the
6 only public polling ever done on the issue, Arizonans for Responsible Water Policy polled
7 over 4,000 Arizonans and found that 89.4 percent preferred smaller, gradual rate increases
8 to the status quo of larger increases every few years.¹⁷ The very people RUCO claims to
9 be protecting overwhelmingly want the benefits that RUCO argues against in this case.

10 As the Commission is aware, a utility cannot generally recover costs associated
11 with replacement infrastructure until after such plant is included in rate base as part of the
12 utility's next general rate case. That lag in recovery is not beneficial to either the utility or
13 ratepayers. For utilities, regulatory lag increases borrowing costs and undercuts their
14 ability to actually earn an authorized return.¹⁸ This results in higher costs to ratepayers as
15 the higher borrowing costs are included in future rates and the utility is forced to file more
16 frequent rate cases to attempt to recoup its costs of service.¹⁹ Regulatory lag also leads to
17 larger rate increases when those costs actually are put in rates and no one enjoys "rate
18 shock."

19 In no uncertain terms, the SIBs will provide revenue to support investment in the
20 water and wastewater infrastructure replaced by the Company.²⁰ Perhaps more
21 importantly, the SIB revenue will be credit supportive, allowing LPSCO to attract the
22 capital necessary to undertake its infrastructure replacement program on more favorable
23 terms, a critical factor that RUCO hasn't addressed in its brief. RUCO's attempts to game

24 ¹⁷ Krygier Dt at 4-5, 9-13, Exhibit CDK-DT1.

25 ¹⁸ Krygier Dt. at 14-16.

26 ¹⁹ Krygier Dt. at 12-13, 15.

²⁰ *Id.*

1 the system through regulatory lag are indefensible and contrary to sound ratemaking
2 principles, the customers' own wishes, general principles of fairness and Arizona law.²¹

3 **B. The SIBs Promote Safe and Reliable Utility Service, Including Needed**
4 **Plant Improvements and Upgrades.**

5 Instead of shifting any risks to ratepayers, the SIB will result in long-term benefits
6 to ratepayers as detailed by the Company's and Staff's witnesses, and as the Commission
7 expressly determined in Decision No. 73938.²² In its brief, RUCO conveniently ignores
8 the many substantial benefits of the SIB mechanism for both customers and the utility.
9 To start, the record is undisputed that the water and wastewater SIBs promote safe and
10 reliable utility service. As testified by Mr. Krygier, DSIC-like mechanisms are "designed
11 to allow utility customers to have not only the benefits of rate gradualism, but also
12 improved system reliability, which means fewer failures and outages and a decreased risk
13 of water quality issues, while at the same time providing the utilities sufficient rate
14 recovery to make the investments required to ensure the continuous provision of safe,
15 reliable, and adequate water and sewer service."²³

16 LPSCO provided engineering reports to support the need for and benefits of the
17 SIB-Eligible Projects in terms of service quality and plant upgrades.²⁴ In contrast, RUCO
18 did not present any engineering reports or testimony.²⁵ In the AWC Rate Case, Mr. Olea

19 ²¹ Incredibly, on page 17 of its brief, RUCO argues that regulatory lag "evens out over time" because
20 although regulatory lag deprives the utility of revenue to which it is entitled, the utility will benefit
21 eventually because "[o]nce the plant has been fully depreciated, the utility still earns recovery of (and
22 recovery on) that plant until the next rate case, which may be several years past when the plant was fully
23 depreciated." In other words, RUCO believes it is okay to deprive the utility of just and reasonable rates
24 on plant through regulatory lag on the front end because the utility will be able to make those losses back
25 by charging customers for depreciation expense that the utility *is not entitled to earn* on the back end.
26 Talk about two wrongs don't make a right. The Commission should not endorse the kind of distorted
policies being suggested by RUCO, not to mention that RUCO hasn't cited any Commission decision
authorizing utilities to continue collecting depreciation expense on fully depreciated assets.

²² Decision No. 73938 at 50-54.

²³ Krygier Dt. at 8.

²⁴ Ex. A-20; Ex. A-21.

²⁵ Tr. at 234:24-235:12 (Mease).

1 emphasized that both utilities and customers benefit from increased safety and
2 reliability.²⁶ In that case, even RUCO Director Quinn agreed that “reducing the number
3 of outages for water companies is in the best interest of the residential consumer.”²⁷

4 **C. The Proposed Water and Wastewater SIBs Benefit Customers Through**
5 **Rate Gradualism.**

6 Aside from RUCO, there is widespread agreement in the utility industry that a key
7 benefit from the SIB is “rate gradualism, that is, smaller, more frequent rate adjustments
8 rather than less frequent, but much larger rate increases.”²⁸ Even Mr. Mease conceded that
9 rate gradualism is a good thing.²⁹ Utility customers strongly prefer rate gradualism.
10 As testified by Mr. Krygier, a 2012 poll of 4,000 Arizonans asked “when utility rates have
11 to go up, would you prefer: a) small annual changes, or b) large changes every few
12 years?” The results were sharply in favor of (a), with 89.4 percent preferring the gradual
13 changes.³⁰ That poll and its results are attached to Mr. Krygier’s direct testimony.³¹

14 As rate increases become more gradual, it stands to reason that the complex,
15 contested rate cases with large increases at issue will become less frequent. That is what
16 the evidence from states with DSICs suggests. For example, Pennsylvania’s DSIC
17 mechanism increased the period of time between rate case filings.³² In this case, all SIB
18 increases must be gradual because the LPSCO SIBs contain a 5 percent cap on annual SIB
19 increases.³³ That further embeds gradualism directly into the rate structure of the SIBs.

20 _____
21 ²⁶ Transcript from April 11, 2013 hearing at 304:13-22, AWC Rate Case.

22 ²⁷ Transcript from April 11, 2013 hearing at 390:18-20, AWC Rate Case.

23 ²⁸ Krygier Dt. at 4-5, 9-13, Exhibit CDK-DT1.

24 ²⁹ Tr. at 225:13-15 (“A. In your opinion, is rate gradualism a desirable thing? A. Yes.”).

25 ³⁰ Krygier Dt. at 4-5, 9-13; Tr. at 86:13-18 (“... you see for the two years that they have the data for this
26 survey, 2010 and 2011...92 percent and 85 percent of the customers preferred the smaller, more frequent
increases versus the larger, less frequent increases.”)(Krygier).

³¹ Krygier Dt. at Exhibit CDK-DT1.

³² Krygier Dt. at 7-8.

³³ Ex. A-25 at 6, § IV(A)(3); Ex. A-26 at 6, § IV(A)(3); Tr. at 167:6-18, 184:9-13 (Krygier).

1 **D. The Proposed Water and Wastewater SIBs Benefit Customers Through**
2 **Rate Stability.**

3 Logically, rate gradualism also promotes rate stability for customers. Here, the
4 SIB mechanisms promote rate stability by providing for smaller, more regularly timed
5 increases, as opposed to much larger increases that frequently occur absent such a
6 mechanism. As testified by Mr. Krygier, the SIBs promote rate stability with incremental
7 rate increases based on specific project criteria and surcharge formulas, and also “because
8 the SIB surcharge revenue is capped.”³⁴ Under the proposed POAs, the SIB surcharges
9 for both water and wastewater are capped at 5 percent of the revenue requirement,
10 meaning that rates will not increase above that cap in any given year.³⁵

11 In its brief, RUCO turns the concept of rate stability on its head by arguing that the
12 SIBs will result in rate instability because rates may increase each year with a SIB.³⁶ The
13 gist of RUCO’s argument is that regulatory lag under traditional ratemaking promotes rate
14 stability by delaying implementation of rate increases during the regulatory process. That
15 thinking is both shortsighted and self-defeating because the immediate consequence of
16 regulatory lag is lost revenue for the utility, in turn resulting in more rate cases with
17 greater rate increases.³⁷ RUCO has it exactly backwards on this issue—the current
18 practice of frequent rates cases seeking substantial rate increases doesn’t promote rate
19 stability in any way, shape or form.³⁸

20 In approving the inclusion of CWIP in the determination of fair value, the Arizona
21 Supreme Court acknowledged that rate stability does not occur under the traditional
22

23 ³⁴ Tr. at 167:6-18 (Krygier).

24 ³⁵ Ex. A-25 at 6, § IV(A)(3); Ex. A-26 at 6, § IV(A)(3); Tr. at 167:6-18 (Krygier); Tr. at 184:9-13
(Krygier).

25 ³⁶ RUCO Br. at 4.

26 ³⁷ Krygier Dt. at 5-13, 15; Tr. at 127:6-25 (Krygier);

³⁸ *Id.*

1 system of constant rate cases:

2 We would not presume to instruct the Commission as to how it should
3 exercise its legislative functions. *However, it appears to be in the public*
4 *interest to have stability in the rate structure within the bounds of fairness*
*and equity rather than a constant series of rate hearings.*³⁹

5 That's exactly what the SIB does—it provides stable rates through gradual rate increases
6 using a set surcharge formula with a cap on the surcharge amount, rather than an irregular
7 series of rate cases with large plant additions requiring substantial rate increases.⁴⁰

8 **E. The Efficiency Credit Is a Direct Monetary Benefit to Both Water and**
9 **Wastewater Customers.**

10 One extraordinary feature and benefit of the SIB is the 5 percent efficiency credit.
11 No other DSIC or DSIC-like mechanism—in any state—has a direct monetary benefit for
12 customers like the efficiency credit. Mr. Krygier explained that the efficiency credit is
13 “a direct customer monetary benefit” allowing customers to “get a discount on the
14 ultimate revenue requirement that’s calculated from the capital projects.”⁴¹ Mr. Krygier
15 went on to explain that the efficiency credit is “forever lost” and never recouped by
16 LPSCO.⁴² No other adjuster in Arizona has any similar monetary give back to customers.

17 Even so, RUCO contends that the 5 percent efficiency credit is inadequate
18 compensation for reduced regulatory lag.⁴³ RUCO’s arguments on this point are
19 unsupported and internally contradictory for several reasons. First, the Commission
20

21 _____
22 ³⁹ *Ariz. Corp. Comm’n v. Ariz. Pub. Serv. Co.*, 113 Ariz. 368, 371, 555 P.2d 326 (1976).

23 ⁴⁰ It also bears emphasis that in LPSCO’s last rate case, “[t]he Commission was very critical of LPSCO for
24 having put too much plant in while staying out too long between rate cases, creating the need for a large
increase. In fact, the Commission penalized LPSCO for it by reducing its return on equity at LPSCO’s
prior rate case.” Krygier Dt. at 5. Given that prior Commission decision and absent approval of the SIBs
here, LPSCO will have no choice but to file frequent rate increases.

25 ⁴¹ Tr. at 174:2-21.

26 ⁴² Tr. at 175:19-22.

⁴³ RUCO Br. at 3-4.

1 considered and rejected that argument in Decision No. 73938.⁴⁴ There, the Commission
2 approved the AWC SIB, including the 5 percent efficiency credit and rejected the same
3 objections by RUCO that RUCO is presenting here.⁴⁵ The underlying record necessitates
4 the same result here.

5 Second, RUCO presupposes that the purpose of the efficiency credit is to simulate
6 regulatory lag. On this record, the efficiency credit is not a surrogate or proxy for
7 regulatory lag. Rather, as explained by Mr. Krygier, it is a “100 basis point reduction in
8 the ROE, the most significant customer benefit in the country” and “as Mr. Olea has
9 recently testified, this cost savings is the equivalent of another mechanism that might
10 attempt to track cost savings.”⁴⁶ Put simply, the efficiency credit is a way to track and
11 account for potential cost savings resulting from reduced operating expenses from the
12 replacement infrastructure installed through the SIBs.⁴⁷

13 Third and finally, as a matter of law, the notion of artificially imposing a blanket
14 reduction in revenue as a proxy for lost regulatory lag would be patently illegal and unfair
15 under the constitutional requirements of both *Bluefield Water Works* and *Hope Natural*
16 *Gas*, requiring the Commission to set rates that allow for the recovery of costs, including
17 service on debt and appropriate returns on equity.⁴⁸

18 Perhaps recognizing the fatal flaws in those arguments, RUCO shifts gears and
19 contends that the 5 percent efficiency credit is not enough because it will be dwarfed by
20

21 _____
⁴⁴ Decision No. 73938 at 38.

22 ⁴⁵ Decision No. 73938. at 38-41, 55-57.

23 ⁴⁶ Krygier Rb. at 22, citing Rehearing Testimony of Steven M. Olea (filed Oct. 4, 2013), AWC Rate Case,
at 8:1-7.

24 ⁴⁷ See Rehearing Testimony of Steven M. Olea, AWC Rate Case, at 8:1-7. Tr. at 174:2-25 (Krygier).
25 Although the efficiency credit is not designed to be a proxy for regulatory lag, it relates to the effects of
regulatory lag by providing a revenue reduction for customers.

26 ⁴⁸ *Bluefield Water Works and Improvement Co. v. Public Serv. Comm 'n of West Virginia*, 262 U.S. 679,
693 (1923); *Federal Power Comm 'n v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944).

1 LPSCO's reduced operating expenses resulting from the replaced infrastructure.⁴⁹
2 At hearing, however, Mr. Mease admitted on cross-examination that he does not know
3 whether LPSCO will have any "cost savings" from the SIB mechanism.⁵⁰
4 Given Mr. Mease's testimony, RUCO's argument that the cost savings from SIB plant
5 will be greater than the efficiency credit is nothing more than unsupported speculation and
6 conjecture. Put simply, RUCO can't point to any evidence in the record to support its
7 argument.

8 **F. The Proposed SIBs Benefit Water and Wastewater Customers Through**
9 **Financial Stability and Increased Utility Ability to Attract Capital.**

10 Banks and bondholders aren't going to lend money for replacement infrastructure
11 just because a utility needs it. But a SIB will make LPSCO more attractive for capital
12 investment.⁵¹ With the SIB, "LPSCO will have a more fair and adequate opportunity to
13 earn its authorized rate of return. That's good for business too because it allows us to pay
14 a fair return and continue to attract necessary capital."⁵²

15 By improving earnings and cash flow, the SIBs will protect the utility's financial
16 integrity, and thus its ability to raise funds. As testified by Mr. Krygier, LPSCO
17 anticipates "over \$25M of improvements needed to ensure continued system reliability"
18 for its water and wastewater divisions.⁵³ As recognized by the Commission in
19 Decision No. 73938, the proposed SIBs allow for more gradual rate changes while
20 enabling utilities to raise the funds they need.⁵⁴ That's absolutely true here, as well.

21
22 ⁴⁹ RUCO Br. at 4.

23 ⁵⁰ Tr. at 229:3-21 (Mease)("Q. [Y]ou don't know for certain that any SIB plant, once installed, will result
24 in cost savings, do you? That's just a guess? A. No, not within the - it could or it couldn't. Q. Which I
25 guess my question is you don't know for sure. A. I don't know for sure.").

26 ⁵¹ Krygier Dt. at 12-15.

⁵² *Id.*

⁵³ Krygier Dt. at 9.

⁵⁴ Decision No. 73938 at 49-54.

1 **III. THE PROPOSED SIBS ARE LEGAL AND COMPLY WITH ARIZONA'S**
2 **FAIR VALUE REQUIREMENT.**

3 The overriding theme of RUCO's brief is that RUCO opposes the water and
4 wastewater SIBs because they are new adjusters deviating from traditional ratemaking.
5 As the Commission determined in Decision No. 73938, however, the LPSCO SIBs are a
6 type of adjustment mechanism that is lawful in Arizona.⁵⁵

7 **A. The SIB is A Lawful Adjuster Mechanism.**

8 On page 5 of its brief, RUCO argues that the SIB is not an adjuster mechanism.
9 RUCO claims that a single phrase in *Scates* somehow limits Arizona adjusters strictly to
10 "narrowly defined, operating expenses."⁵⁶ But RUCO's attempt to wield *Scates* like a
11 sword must fail. On its terms, that statement in *Scates* explains the traditional use of
12 automatic adjustment mechanisms "to permit rates to adjust automatically, either up or
13 down, in relation to fluctuations in certain, narrowly defined operating expenses."⁵⁷
14 That statement doesn't prohibit or exclude other types of valid adjuster mechanisms in
15 Arizona. *Scates* is not a sword to be used to slice apart Commission rate orders; it is a
16 shield protecting rate orders that follow the constitutional "fair value" requirement.

17 Here, the SIB is a plant-based adjuster mechanism. *Scates* did not involve a plant-
18 based adjuster mechanism and, therefore, this stray remark from *Scates* doesn't address,
19 let alone preclude, plant-based adjusters. In *Scates*, the Court of Appeals found the
20 Commission acted unlawfully when it changed rates "without any examination of the
21 costs of the utility apart from the affected services, without any determination of the
22 utility's investment, and without any inquiry into the effect of this substantial increase
23

24 ⁵⁵ Decision No. 73938 at 52.

25 ⁵⁶ RUCO Br. at 5, citing *Scates v. Arizona Corp. Comm'n*, 118 Ariz. 531, 535, 578 P.2d 612, 616
(App. 1978).

26 ⁵⁷ *Scates*, 118 Ariz. at 535, 578 P.2d at 616.

1 upon [the utility's]...rate of return on that investment.”⁵⁸ The court’s *holding* was that the
2 Commission “is required by our Constitution to ascertain the value of a utility’s property
3 within the State in setting just and reasonable rates.”⁵⁹

4 *Scates* doesn’t even remotely prohibit plant-based adjusters. Rather, *Scates* allows
5 ratemaking adjuster mechanisms as long as the mechanism is approved in a general rate
6 case and comports with Arizona’s fair value requirement in Article 15, § 14 of the
7 Arizona Constitution.⁶⁰ On its terms, the proposed SIBs meet the fundamental
8 requirements of *Scates*—“when courts have upheld automatic adjustment provisions, they
9 have generally done so because the clauses are initially adopted as part of the utility’s rate
10 structure in accordance with all statutory and constitutional requirements and, further,
11 because they are designed to insure that, through the adoption of a set formula geared to a
12 specific readily identifiable cost, the utility’s profit or rate of return does not change.”⁶¹

13 LPSCO’s SIBs satisfy both elements of *Scates* because LPSCO seeks approval of
14 the SIBs in a general rate case, the Commission will make a fair value finding in setting
15 rates, the SIBs require an evaluation and finding of fair value as part of the required SIB
16 filings and the SIB rate of return is limited to that approved by the Commission in this
17 case. Here, the LPSCO SIBs do all of the things absent in *Scates* because each SIB
18 surcharge order will be based on an analysis of the impact of the SIB plant on the fair
19 value rate base, revenue, and the fair value rate of return.⁶²

20 Boiled down, the SIB is an adjuster mechanism, as Mr. Olea testified in the AWC
21 case⁶³ and the Commission determined in Decision No. 73938 that the AWC SIB “is an
22

23 ⁵⁸ *Id.* at 533, 578 P.2d at 614.

24 ⁵⁹ *Id.* at 534, 578 P.2d at 615.

25 ⁶⁰ *Id.* at 535, 578 P.2d at 616.

26 ⁶¹ *Id.* (citations omitted).

⁶² Tr. at 84-86, 106-109 (Krygier).

⁶³ Transcript from April 11, 2013 hearing at 297:21 – 298:3, AWC Rate Case.

1 adjustment mechanism established within a rate case as part of a company's rate
2 structure..."⁶⁴ Moreover, the SIB is a type of DSIC, and the courts in Pennsylvania have
3 recognized that DSICs are adjuster mechanisms.⁶⁵ The SIB also meets the definition of
4 adjusters used in many ratemaking authorities and treatises.⁶⁶ On this record, the
5 Commission should make the same finding for LPSCO's SIBs here.⁶⁷

6 **B. Plant-Based Adjusters Are Legal In Arizona and the Commission Has**
7 **Approved and RUCO Has Supported Numerous Plant-Based Adjusters**
8 **for Other Utilities.**

9 In Arizona, there is no textual basis in the Arizona Constitution for a supposed
10 prohibition of plant costs in adjuster mechanisms. Arizona law doesn't limit valid
11 adjusters to operating expenses by any stretch of the imagination. To the contrary, as long
12 ago as 1979, in *Arizona Community Action Association v. Arizona Public Service*
13 *Company*, the Arizona Supreme Court recognized that step increases based on post-test
14 year construction work in progress would be lawful.⁶⁸

14 ⁶⁴ Decision No. 73938 at 52. In that decision, the Commission further stated that "[t]he SIB is a different
15 type of adjuster mechanism than has been previously been reviewed by the courts because it allows
16 recovery of plant costs associated with AWC's substantial distribution system improvement needs, rather
17 than fuel costs." Decision No. 73938 at n. 39.

18 ⁶⁵ See *Popowsky v. Pennsylvania Pub. Util. Comm'n*, 869 A.2d 1144, 1158 (Pa. Comm. Ct. 2005) ("water
19 utilities may recover certain capital costs through an automatic adjustment clause in its tariff" and treating
20 a DSIC for water as an automatic adjustment clause).

21 ⁶⁶ See, e.g., Morin, *New Regulatory Finance* (2006) at 556 (defining adjusters relative to costs and noting
22 that "[u]nder this style of regulation, an automatic adjustment factor is applied to individual cost
23 components that are outside the control of management."); 73B C.J.S. Public Utilities § 120 ("Approval by
24 a public utility regulatory commission of tariff provisions for automatic adjustments in rates according to a
25 predetermined formula, without the necessity for proceedings by the commission whenever specified costs
26 of the utility change by a certain amount, may be permissible."); 16 U.S.C. § 824d(f)(4) ("As used in this
subsection, the term "automatic adjustment clause" means a provision of a rate schedule which provides
for increases or decreases (or both), without prior hearing, in rates reflecting increases or decreases
(or both) in costs incurred by an electric utility...").

⁶⁷ In the Global ROO, Judge Nodes determined that "The SIB mechanism also addresses the concerns
cited in *Scates* in that the SIB: is an adjustment mechanism established within a rate case as part of a
company's rate structure; adopts a set formula that would allow only readily identifiable and narrowly
defined plant to be recovered through the surcharge; and will apply the rate or return authorized herein to
SIB plant (less the five percent efficiency credit)." Global ROO at 56-57.

⁶⁸ *Arizona Community Action Assoc. v. Arizona Public Service Co.*, 123 Ariz. 228, 231, 599 P.2d 184
(1979) (noting "The adjustments ordered by the Commission in adding the CWIP to that determination of
fair value were adequate to maintain a reasonable compliance with the constitutional requirements if used

1 RUCO's attempt to confine adjusters strictly to operating expenses is flatly
2 inconsistent with numerous adjuster mechanisms approved by the Commission that
3 included plant costs – many done with RUCO's agreement and active support.⁶⁹
4 During the AWC rate case, there was extensive testimony regarding the history of APS's
5 RES, EE/DSM and EIS mechanisms.⁷⁰ Each of those is an adjuster mechanisms and each
6 includes (or has in the past included) recovery of capital costs for utility plant investment,
7 just like the SIB mechanisms here.⁷¹ RUCO's support for those plant-based adjusters
8 contradicts and refutes its SIB objections here.

9 The SIB mechanism also is very similar to the ACRM approved by the
10 Commission in many past cases—another plant-based adjuster.⁷² As the Commission
11 noted in Decision No. 73938, “[f]rom a practical perspective, the SIB would operate very
12 similarly to the existing ACRM, with which the Commission now has extensive
13 experience, and which the Commission has determined to be lawful.”⁷³ If the ACRM is
14 lawful, so is the SIB.

15 Perhaps the best example of a plant-based adjuster similar to the proposed SIBs is
16 the Commission's approval of APS's EIS in Decision No. 73183 (May 24, 2012)
17 discussed in detail in LPSCO's opening brief.⁷⁴ Conspicuously absent from RUCO's
18 brief is any discussion of the APS EIS. RUCO's failure to address the EIS is telling.

19
20 only for a limited period of time.”). *See also* Decision No. 73938 at 42-43 (discussing *Arizona Community*
Action in the context of a SIB).

21 ⁶⁹ *See* Krygier Dt. at 10-11.

22 ⁷⁰ *E.g.*, Re-hearing Direct Testimony of Paul Walker (filed Oct. 4, 2013), AWC Rate Case, at 4-5.

23 ⁷¹ *Id.*; Krygier Dt. at 10-11.

24 ⁷² For past decisions approving ACRMs, *see e.g.* Decision No. 66400 (Oct. 14, 2003)(AWC Northern
25 Group)(extensively discussing legality of ACRM); Decision No. 66849 (March 19, 2004)(AWC Eastern
26 Group); Decision No. 68310 (Nov. 14, 2005)(approving ACRM for certain districts of Arizona-American
Water Co.); Decision No. 71236 (August 6, 2009)(Appaloosa Water Co.); Decision No. 71410 (Dec. 8,
2009)(extending ACRM for Arizona-American Water Company to additional district).

⁷³ Decision No. 73938 at 50.

⁷⁴ LPSCO Br. at 19-22.

1 That EIS mechanism was approved in accordance with a settlement agreement signed by
2 APS, Staff, RUCO and various other parties on or about January 6, 2012 without any
3 challenge to that surcharge's legality.⁷⁵ The EIS and SIBs are materially identical adjuster
4 mechanisms. In fact, the SIBs actually contain an additional customer benefit through the
5 efficiency credit, which is not included in the EIS. All of RUCO's legal arguments in its
6 brief are contradicted by approval of the APS EIS because both the SIB and EIS provide a
7 return on utility investment in plant based on each company's WACC as approved by the
8 Commission in each company's recent general rate case.⁷⁶ If the EIS is legal, so are the
9 LPSCO SIBs.

10 **C. The Proposed SIBs Comply With Arizona's Fair Value Requirement.**

11 On pages 9-12 of its brief, RUCO argues that the SIBs will effectively increase
12 FVRB without any determination by the Commission of "fair value."⁷⁷ In making that
13 argument, RUCO argues that "[t]he Commission, however, will not be making a new
14 FVRB finding as part of each surcharge filing..."⁷⁸ RUCO then argues that such analysis
15 will increase "fair value rate base without a meaningful consideration of fair value."⁷⁹
16 RUCO doesn't cite any cases or persuasive legal authority, instead urging the
17 Commission to go beyond what the Arizona Constitution and case law requires.⁸⁰

18 RUCO is mistaken both factually and legally on these issues. Factually speaking,
19

20 ⁷⁵ Decision No. 73183, Exhibit A.

21 ⁷⁶ *Id.*

22 ⁷⁷ RUCO Br. at 9.

23 ⁷⁸ *Id.*

24 ⁷⁹ *Id.*

25 ⁸⁰ It appears that RUCO may have borrowed the arguments raised in comments by RAPA relating to a
26 proposed PRISM for water and wastewater utilities in Alaska. In Exhibit R-10, RAPA submitted
comments, arguing that the proposed PRISM "is structured in a way that will deprive the Commission and
any interested person from testing included cost items in a meaningful way." Ex. R-10 at 5. RAPA also
argued that the "proposed procedure also appears unlikely to result in meaningful review." Ex. R-10.
at 30. Obviously, RUCO's attempt to use the RAPA comments to create a new Arizona constitutional
requirement for fair value should be rejected. See also Section III(G), *infra*.

1 RUCO is mistaken when it argues that the Commission “will not be making a new FVRB
2 finding as part of each surcharge filing.” That is wrong under the terms of the SIBs and
3 POAs. As set forth on SIB Schedule D, and as testified by Mr. Krygier at hearing,
4 the SIB mechanism requires a finding of FVRB with each SIB filing for the Company as
5 established in this rate case plus SIB plant, along with the rate of return as applied to that
6 FVRB and associated revenue.⁸¹

7 On its plain terms, the SIB mechanism requires the evaluation and consideration of
8 FVRB relating to any SIB filing and approved surcharge. As the Arizona Supreme Court
9 explained in *Simms*, “[w]hile our constitution does not establish a formula for arriving at
10 fair value, it does require such value to be found and used as the base in fixing rates.
11 The reasonable and justness of the rates must be related to this finding of fair value.”⁸²
12 “Fair value means the value of properties at the time of inquiry.”⁸³ Here, the SIBs require
13 a determination of the fair value of the Company’s rate base along with the SIB plant at
14 the time that the surcharges are proposed.⁸⁴

15 As a matter of law, neither the Arizona Constitution nor any Arizona cases require
16 the Commission to make the type of “meaningful finding of fair value” urged by RUCO.
17 Instead, all the Constitution requires is that the Commission determine and consider fair
18 value in setting rates or approving a mechanism like the SIB. The Arizona Supreme
19 Court’s decision in *US West Comm., Inc. v. Arizona Corp. Comm’n*, is clear:

21 ⁸¹ Tr. at 84:17 – 85:5 (Krygier).

22 ⁸² *Simms v. Round Valley Light & Power Co.*, 80 Ariz. 145, 151, 294 P.2d 378, 382 (1956).

23 ⁸³ *Simms*, 80 Ariz. at 151, 294 P.2d at 382 (internal citation omitted). See also *Consolidated Water*
24 *Utilities, Ltd., v. Arizona Corp. Comm’n*, 178 Ariz. 478, 482 n. 6, 875 P.2d 137, 141 n. 6 (App. 1993)
25 (“The fair value rate base is the fair value of the company’s properties within the state at the time the rate
26 is fixed.”); *Los Angeles Gas & Electric*, 289 U.S. at 305 (a utility is entitled to “a fair return upon the
reasonable value of the property at the time it is being used for the public”); *Southwestern Bell*, 262 U.S. at
286 (“[T]he value of the property is to be determined as of the time when the inquiry is made regarding
the rates.”), quoting *Willcox v. Consol. Gas Co.*, 212 U.S. 19, 52 (1909).

⁸⁴ Ex. A-25 at 4-5, § III(C); Ex. A-26 at 4-5, § III(C); Tr. at 84:17-85:5 (Krygier).

1 ...But while the Constitution clearly requires the Arizona Corporation
2 Commission to perform a fair value determination, only our jurisprudence
3 dictates that this finding be plugged into a rigid formula as part of the rate-
4 setting process. *Neither section 3 nor section 14 of the constitution*
5 *requires the corporation commission to use fair value as the exclusive rate*
basis...In this and any other fashion that the corporation commission
deems appropriate, the fair value determination should be considered.
The commission has broad discretion, however, to determine the weight to
*be given this factor in any particular case.*⁸⁵

6 *Phelps Dodge Corp. v. Arizona Corp. Comm'n* echoes those sentiments: "...consistent
7 with the pronouncement in *US West II*...the Commission should consider fair value when
8 setting rates within a competitive market, although the Commission has broad discretion
9 in determining the weight to be given that factor in any particular case."⁸⁶

10 Likewise, the Commission has broad discretion in setting rates, including
11 consideration and use of various ratemaking mechanisms as long as the method complies
12 with the fair value mandate set forth in Article 15, § 14.⁸⁷ Put simply, the Commission
13 has discretion to adopt mechanisms necessary to address particular ratemaking issues,
14 including matters subsequent to an historic test year,⁸⁸ construction projects contracted
15 and commenced during the test year,⁸⁹ and construction work in progress but not yet in
16 service.⁹⁰ Further, the Commission may adopt interim rates or automatic adjustment
17 mechanisms without first determining fair value rate base.⁹¹

18 As a matter of law, therefore, the SIB mechanism at issue here falls within the
19 Commission's broad discretion and is consistent with these prior decisions and approved
20 ratemaking methods. In this rate case, the Commission will determine the "fair value" of
21

22 ⁸⁵ 201 Ariz. 242, 244-245, 34 P.3d 351, 353-355 (2001) (emphasis added).

23 ⁸⁶ 207 Ariz. 95, 107, 83 P.3d 573, 585 (App. 2004).

24 ⁸⁷ *Arizona Corp. Comm'n v. Arizona Pub. Serv. Co.*, 113 Ariz. 368, 555 P.2d 326 (1976); *Arizona Cmty.*
Action Ass'n v. Arizona Corp. Comm'n, 123 Ariz. 228, 599 P.2d 184 (1979).

25 ⁸⁸ *Arizona Pub. Serv.*, 113 Ariz. at 371.

26 ⁸⁹ *Id.*

⁹⁰ *Arizona Cmty. Action*, 123 Ariz. at 230, 599 P.2d at 186.

⁹¹ *RUCO v. Arizona Corp. Comm'n*, 199 Ariz. 588, 20 P.2d 1169 (App. 2011).

1 LPSCO's rate base. Any SIB surcharge will, in turn, be based on specific infrastructure
2 added to that approved rate base and proven to be used and useful. LPSCO is required to
3 file annual summary schedules itemizing the actual cost of constructing such SIB plant
4 with supporting documents, along with FVRB information sufficient for the Commission
5 to determine how the proposed SIB surcharges will impact the Company's rate of return.⁹²

6 Only RUCO believes these findings and analyses are meaningless.

7 **D. The SIB Is Not Single Issue Ratemaking.**

8 In its brief, RUCO twists its fair value argument by claiming that the Commission
9 will not make a meaningful fair value finding because the Commission "will not consider
10 other expenses and revenues in the calculation."⁹³ In this argument, RUCO seemingly
11 concedes that the Commission will determine fair value with each SIB filing, but contends
12 that such finding will be meaningless by failing to consider current operating expenses.
13 RUCO then morphs its argument into a claim that "[t]he SIB/CSIB mechanism is single
14 issue ratemaking; it is not fair value ratemaking."⁹⁴ Unfortunately, RUCO mixes up the
15 issues. The issue of considering operating expenses during the test year does not have any
16 impact on a finding of FVRB for LPSCO. FVRB is not contingent on operating
17 expenses—it is based on the fair value of used and useful plant/property.⁹⁵

18 As to RUCO's claim of piecemeal or single issue ratemaking, that argument can be
19 readily rejected because the SIBs are part of the Company's ongoing general rate case as
20 determined by the Commission. The SIB mechanism will be approved in the Company's
21 general rate case, authorizing the Company to implement the surcharge in the years before
22 the Company's next general rate case. On its own terms, the SIB mechanisms are linked

23 ⁹² *Scates*, 118 Ariz. 535, 578 P.2d at 616.

24 ⁹³ RUCO Br. at 9.

25 ⁹⁴ RUCO Br. at 11.

26 ⁹⁵ Ariz. Const. Art. 15, § 14 ("The corporation commission shall, to aid it in the proper discharge of its duties, ascertain the fair value of the property within the state of every public service corporation doing business therein...").

1 to the Company's general rate case by requiring that the rate of return, depreciation rates
2 and gross revenue conversion factor approved by the Commission be applied to any SIB
3 filings. That is not determination of rates outside of a rate case or piecemeal ratemaking
4 in any way, shape or form.

5 On pages 3-4 of its brief, RUCO claims "the operating expenses associated with
6 the SIB/CSIB plant as well as the other rate case elements normally considered in a rate
7 case will not be factored into the [SIB] calculation." In turn, RUCO argues that "[t]his
8 mismatch works against the ratepayer's interests and assures that ratepayers will not pay
9 their actual cost of service and will pay more over time."⁹⁶ RUCO's claim that the SIBs
10 do not consider current operating expenses with each SIB filing and that customers will
11 pay more over time is illusory and utter speculation for four reasons.

12 First and foremost, RUCO did not offer any evidence that LPSCO's operating
13 expenses will decrease or change significantly with installation of the SIB plant. As noted
14 above, Mr. Mease testified that he doesn't know whether operating expenses will actually
15 decrease with installation of the SIB plant.⁹⁷ Second, the SIBs would be approved as part
16 of LPSCO's rate design in a general rate case, which includes the necessary evaluation
17 and approval of operating costs going forward. No Arizona law, statute or case requires
18 that a fair value determination include the added cost analysis urged by RUCO.

19 Third, the 5 percent efficiency credit accounts for some potential changes in
20 operating expenses. As testified by Mr. Krygier, "it is very hard to quantify cost savings
21 resulting from new plant improvements. Power costs may go down because of new plant
22 that is more efficient but the costs for power may go up. Water loss may be reduced
23 reducing line maintenance costs, but maintenance of other plant may result in the same
24 test year cost. This is why the proposed SIB includes a 100 basis point reduction in the

25 ⁹⁶ RUCO Br. at 3.

26 ⁹⁷ Tr. at 229:3-21.

1 ROE, the most significant customer benefit in the country.”⁹⁸ Put simply, the 5 percent
2 efficiency credit accounts for and credits customers for potential savings in operating
3 expenses, even if those cost savings do not materialize or can’t be tracked in actuality.

4 Finally, the POAs require a detailed earnings test, including an evaluation of
5 operating income, costs and expenses.⁹⁹ At hearing, Mr. Mease acknowledged that
6 “as part of the earnings test, the company would also submit information regarding any
7 adjustments made to the operating revenue and expense adjustments...”¹⁰⁰ On its terms,
8 the earnings test shall be “a) based on the most recent available operating income, b)
9 adjusted for any operating revenue and expense adjustments adopted in the most recent
10 rate case.”¹⁰¹ By definition, determining “the actual rate of return reflected by the
11 operating income for the affected system” involves consideration of current operating
12 expenses in the year of the earnings test.¹⁰² An evaluation of the Company’s “most recent
13 available operating income” obviously accounts for the Company’s most recent operating
14 expense.¹⁰³ As such, RUCO’s argument that the SIB filings do not consider actual
15 operating expenses is unsupported and meritless.

16 **E. Alternatively, the SIB Is a Valid and Lawful Surcharge Mechanism.**

17 As expressly stated by the Commission in Decision No. 73938, the SIB is a
18 different type of adjuster mechanism designed around recovery of the costs of plant
19 investment in system improvements.¹⁰⁴ Under these circumstances, the SIBs are a lawful
20 adjuster mechanism under *Scates* and Arizona case law for the reasons stated above.

21 ⁹⁸ Krygier Rb. at 22-23.

22 ⁹⁹ Ex. A-25 at 7-8, § IV(C); Ex. A-26 at 7, § IV(C).

23 ¹⁰⁰ Tr. at 223:13-22 (Mease).

24 ¹⁰¹ Ex. A-25 at 7-8, § IV(C)(2); Ex. A-26 at 7-8, § IV(C)(2).

25 ¹⁰² Ex. A-25 at 7, § IV(C)(1); Ex. A-26 at 7, § IV(C)(1).

26 ¹⁰³ A perfect illustration is the Commission’s Utility Annual Report form for water and sewer utilities. Page 8 of that Commission form is the “Comparative Statement of Income and Expenses,” including calculation of “Operating Income/(Loss)” based on Total Revenues minus Total Operating Expenses.

¹⁰⁴ Decision No. 73938 at 52.

1 If the Commission were to change its mind and determine that the SIBs are not
2 adjuster mechanisms, they still are lawful ratemaking surcharges authorizing rate
3 increases based on a determination and evaluation of the Company's FVRB.¹⁰⁵
4 Under *RUCO v. Arizona Corp. Comm'n*, the Commission is authorized to impose rate
5 surcharges for specific costs if the Commission first determines and considers the utility's
6 FVRB.¹⁰⁶ There, the Court explained: "We hold that in the absence of an emergency or
7 automatic adjustment clause, the Arizona Corporation Commission cannot impose a rate
8 surcharge based on a specific cost increase without first determining a utility's fair value
9 rate base."¹⁰⁷ Thus, there are three separate methods for modifying rates outside of a rate
10 case: (1) as part of an adjuster mechanism approved in a rate case; (2) as part of an
11 emergency; or (3) as a rate surcharge *with* a fair value finding.

12 Even if the SIB mechanism for some reason is not considered an adjuster
13 mechanism, it is a valid surcharge mechanism under *RUCO v. ACC* because each
14 surcharge order will include a fair value finding. It is beyond dispute that the SIBs require
15 a finding of fair value before the Commission can approve the SIB surcharge.

16 RUCO's claim that the SIBs somehow expose customers to unnecessary rate
17 increases also is complete hyperbole. The ratemaking terms, conditions and protections
18 set forth in LPSCO's POAs prevent that from happening. For starters, the SIBs would be
19 approved in the Company's general rate case, authorizing the Company to implement the
20 surcharge in the years before the Company's next general rate case.¹⁰⁸ The SIBs require
21 that the rate of return, depreciation rates and gross revenue conversion factor approved by
22 the Commission here be applied to any SIB filings.¹⁰⁹ Further, SIB plant is subject to a

23 _____
¹⁰⁵ *RUCO v. Ariz. Corp. Comm'n*, 199 Ariz. at 589, 20 P.3d at 1170.

24 ¹⁰⁶ *Id.*

25 ¹⁰⁷ *Id.*

26 ¹⁰⁸ Ex. A-25 at 2, § I; Ex. A-26 at 2, § I.

¹⁰⁹ Ex. A-25 at 6, § IV(A); Ex. A-26 at 6, § IV(A).

1 detailed review as part of this rate case before a project is included on the list of SIB-
2 Eligible Plant, and then a subsequent review prior to any surcharges.¹¹⁰

3 The extensive protections contained in the POAs don't stop there. As noted, the
4 five percent efficiency credit is deducted from the SIB revenue requirement, directly
5 reducing the SIB revenue requirement and effectively reducing the return on equity for
6 plant investments under the SIBs, in turn further assuring that LPSCO's rate of return
7 does not increase.¹¹¹ And, of course, the SIBs require reconciliation and true-up of any
8 and all amounts collected.¹¹²

9 **F. RUCO Does Not State Any Persuasive Reason for Rejecting the**
10 **Wastewater SIB.**

11 On pages 13-15 of its brief, RUCO opposes the wastewater SIB for two reasons.
12 First, RUCO claims that the wastewater SIB is different from the water SIB. Second,
13 RUCO opposes the wastewater SIB because it's the first one of its kind requested by an
14 Arizona utility. Specifically, RUCO claims that the wastewater SIB "is not the result of a
15 collaborative effort of the wastewater industry and appears to have been put together
16 hastily."¹¹³ These arguments are meritless on all accounts.

17 The adoption of the SIB mechanisms reflects a Commission policy that fosters
18 investment in plant and promotes rate gradualism, rate stability and utility access to
19 capital. RUCO doesn't offer any persuasive reason for discriminating against sewer
20 customers relative to water customers in approving such an important ratemaking tool.
21 If the SIB for wastewater meets the same criterion as the SIB for water, then there is no
22 basis for approving one and not the other.¹¹⁴

23 _____
24 ¹¹⁰ Ex. A-25 at 3-4, § III; Ex. A-26 at 3-4, § III; Tr. at 199:25-200:14 (Hains).

25 ¹¹¹ Ex. A-25 at 6, § IV(A)(1); Ex. A-26 at 6, § IV(A)(1).

26 ¹¹² Ex. A-25 at 7, § IV(B)(1); Ex. A-26 at 6-7, § IV(B)(1).

¹¹³ RUCO Br. at 13.

¹¹⁴ Krygier Rj. at 7; Staff Br. at 14.

1 RUCO's justifications for its opposition to the wastewater SIB are meritless.
2 To start, RUCO differentiates the wastewater SIB from the water SIB because the
3 "NARUC accounts for water and wastewater infrastructure are different – perhaps
4 because the infrastructure itself is, for the most part, different."¹¹⁵ No kidding. It goes
5 without saying that wastewater collection pipes and infrastructure are different than water
6 distribution pipes and infrastructure. Fortunately for all of us, utilities don't use the same
7 pipes to deliver water as they do to collect raw sewage. Nevertheless, all of the benefits
8 and needs for the SIB mentioned above apply just as equally and fully to wastewater
9 infrastructure as water.

10 Further, the testimony provided by Mr. Krygier fully supports and establishes the
11 needs for and benefits of the wastewater SIB.¹¹⁶ As established at hearing, wastewater
12 pipes and water pipes both leak and degrade over time, necessitating capital
13 improvements.¹¹⁷ DSIC like adjuster mechanisms are not based on a specific type of pipe
14 or a specific NARUC account number; rather, they are based on concepts of rate
15 gradualism and rate stability relating to utility costs, and the desire to foster necessary
16 infrastructure replacement. As testified by Mr. Krygier, "the needs of a water SIB to
17 replace leaky pipe, sewer pipe leaks as well. So there are many similarities between the
18 two" and "the challenges of the water industry and the wastewater are similar in
19 nature."¹¹⁸ Even worse, leaking wastewater pipes pose a public health hazard and are one
20 of the "underlying reason for the wastewater SIB."¹¹⁹ Mr. Mease agreed that wastewater

21 ¹¹⁵ RUCO Br. at 13.

22 ¹¹⁶ Krygier Dt. at 4-15; Krygier Rb. at 21-25; Krygier Rj. at 6-9; Tr. at 183:2-13; Tr. at 72:16-19 ("Q. And
23 the company also requested what we have called a CSIB, which is essentially the same thing for the
24 wastewater side of the company operations? A. That's correct"; Tr. at 75:-13-15 (identifying positions
regarding a water SIB and wastewater SIB); Tr. at 76:21-25 (identifying engineering report for
infrastructure needs of wastewater division); Ex. A-20; Tr. at 81:5-11 (testifying that water and wastewater
SIBs are "materially the same" and subject to the same reasons for approval).

25 ¹¹⁷ Tr. at 89:13-18, 139:18-25, 182:24 – 183:5 (Krygier); Tr. at 233:24-234:23 (Mease).

26 ¹¹⁸ Tr. at 89:13-24.

¹¹⁹ Tr. at 183:4-5.

1 pipes leak just like water pipes, and that leaking wastewater pipes are a health hazard.¹²⁰

2 When viewed in full light, RUCO opposes a wastewater SIB for LPSCO simply
3 because LPSCO is the first utility to ever ask for one in Arizona. The benefits of the
4 wastewater SIB aren't lessened because LPSCO is the first one to ask. Nor do the
5 fundamental benefits of rate gradualism, rate stability and attraction of capital to fund
6 major plant investment and replacement needs vary depending on whether the project
7 involves water pipe instead of sewer pipe or whether the plant falls under a NARUC water
8 account or a NARUC sewer account. Rather, the need for and benefits of a SIB are
9 identical for both water and wastewater service. It is undisputed that the wastewater SIB
10 operates exactly the same as the water SIB, and will provide the same benefits of rate
11 gradualism, rate stability and access to capital as the water SIB.¹²¹ In fact, a line-by-line
12 comparison of the wastewater SIB with the water SIB demonstrates that the mechanics,
13 analysis and operation under both SIBs are identical, with the only differences being the
14 use of wastewater terms instead of water terms.¹²²

15 RUCO's further suggestion that the wastewater SIB should not be approved
16 because it was not subject to a collaborative effort of the wastewater industry is
17 disingenuous. It's RUCO that is legally challenging the results of the collaborative effort
18 that led to the AWC SIB in Arizona's courts. To now say that the wastewater SIB is
19 flawed because there was no settlement is just silly. The underlying benefits of the
20 wastewater SIB do not vary or change with a collaborative process. Further, the policies
21 and conclusions from the collaborative process for the AWC SIB apply equally and fully
22 to LPSCO's wastewater improvements and projects here. In fact, the LPSCO water and

23 ¹²⁰ Tr. at 235:13-23.

24 ¹²¹ Krygier Dt. at 6; Krygier Rj. at 7; Ex. A-25; Ex. A-26; Tr. at 72:16-19, 75:13-15, 76:21-25, 81:5-10
(Krygier).

25 ¹²² Compare A-25 with A-26. See also Staff Br. at 14 ("Functionally the CSIB and the SIB are
26 identical... While the SIB and the CSIB are different types of systems, the process of administration for
either would work in a substantially similar manner.").

1 wastewater SIBs “are materially the same” as the AWC SIB approved by the Commission
2 in Decision No. 73938, and the POAs are part of a collaborative process between the
3 Company and Staff.¹²³ RUCO’s arguments are getting more strained and continue to lack
4 any merit.

5 **G. The RAPA Report Is Nothing More Than Consumer Advocacy and**
6 **Should Be Summarily Ignored.**

7 RUCO spends six pages of its opening brief repeating and block quoting the
8 arguments of its sister agency in Alaska, RAPA, with respect to DSIC mechanisms.
9 RUCO attempts to portray the RAPA comments as an objective analysis of DSIC-like
10 mechanisms. This is quite a whopper. In truth, RUCO misleads the Commission by
11 portraying the RAPA comments in that light.

12 In reality, the RAPA comments reflect the activism of a consumer advocacy
13 section of the Alaska Attorney General’s Office and do not present a balanced view of the
14 DSIC mechanism or an objective analysis of Arizona’s SIB mechanism. Even worse, the
15 RAPA comments suggest several positions contrary to Arizona law and consider
16 circumstances substantially different than the SIBs at issue here. The RAPA comments
17 are nothing more than obvious consumer advocacy.

18 Beyond the obvious biases embedded in the RAPA comments, an examination of
19 the positions espoused in those materials (and RUCO’s arguments) reveal that they are
20 erroneous or irrelevant to the facts and circumstances presented here. For example,
21 RUCO uses the RAPA comments as support for the benefits of regulatory lag, even
22 arguing that “[o]ther than an after-the-fact review for prudence, regulatory lag is the only
23 regulatory tool available to protect captive ratepayers because it creates an economic
24 incentive for utilities to curtail unnecessary spending.”¹²⁴ That claim is not only

25 ¹²³ Tr. at 76:7-8 (Krygier).

26 ¹²⁴ RUCO Br. at 19.

1 unsupported in this record, but patently misleading. In truth, the proposed SIBs contain a
2 myriad of ratepayer protections as detailed above, including a surcharge cap, the 5 percent
3 efficiency credit, an earnings test (including an evaluation of operating costs and
4 expenses), Commission review of the SIB plant both before and after a surcharge is
5 proposed, and limits on the number of SIB filings in between rate cases, among others—
6 none of which were addressed in the RAPA report.¹²⁵

7 Using the RAPA comments, RUCO trumpets regulatory lag as an important tool to
8 curb unnecessary spending by utilities. RUCO's position is irresponsible and lacks any
9 evidentiary support, relying solely on RAPA's position paper. Specifically, there is not a
10 scintilla of evidence in the record of any unnecessary spending by LPSCO. As a matter of
11 law and fact, the RAPA comments are irrelevant and immaterial to this case.

12 **IV. RUCO'S OTHER RED HERRINGS SHOULD BE IGNORED.**

13 Finally, the Commission should disregard RUCO's other red herrings in its brief
14 relating to extraordinary circumstances and alleged differences with the LPSCO SIBs.

15 **A. RUCO's Extraordinary Circumstances Argument Is Meritless.**

16 To start, RUCO suggests that the circumstances underlying the AWC SIB are
17 different than LPSCO, hinting that AWC was faced with an extraordinary or unique set of
18 circumstances. RUCO then contends that the SIBs should be denied for LPSCO because
19 the plant replacements projects are routine in nature.¹²⁶ These arguments miss the point
20 and conflict with RUCO's consistent arguments in the AWC case that AWC's situation
21 was not extraordinary at all.

22 Whether or not the SIB plant replacement is routine in nature does not change the
23 need for and benefits of the SIB mechanisms. LPSCO faces \$25 in needed improvements
24 to its water and wastewater systems. In turn, customers want rate gradualism and

25 ¹²⁵ See Ex. R-8 at 3:2-6.

26 ¹²⁶ RUCO Br. at 7-8, 13.

1 stability—irrespective of whether the plant being replaced is routine, extraordinary or
2 subject to governmental mandate.¹²⁷ Perhaps even more alarming, RUCO’s approach
3 sends the wrong message to utilities—namely, that a company should be in financial ruin
4 or neglect its capital replacement needs for many years before regulators find ways to help
5 the company and its customers.¹²⁸ RUCO should be thinking of and proposing long-term
6 solutions, not promoting financial and operational irresponsibility as the only way to meet
7 adjuster eligibility standards.

8 **B. The LPSCO SIBs and the AWC SIB Are Virtually Identical.**

9 Almost inconceivably, RUCO argues that the AWC SIB is different than the
10 LPSCO SIBs. RUCO cites three minor differences—(1) a different process for adding
11 SIB-Eligible Projects; (2) the alleged failure to discuss consequences of the earnings test
12 in the LPSCO POAs; and (3) a convoluted argument that the LPSCO SIBs have expanded
13 the purpose of the SIBs to include “almost every type of plant.”¹²⁹ RUCO’s attempts to
14 distort the POAs should be rejected because the LPSCO SIBs contain the same features,
15 provisions and protections as the SIB approved in Decision No. 73938.

16 In no uncertain terms, the AWC SIB and the LPSCO POAs contain the exact same
17 criteria for SIB-Eligible Projects.¹³⁰ Just like the AWC Settlement Agreement, all of the
18 infrastructure replacement projects contemplated for SIB recovery under the LPSCO
19 POAs must be reviewed by Staff and approved by the Commission prior to LPSCO filing
20 for recovery of the capital costs associated with such projects through a SIB surcharge.¹³¹
21 Just like with AWC, Staff has reviewed all of those SIB-Eligible Projects listed on SIB

22 _____
¹²⁷ Krygier Rb. at 22-23.

23 ¹²⁸ *Id.*

24 ¹²⁹ RUCO Br. at 14-15.

25 ¹³⁰ Ex. A-25 at 2, § I; Ex. A-26 at 2, § I; Ex. A-19 at 4, § 2.1.

26 ¹³¹ Ex. A-26 at 3, § I (definition of SIB Plant Table I); Ex. A-25 at 2, § I (definition of SIB Plant Table I);
Ex. A-19 at 4, § 2.4 (“A list of these projects and an estimation of the capital costs of each is set forth in
SIB Plant Table I, attached hereto as Exhibit A”).

1 Plant Tables I for LPSCO's water and wastewater divisions and approved the costs of
2 those SIB-Eligible Projects.¹³²

3 Under the POAs, SIB-Eligible Plant must satisfy at least one of the following
4 conditions: (1) water loss exceeding 10 percent (for water) or replacement plant
5 necessary to address excessive infiltration and inflow (for wastewater); (2) assets have
6 remained in service beyond their useful service lives; or (3) any other engineering,
7 operational or financial justification supporting replacement, including increased levels of
8 repairs or failures, meter replacements and assets required to be moved or replaced by a
9 government agency.¹³³ Those are the same basic criteria as the AWC SIB.¹³⁴

10 Based on those criteria, "[t]he Company can seek Commission approval to add
11 projects in SIB Plant Table I only in the event of emergency circumstances."¹³⁵
12 RUCO's argument that the LPSCO SIBs are somehow different because "now, projects
13 can only be added under 'emergency circumstances'" is immaterial. The LPSCO SIBs
14 and the AWC SIB contain and apply the same fundamental criteria for SIB-Eligible
15 Projects. From there, it is up to the Commission to determine whether a specific project
16 should be added to SIB Plant Table I for LPSCO as an "emergency."¹³⁶

17 Next, RUCO claims that the LPSCO earnings test is somehow different than the
18 earnings test for AWC because Decision No. 73938 describes the consequences of the
19 earnings test, but the POAs do not. Again, however, it is for the Commission to determine
20 the consequences of the earnings test—not LPSCO or Staff. As stated by Mr. Krygier at
21 hearing, if an earnings test shows that LPSCO is earning a higher rate of return under the
22

23 ¹³² Tr. at 199:25-200:14 (Hains)("Q. All right. And in your review of those tables submitted by the
24 Company, did Staff find the plant cost to be reasonable and appropriate? A. Yes.")

25 ¹³³ Ex. A-25 at 8, § V(A-D); Ex. A-26 at 8, § V(A-D).

26 ¹³⁴ *Id.*; Ex. A-19 at 6-7, §§ 6.1-6.4.

¹³⁵ Ex. A-25 at 8, § V(A); Ex. A-26 at 8, § V(A).

¹³⁶ Tr. at 185:7-14 (Krygier).

1 SIBs than authorized, LPSCO would be subject to the same consequences as AWC under
2 Decision No. 73938—namely, the SIB surcharge would be disallowed.¹³⁷

3 Last, RUCO makes a tortuous argument that the LPSCO SIBs have somehow
4 expanded the SIB “to include almost every type of plant.”¹³⁸ At hearing, Mr. Krygier
5 explained that only certain limited types of plants qualify as SIB-Eligible.¹³⁹
6 RUCO’s argument is difficult to follow and ignores the SIB eligibility criteria listed in the
7 POAs that are identical to the AWC SIB as approved in Decision No. 73938.¹⁴⁰
8 Apparently RUCO takes issue with fire flow improvements, citing the Commission’s
9 Decision No. 70351 (May 16, 2008) denying a FCRM for EPCOR’s Sun City Water
10 District.¹⁴¹ That decision, however, doesn’t address whether the LPSCO SIBs mirror the
11 AWC SIB. Unlike the FCRM decision, the SIB mechanisms here are premised on \$25
12 million in capital improvements needed for LPSCO’s water and wastewater systems, and
13 the benefits of rate gradualism, rate stability and access to capital from the SIBs so needed
14 improvements can be financed. In Decision No. 73938, the Commission discussed the
15 FCRM decision on pages 48-49 and approved the AWC SIB based on its separate record,
16 justifications and benefits. The Commission should do the same here.

17 **V. CONCLUSION.**

18 For the reasons set forth above and in LPSCO’s Opening Brief, LPSCO requests
19 that the Commission adopt the Settlement and approved the water and wastewater SIBs on
20 the terms and conditions set forth in the SIB Plans of Administration.

21
22
23 ¹³⁷ Tr. at 161:6-17.

¹³⁸ RUCO Br. at 15.

24 ¹³⁹ Tr. at 180:12-24 (SIB does not include a water treatment plant or water wells); Tr. at 139:10-14
25 (describing limitations under NARUC accounts); Tr. at 142:11-17 (same). *See also* Ex. A-25 at 1, § II
(definition of SIB-Eligible Plant); Ex. A-26 at 1, § II (definition of SIB-Eligible Plant).

¹⁴⁰ Tr. at 142-143 (Krygier).

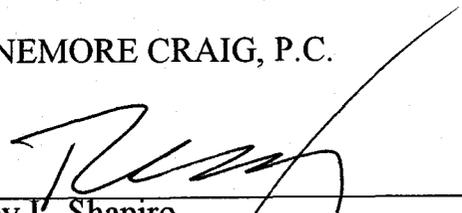
26 ¹⁴¹ RUCO Br. at 15-16.

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26

RESPECTFULLY SUBMITTED this 31st day of January, 2014.

FENNEMORE CRAIG, P.C.

By:


Jay L. Shapiro
Todd C. Wiley
Attorneys for Liberty Utilities
(Litchfield Park Water & Sewer) Corp.

ORIGINAL and 13 copies filed
this 31st day of January, 2014, with:

Docket Control
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

COPY hand-delivered
this 31st day of January, 2014 to:

Teena Jibilian, Administrative Law Judge
Hearing Division
Arizona Corporation Commission
1200 West Washington
Phoenix, AZ 85007

Robin Mitchell, Esq.
Matthew Laudone, Esq.
Legal Division
Arizona Corporation Commission
1200 West Washington
Phoenix, AZ 85007

Dan Pozefsky, Esq.
Residential Utility Consumer Office
1110 W. Washington St., Suite 220
Phoenix, Arizona 85007

COPY sent via U.S. mail
this 31st day of January, 2014, to:

Olivia Burnes
356 N. Cloverfield Circle
Litchfield Park, Arizona 85340

By:

