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Arizona Corporation Commission
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# BEFORE THE ARIZONA CORPORATION

COMMISSIONERS
**Susan Bitter Smith, Chairman**
**Bob Burns**
**Tom Forese**
**Doug Little**
**Bob Stump**

| In the matter of the Application of EPCOR Water Arizona, Inc., for a determination of the current fair value of its utility plant and property and for increases in its rates and charges for utility service by its Mohave Water District, Paradise Valley Water District, Sun City Water District, Tubac Water District, and Mohave Wastewater District. | **Docket No. WS-01303A-14-0010**<br><br>**30 April 2015** |
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## REPLY BRIEF

**by Marshall Magruder**

This Reply Brief responds to the Administrative Law Judge's direction that briefs should provide evidence supporting one's arguments with a Reply to the other party's Briefs. The following parties filed six Briefs on 17 April 2015:

1. EPCOR Inc., the applicant, EPCOR's Post Hearing Opening Brief (EPCOR Brief)
2. Commission Staff's Opening Brief (Staff Brief)
3. Residential Utility Consumer's Office (RUCO) Closing Brief (RUCO Brief)
4. Santa Cruz Valley Citizens Council (SCVCC) Closing Brief (SCVCC Brief)
5. The "Resorts" Closing Brief ("Resorts" Brief)
6. Magruder Post-Hearing Brief (Magruder Brief)

The Magruder Brief presented arguments concerning **three Major Issues** and **other issues that arose** during these proceedings. The following is a reply for these major issues:

**I. MAJOR ISSUE 1 – The Present and Proposed Rates do not comply with the Arizona State Constitution, Arizona Revised Statues, a Commission Order and precedents** ("legal requirements"[1]) **with unreasonable differences in rates and charges between locations and classes of service in all the Company's Arizona service areas for the same contemporaneous service. The rates and charges must the same for all customer locations to comply with Arizona legal requirements and to reduce rate shock.**[2]

[1] Arizona Constitution, Title XV, Section 12; Arizona Revised Statutes, §§ 40-203, 40-248, 40-334, 40-361, 40-362, 40-367; Commission Order No. 71410 at 78. The "Legal Requirements" are quoted in **Exhibit Magruder-5**.

[2] Magruder Brief, at 9:9-16,16-41; 54:14-55-55:12, 61, 64; Magruder Surrebuttal Testimony (**Exhibit Magruder-2**) at 2:24-4:15, 9-11 Attachment A; Magruder Direct Testimony (**Exhibit Magruder-1**), at 7, 13- 28.

1. EPCOR, Staff, RUCO and "Resorts"[3] Briefs or testimonies did not respond to this critical legal issue; however, the Company strongly supports consolidated rates.

2. SCVCC supports rate consolidation to eliminate rate disparity and discriminatory rates in Tubac service area compared to costs 3½ times that of others for the same volume of water. The SCVCC urged "the Commission to consider consolidation of all EPCOR's water districts in the near future" and follow the practice of other types of utilities.[4] The SCVCC reiterates its position that the average residential customer already experiences "rate shock." A proposal of 61% (to $86/month) only exacerbates the customer's burdens that already pay significantly more than any other EPCOR water customers. To reduce these financial impacts, "there must be a phased in-approach spanning at least three years, with no recovery of foregone revenue."[5]

The Magruder Brief recommended the four water service areas be combined into one revenue-neutral, integrated rate structure during these proceedings and that this rate structure and all other water service area rates be further combined over several years into a single companywide rate structure in a future rate case[6] with Companywide Rules and Regulations.[7]

## II. MAJOR ISSUE 2 – The Proposed Low Rate Plan[8] fails to provide equitable and fair rates for all lower income ratepayers, has proven dysfunctional, and does not comply the legal requirements.[9]

1. The EPCOR, the Staff and RUCO Briefs propose and tweak an unsatisfactory Low Income Rate Plan shown to be inefficient, not effective, has failed in the five years since first ordered by the Commission, must refund over-collected surcharge to ratepayers, significantly overcharges small businesses and fails to meet the "legal requirements" cited above.

The Company proposes an additional rate increase for all the highest Rate Tiers with considerably different surcharges ($0.578/1000 gallons in Tubac; $0.0570/1000 gallons in Mohave, $0.021/1000 gallons in Sun City, and $0.012 in Paradise Valley).[10] This surcharge has

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[3] "Resorts" are a joint filing by Sanctuary Camelback Mountain Resort & Spa, JW Marriott Camelback Inn, and Omni Scottsdale Resort & Spa at Montelucia, hereafter the "Resorts."

[4] Closing Brief by James Patterson and Rich Bohman on Behalf of the Santa Cruz Valley Citizens Council, 17 April 2015 (hereafter SCVCC Brief), at 9:19-10:13.

[5] SCVCC Brief at 8:24-9:17. This Brief cites examples where the Commission has forgone such revenue.

[6] Magruder Brief, at 64:5-21.

[7] *Ibid.*, at 21:6-8 and footnote 32; 44:25-29 and footnote 60; 48:16-20. It was also recommended that the new, easy to read, Rules and Regulations (R&Rs) be in the Company's website and translated into Spanish.

[8] *Ibid.*, at 44:10-29 quotes the "plan" for a service area from the EPCOR's Rate Case Application.

[9] Magruder Brief, at 9:18-27, 42-46, 61, 64; Magruder Surrebuttal Testimony, at 4:17-5:18, 6:23-32; Magruder Direct Testimony, at 7, 29-33. The "Legal Requirements" are quoted in **Exhibit Magruder-5**.

[10] EPCOR Brief, at 44:16-20. The few dollars in a reduced fixed Service Charge for the low-income ratepayers is contrary to the Company's other goal for higher fixed revenue. Also the rate tables in Schedules H submitted by EPCOR, Staff, and RUCO did NOT include this surcharge in the rate analyses but showed this "rate" as a

significant locational differences and can only be described as an arbitrary and capacious rate adjustment that fails to comply with legal requirements, especially the customers with just two Rate Tiers. This low-income plan is contrary to other utilities that raise rates in all tiers.

2. The Staff Brief has the "over recovered" revenue from Mohave and Sun City "low income" surcharge removed, included in the test year revenue, and to be amortized over three years,[11] an inconsistent methodology as the surcharge remains for the other areas.

3. The RUCO Brief recommend a Plan of Administration be filed in this docket showing how this program operates and to provide examples of how it intends use the surcharge.[12]

4. The other party's did not respond to this issue.

The Magruder Brief recommends a fair and reasonable solution, easy to implement, without any administrative overhead in an integrated rate structure.[13] The proposed "low income" surcharge, different between service areas, increases the rate differences between locations.[14] Magruder Brief lists eleven benefits of a "*water lifeline*" for all ratepayerscompared to ten administrative and other program costs associated with the proposed Low Income Plan.[15] The proposed plan should be rejected due to its high cost to benefit ratio.

## III. MAJOR ISSUE 3 – The present and proposed Rate Structure does not use cost as the key driver for rates, is not designed with adequate tiers for ratepayers to conserve water, does not meet legal requirements with the same rates in all service areas.[16]

1. EPCOR's Brief briefly stated rate design was important:

> *"Rate design is also an issue in dispute between the parties – an issue that demands attention given its tendency to drive consumer behavior and increased likelihood to put the Company at further risk of not earning its authorized return."* [EPCOR Brief, at 4:7-10]

The Company addressed this issue was misleading, by stating:

> *"The Company's proposed rate design, which will appropriately incent conservation, recovers a smaller, and more appropriate, percentage of metered revenue from the highest commodity rate, whereas Commission's Staff's proposed rate design recovers a greater percentage."* [*Ibid.*, 4:22-43:2]

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footnote on the last page. The Company was inconsistent in its Final H-3 Schedules with different Low Income Surcharges, see Magruder Brief, at 28, footnote 39; and at 27, Tables 4(b) and 4(c).

[11] Staff Brief, at 10:18-11:4.

[12] RUCO Brief, at 43:18-22.

[13] Magruder Brief, at 64:23-65:3.

[14] *Ibid.*, at 53:4-17; Magruder Surrebuttal Testimony at 11, Table 2.11-4 (Rev. A).

[15] *Ibid.*, at 45:1-46: 15-36. The term "water lifeline" is used as arbitrary words for this approach, and is not considered as a final recommended term to be used by the Company.

[16] Magruder Brief, at 9:29-10:4, 47-52, 61-62, 65; Magruder Surrebuttal Testimony, at 5:18-7:35; Magruder Direct Testimony, at 7, 34-44, 55-58 Appendix 3, Consolidated Rate Schedule.

The Company wants its proposed rate structure and tiers so it will have greater rate stability and earn its authorized return.[17] Has made no recommendations on reducing its cost as the requirements for its service decreases, thus "incentives" itself and not the ratepayer.

2. SCVCC supported any new rates to be implemented over a three-year period for service areas with significant rate changes with consolidated rates.

3. RUCO Brief discussed the Paradise Valley service area at "useless" with serious design flaws in relation to "cross-over" issues and indicated that the Company would NOT correct its schedules to correct these serious rate design flaw. RUCO also stated that the Staff's rate design is similarly flawed.[18]

4. The other parties including the Staff did not address this issue.

The Magruder Brief proposed a **revenue neutral rate structure that meets all the Company's revenue requirements, complies the legal requirements, provides a "*water lifeline*" for all low-consuming and lower-income ratepayers, equalizes the significant unreasonable rate and proposed surcharge differences between locations, simplifies the company's administration, reduces rate case costs** and recommends **implementation over a multi-year perio**d (with no more than a 10% rate change per year) that supports the Company's strong position for consolidated rates.[19]

The Company, Staff and RUCO proposed rate structures do not lead to water conservation, when compared to the Magruder guidelines, with cost as the significant driver for volumetric rates[20] with the necessary additional Rate Block Tiers that are essential to send Price Signals to customers to conserve water.[21] The Company, Staff and RUCO proposed rate schedules have most rate categories with only two tiers, that does NOT "incent" any water conservation, as misleadingly claimed by the Company's comment above.[22]

The **proposed rate structures are unsatisfactory** and must be combined into one structure for the four water service areas in this case, with at least seven rate tiers, with a "*Water Lifeline*", the First Tier for ALL residential rate categories and smaller commercial (<2-inch) rate categories of 3,000 gallons with a volumetric rate of about $1.00 per 1,000 gallons, with progressively increasing rates (per 1000 gallons) for the higher tiers in order the meet the

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17 *Ibid.*, at 44:4-7.
18 RUCO Brief, at 41:16-42:4.
19 Magruder Brief, at 66:5-29; Magruder Surrebuttal Testimony, at 8:1-25.
20 Magruder Brief, at 50:21-51:35.
21 *Ibid.*, at 52:20-27 which recommends at least seven rate tiers so ratepayers can see how close they are on their bill to the next lower tier. The "two-tier" proposed design cannot accomplish this.
22 *Ibid.*, at 65:5-29.

Company's revenue requirement.[23] The Service Charge for the smallest residential rate and commercial categories should be low so that First Tier ratepayers will have a monthly bill between $20.00 and $25.00 to benefit lower income and all lowest consuming ratepayers.[24]

The Magruder testimonies and Brief provide abundant evidence to conclusively prove the present and proposed rate structures are illegal, unreasonable, unfair, discriminatory, fail to promote water conservation, and do not provide rate relief for the lowest income ratepayers.[25]

## IV. OTHER ISSUES that Arose during these Proceedings.

The Magruder Brief described six additional issues as follows:

### A. EXCESSIVE SURCHARGES AND FEES.

At least eleven surcharges, adjustments, mechanisms, and fees were addressed in these proceedings. The Magruder Brief considered these as excessive and recommended few are billed directly to customers because they decrease stable, predictable monthly bills and will result with many changes during the year. Many of these excessive surcharges and fees "need to be squashed before they see daylight"[26] or when appropriate, added to the rate base.

RUCO discusses the various cost adjustments, surcharges, fees and other mechanisms with ratepayer impacts quotes from Decision No. 68302 the following that is very applicable to these excessive number of surcharges and fees that most of the below do not meet:

> *"Adjustment mechanisms should therefore be used only in extraordinary circumstances to mitigate the effect of uncontrollable price volatility or uncertainty in the marketplace."* [RUCO Brief, at 42:11-23, Exhibit R-9, at 48-48]

1. **Affordable Car Act Adjustment Surcharge (ACAM)**.[27] This surcharge is to cover any additional or decreased in Company expenses due volatility and unpredictable health care cost associated with the Affordable Care Act (ACA).

a. EPCOR and the Commission Staff supported this surcharge however; the magnitude of a proposed surcharge was not specified and is unknown.

b. RUCO did not support this unknown expense. It maybe not a potential cost for such expenses incurred by any company. RUCO recommends denial of ACAM.[28]

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[23] *Ibid.*, at 50:21-51-35 including footnotes 62 to 67; at 65:1-2.
[24] *Ibid.*, at 61:23-31.
[25] Magruder Brief, all; Magruder Surrebuttal Testimony, all; Magruder Direct Testimony, all, Appendix 3, Consolidated Rate Schedule.
[26] Magruder Brief, at 53:4-17 including footnote 68 [Emphasis in original].
[27] EPCOR Brief, at 40:8. This "adjustor" is called "Health Care Cost Adjustor" in this brief.
[28] RUCO Brief, at 43:11-15.

c. SCVCC witness Patterson does not support. This a normal business risk and such a surcharge, as an unusual pass-though by the Company, as transfers a business risk away from the Company. Thus, EPCOR should be granted a lower cost of capital.[29]

d. Other party's briefs did not discuss to this issue.

Magruder Reply. Magruder agrees with RUCO and SCVCC and recommended this normal employee expense, even with its unknown volatility, to make such a surcharge is "frivolous" should not be implemented and only considered an a normal business expense in rate cases.[30] Further, based on a bipartisan Congressional Budget Office forecasts lower medical insurance costs in the next decade.[31]

2. **Power Cost Adjustor Mechanism (PCAM) Surcharge**. This surcharge would automatically increases rates whenever Arizona Public Service (APS) raised its electricity rates when approved by the Commission based on gallons of water pumped, rather than sold.

a. EPCOR and the Commission Staff Briefs supported this surcharge based on an APS study of projected future costs of electricity.

b. RUCO Brief did not support this surcharge based on unknown costs, potential rebates if overcharged, and, the option always exists if excessive expenses occur, an interim rate increase could be requested if such costs become extreme. RCUO does approve of including known and measurable already Commission-approved rate increases for electricity utilities, but not forecast projections.[32]

c. SCVCC Brief compared the power costs for the adjacent and similar sized Baca Float water company with this charge for the Tubac service area and noted that EPCOR's power expenses were 139% higher.[33]

d. Other party's briefs did not discuss to this issue.

Magruder Reply: Magruder concurs with RUCO only for Commission-approved fixed (non-variable) electricity rate changes and not for "projected" future costs and disagrees with ECCOR and Staff positions. Magruder Brief stated as a normal business cost and this should not be a monthly variable billing adjustment, without customer notice or inputs. Some water service areas are in different electric service areas. If approved, basis this surcharge on gallons of water pumped is not correct, it is a prudent electricity cost that is the cost factor.

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29 SCVCC Direct Testimony by Patterson, at 4:10-16.
30 Magruder Brief, at 53:19-29; 66:3.
31 **Magruder Exhibit-10**, *Arizona Daily Star,* Report says Affordable Care cost falling," 10 March 2015, at A10.
32 RUCO Brief, at 31:14-23.
33 SCVCC Brief, at 6:6:7, Exhibit A, "Expense Comparison – EPCOR Water Tubac vs. Baca Float Co.

UNS Electric rates change monthly due to a rolling 12-month average PPFAC rate, presently refunding because of PPFAC overcharges. With several electric utilities, different rate structures, different rate case approvals and other factors, this expense is considered in routine water rate cases. Monthly changing surcharges should not be approved to create customer confusing billing statements with variations beyond the ratepayer's control.[34]

The Company needs to benefits from the electric utilities energy efficiency programs, such as Time of Use (TOU) schedules for nighttime pumping and equipment upgrades. [35]

3. **Declining Use Adjustment (DUA)**. All service areas reduced water consumption since their last rate case. The Company proposed an adjustment to makeup for lost revenue.[36]

a. EPCOR proposes adding a "declining usage adjustment" (DUA) based on revenue changes between rate cases. This adjustment was proposed to decrease impacts of lower water usage on revenue by increasing the fixed Service Charge part of revenue structure and decreasing the volumetric part of revenue. The Company stated if only 30-40% of its revenue was from the Service Charge, this "nearly endure the under-recovery of costs." The Company disagreed with Staff's ratio of fixed to total revenue as adequate for cost recovery.[37]

b. Staff appears to agree with the Company on this issue of a DUA however; its implementation shows a lower ratio of fix revenue to total revenue than the Company. [38]

c. The RUCO recommends to deny this adjustment.[39] RUCO's testimony shows some areas have increased water consumption since the test year with potential DUA rebates in some areas while possibly not in others.[40] RUCO recommended an annual water usage report for each customer class and meter size to establish clear long-term usage trends. [41]

d. Other party's briefs did not discuss to this issue.

Magruder Reply: Magruder recommended deny an unpredictable Declining Use Adjustment (Low Water Use surcharge) due to very negative customer reactions for those who are trying to conserve water. A different mechanism, such as a higher ROI, with a revenue "true-up" in the next rate case, based the RUCO recommended water usage report results.[42]

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34 Magruder Brief, at 54:1-12. This surcharge was called a "Power Purchase Surcharge" in this Brief.
35 *Ibid.*, at 49:18-21.
36 *Ibid.*, at 54:13-55:12. This surcharge was called a "Low Water Use Surcharge" in this Brief.
37 EPCOR Brief, at 42:6-43:16.
38 *Ibid.*, at 42:11-43:6.
39 RUCO Brief, at 26:12-15.
40 *Ibid.*, at 26:12-29:22; **RUCO Exhibit R-29**.
41 *Ibid.*, at 29:19-22.
42 Magruder Brief, at 54:14-55:12; RUCO Brief at 29:19-22.

4. **Central Arizona Project (CAP) Surcharge**. This is an annual, variable fee for purchasing CAP water levied by an outside organization with some risk possibly associated with future power cost from the Navajo Generation Station and the ongoing drought impacts on CAP water allotments. This surcharge impacts only the Paradise Valley service area.

a. EPCOR proposed to continue to file with the Commission annual CAP surcharge adjustments as its annual rates are changed, which are expected to increase.

b. Staff agrees with the Company's recommendations.

c. RUCO disagrees with EPCOR and Staff as RUCO claims the Company violated Commission Orders that ordered inclusion of this surcharge in base rates instead.[43]

d. Other party's briefs did not discuss to this issue.

Magruder Reply: This is an annually variable cost and should be continued as a unique customer surcharge to impacted ratepayers. An annual filing for approval should be required.[44] Highlighting this as a billing item, due to the ongoing drought and potentially higher CAP fees, impacted ratepayers can see the impact of the CAP fees on their bills.

5. **Ground Water Use Surcharge**. This is a similar fee for ground water use applicable only to Sun City ratepayers that is not controlled by the Company.

a. EPCOR and Staff recommend the present surcharge process continue.[45]

b. Other party's briefs did not discuss to this issue.

Magruder Reply: This is an annually variable cost that should be continued as a unique customer surcharge to the impacted ratepayers. An annual filing for approval should remain.[46]

6. **Deferred Arsenic Media Replacement O&M Surcharge (DAMRO).**[47] This is a new surcharge proposed for the arsenic media used in the Tubac Arsenic Treatment Plant (ATP).

a. EPCOR Final Schedule has this surcharge rate at $1.77 per 1000 gallons from all Tubac service area customers. The Company proposed and RUCO agreed that arsenic media cost of $101,712 would be recovered as a surcharge over a three-year period. The Company disagrees with Staff to remove from rate base $178,533 as Water Treatment Equipment-Media, after adjustments, and that $172,839 remain in rate base for Water Treatment Equipment-Non Media.[48]

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[43] *Ibid.*, at 36:2-37:5.
[44] Magruder Brief, at 55:14-21.
[45] EPCOR Brief, at 36:2-6
[46] Magruder Brief, at 55:23-25.
[47] *Ibid.*, at 30:1 and 2, misused the acronym "SAMRO" instead of the correct acronym, DAMRO.
[48] EPCOR Brief, at 30:4-17.

b. Staff agrees with RUCO that the Step-1 ARCM surcharge of $172,839 be removed from the test year revenue.[49]

c. RUCO Brief recommends removal of the Step-1 ARCM Surcharge test year costs of $17,337 for the Tubac District.[50] RUCO also recommends the remaining Step-2 ARCM Deferred O&M surcharge of $101,712 continue and monitored by annual reports until fully recovered over a three-year period. RUCO does not agree with the Company that the Step-1 ARCM be included in rate base in the next rate case application.[51]

d. SSVCC Brief has the $101,712 deferred Arsenic Media costs amortized over two years by adding $50,856 to operating expense to determine rates. This expense equals an "arithmetic" average of $85 a year or $7.08 per month per ratepayer. SSVCC is concerned that the Company does not remove this temporary expense after amortization: "there appears to be no mechanism to reflect a rate reduction once the amortization period ends.[52] SSVCC determined the Tubac arsenic media costs were 27% higher when compared with the adjacent Baca Float water company.[53]

e. Other party's briefs did not discuss to this issue.

Magruder Reply. There are ATP service areas without surcharges for routine changes in the media used to remove arsenic. This expense is in the ratebase. This surcharge is an Operations and Maintenance cost associated with routine operations: media replacement.

It is recommended that this unique, service area-dependent, surcharge be denied but included in the combined Companywide rate base.[54] If ordered, a longer, 3-year amortized period is preferred when compared to two years, after which special arsenic media-treatment plant surcharges and rates must be removed for this service area.

DAMRO, a term this party uses to combine Step-1 ARCM and Step-2 ARCM EPCOR has proposed at $1.77/1000 gallons plus a fixed monthly charge for All Tubac customers.

Inclusion of DAMRO ($1.77/1000 gallons + increased service charge for arsenic treatment) is in the above **Table 1** from the Magruder Brief. DAMRO is the monthly cost in Proposed EPCOR Final Proposed Monthly Average Usage Customer costs in Table 1(b) and the Magruder Proposed Monthly Average Usage Customer costs in Table 1(d).[55]

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[49] RUCO Brief, at 32:19-20.
[50] *Ibid.*, at 23, Adjustment No. 5, Remove ARCM Surcharge and Deferred O&M Cost.
[51] *Ibid.*, at 32:1-18.
[52] SCVCC Brief, at 4:23-5:8.
[53] SCVCC Direct Testimony of James S. Patterson, at 5:11-6:1, 6:12-13, 8, Exhibit A, "Expense Comparison – EPCOR Water Tubac v Baca Float Water Co.
[54] Magruder Brief, at 55:27-56:3.
[55] *Ibid.*, at 21:14-23:24:14, Table 1.

## TABLE 1. COMPARISON OF PRESENT AND PROPOSED RESIDENTIAL COSTS FOR MONTHLY AVERAGE USAGE.[56]

### Table 1(a).
***PRESENT COST: Average Usage, Monthly Cost, and Cost per 1000 Gallons Of Water***

| *AVERAGE Monthly Usage* | Residential Rate Categories | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 5/8 and 3/4-inch meter service | | | | 1-inch meter service | | | |
| | Tubac | Sun City | Paradise Valley | Mohave | Tubac | Sun City | Paradise Valley | Mohave |
| Use in gallons | 8,348 | 7,203 | 19,271 | 6,800 | 13,838 | 14,786 | 55,400 | 23,601 |
| Present COST | *$53.57* | *$17.35* | *$52.30* | *$20.63* | *$146.05* | *$43.44* | *$165.40* | *$80.90* |
| COST per 1000 gallons | ***$6.42 w/ARCM*** | ***$2.41*** | ***$2.71*** | ***$3.03*** | ***$10.55 w/ARCM*** | ***$2.94*** | ***$2.99*** | ***$3.43*** |

### Table 1(b).
***EPCOR <u>FINAL PROPOSAL</u>: Average User Monthly Cost and Cost Increase***
**[Based on EPCOR's 6 April 2015 Final Schedule H-2]**

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Proposed COST INCREASE | **+$32.72 (+25.50)** | **+$2.79** | **+$4.47** | **+$8.63** | **+$46.55 (+$55.05)** | **+$6.20** | **+$14.20** | **+$21.92** |
| Proposed COST (+DAMRO Tubac only) | *$86.29 (+$25.50) $110.79* | *$20.46* | *$56.76* | *$29.26* | *$192.60 (+$55.05) $247.65* | *$49.64* | *$179.60* | *$102.82* |
| Percent COST INCREASE | **+61.07% (+108.68%)** | **+17.91%** | **+8.54%** | **+41.84%** | **+31.87% (69.57%)** | **+14.27%** | **+8.58%** | **+27.10%** |
| COST per 1000 gals (+DAMRO Tubac only) | ***$10.34 +1.77 $12.11*** | ***$2.84*** | ***$2.96*** | ***$4.30*** | ***$13.92 +$1.77 $24.69*** | ***$3.35*** | ***$3.24*** | ***$4.36*** |

### Table 1(c).
***MAGRUDER <u>CONSOLIDATED RATES</u>: Monthly Cost for Average User and Water Lifeline***
**[Based on Magruder Direct Testimony, Appendix 3, for Combined Rates in the "last rate case"]**

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **AVERAGE Usage Cost** | *$39.81* | *$36.95* | *$ 64.33* | *$35.94* | *$ 49.45* | *$52.30* | *$179.54* | *$ 78.74* |
| ***Water Lifeline @*** **3,000 gallons** | **$17.44** | **$17.44** | **$17.44** | **$17.44** | **$22.94** | **$22.94** | **$22.94** | **$22.94** |

### Table 1(d).
***MAGRUDER COMBINED RATES <u>PLUS 10% REVENUE INCREASE</u>: Average User Cost***
**[Based on Magruder Direct Testimony, Appendix 3, for Combined Rates in the "last rate case" plus 10%]**

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **AVERAGE Usage Cost** | *$43.79* | *$40.64* | *$70.76* | *$39.54* | *$54.41* | *$57.53* | *$197.49* | *$86.61* |
| ***COST Change from PROPOSED*** | (-$42.50) (-$68.39 w/DAMRO) | **+$20.18** | **+$14.00** | **+$10.28** | (-$138.19) (-$193.24 w/DAMRO) | **+$7.89** | **+17.89** | (-$66.61) |
| ***Water Lifeline @*** **3,000 gallons** | **$19.15** | **$19.15** | **$19.15** | **$19.15** | **$25.23** | **$25.23** | **$25.23** | **$25.23** |

Proposed EPCOR **Deferred Arsenic Media Replacement O&M (DAMRO) surcharge of $1.77 per 1,000 gallons** for Tubac. **No other service area with an arsenic treatment plant has a DAMRO surcharge for arsenic media replacement.** (Ref: EPCOR Final Schedule H-3, 6)

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[56] *Ibid.*, at 21-22:16.

These tables most clearly show significant differences in present in Table 1(a) and Final proposed rates in Table 1(b) among the water service areas, the impacts for consolidated rates previously proposed by Magruder, and the additional impact of the Arsenic Media costs.

7. **Water Storage Tank Cleaning and Maintenance Surcharge**

a. EPCOR has proposed a 14-year storage tank-cleaning plan for the Paradise Valley service area, proposed this as an expense item, and agrees to "true-up" once finished.[57]

b. Staff Brief concurs with the Company's position.

c. RUCO Brief does not agree in pre-funding *estimated* expenses because they are not "known and measurable" that shifts the risk to the ratepayer, if the costs are less than approved based on "estimates." RUCO indicates there are many unknowns with a 14-year proposal for cleaning and maintaining tanks only in Paradise Valley.[58] RUCO provided a viable alternative for the Company to legally accomplish its goals with true-ups in future rate cases.[59]

d. Other party's briefs did not discuss to this issue.

Magruder Reply. All tanks require maintenance and cleaning. This is routine Company expense required to maintain safe and reliable water service in all its service areas. There are many unknowns. Other water storage tanks not included. These expenses should be in the test year and not as an additional charge for a single service area.

RUCO's alternative requires consideration is a reasonable and appropriate way to plan for these charges to be included in revenue; however, the Company will need to do this.

8. **Tubac Water Storage Tank Surcharge**. This is to add to the Tubac rate base a new expense of an unknown size, water storage tank, at an unknown location, with unknown cost, etc. and is discussed separately in IV.E below.

Magruder Reply. This capital asset cost should not be in this case. This rate base asset and should not be levied as a surcharge on only a service area but in the total companywide combined revenue requirements, along with ALL other capital improvements[60]

9. **Low Income Surcharge**. This is discussed in **Major Issue 2** above.

a. EPCOR Brief proposed a highly variable surcharge in **Major Issue 2** above.

b. The Staff Brief supports the Company's proposed Low Income Plan with slightly lower surcharge but does not consider the benefit/cost issues raised in **Major Issue 2**.

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[57] EPCOR Brief, at 32:14-34:4.
[58] RUCO Brief, at 38:11-39:21.
[59] *Ibid.*, at 40:1-41:7.
[60] Magruder Brief, at 65:34-35.

c. Other party's briefs did not discuss to this issue.

Magruder Reply. This Low Income Plan violates the legal requirements, is unfair, places unreasonable charges on ratepayers and rejected as recommended in **Major Issue 2**.

10. **System Improvement Benefits (SIB) Surcharge**. The Company requested a SIB charge mechanism for Mohave, Paradise Valley and Sun City water service areas.

a. EPCOR proposed a SIB surcharge for projects the Company intends to complete and believes it has complied with Commission SIB project criteria.[61]

b. Staff concurs with EPCOR's request to establish a SIB mechanism and requires the Company to comply with a Plan of Administration.[62]

c. RUCO does not agree with EPCOR or Staff. RUCO strongly opposes granting a SIB project mechanism totaling $28,246,638.[63] For example, under the SIB water mains are to be replaced at 2.1 miles per year; however, the Company replaced 1.8 miles during the test year, not a significant change from its normal operations without a SIB. In a similar meter replacement program, during the test year 4000 meters were replaced, the same for the SIB.[64]

RUCO shows, due only to SIB, monthly customer costs increases by year 5 to 62.99% (Mohave), 37.59% (Sun City) and 22.61% (Paradise Valley) that exceeds the SIB's purpose and is "illegal." RUCO argues the SIB shifts risk from the Company to ratepayer without adequate financial compensation, is not an "adjustor" mechanism, increases Company's fair value rate base without determining fair value, is not in the public interest, does not set aside depreciation expense, and is not urgent. The Company did not request interim rates.[65]

d. The "Resorts" Brief. This Brief recommends that the Commission reject the proposed SIB surcharge because it will increase the total Paradise Valley water districts base revenue by 9.75%, for not providing adequate Notice, and the proposed SIB does not meet the Commission's "extraordinary circumstances" requirement.[66]

The "Resorts" is concerned about paying twice for same asset because of "accumulated depreciation" practices the Company uses with potential double counting issue, and short time frame schedule. This brief agrees with the nine reasons why RUCO opposes a SIB and concludes that a SIB is not appropriate for a healthy company and should not be employed[67]

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[61] EPCOR Brief, at 37:13-22.
[62] *Ibid.*, at 38:1-5.
[63] RUCO Brief, 52:5-53:16.
[64] *Ibid.*, 55:16-56:19.
[65] *Ibid.*, 4:3-18, 56:21-57:3, 57:5-60:12, 60:14-63:14, 63:16-66:3, 66:6-13..
[66] "Resorts" Brief at 2:2-3:17.
[67] *Ibid.* at 3:18-4:1, 4:2-22.

e. Other parties did not respond.

Magruder Reply. This is another Operations and Maintenance (O&M) plan to obtain pre-funding for routine maintenance tasks required by the Company to provide reliable service. O&M expenses belongs in the rate base due to multiple factors, the costs of the SIBs are uncertain, detailed actions unknown, and without a prudency review, approval is impossible. Proposed SIB plans should not be approved. An alternative was suggested and that any SIBs should be for ALL service areas, not a few.[68]

11. **Ground Water Withdrawal Tax**. This tax on billing statements has an unknown origin and its identification has not been found. Only the Magruder Brief discussed this tax.

Magruder Reply. The source, need and rational for this "fee" and who receives this fee are unknown. It appears to be a minor fee, at about $0.01 per 1000 gallons.[69]

## B. EXCESSIVE DEPRECIATION CLAIMED BY THE COMPANY.

During the course of this case, the Company depreciated assets past the end of their useful lives to its benefit and carried this excessive depreciation for many years.

1. EPCOR Brief. The Company recommended approval of excessive depreciation debt balances from prior cases without correcting prior errors. The Company agrees in the future to cease recording depreciation when the full value of an asset is fully depreciated to eliminate future over-depreciated assets.[70]

2. Staff Brief. Staff agrees with the Company to not depreciate beyond an asset's value in the future, opposes the Company's approach to not correct for mistaken entries approved in a prior rate case and recommends $2,836,903 be reduced from total rate base to account for accumulated depreciation.[71]

3. RUCO Brief. RUCO and Staff both oppose the Company's approach as a dangerous precedent to not correct these serious errors, permitting prior customer overcharges to stand without remediation.

RUCO says this undermines the Commission's authority to properly account for depreciation, has ratepayers having to pay for errors for unexplained and unsupported accumulated depreciation debt balances.[72] RUCO states this is a serious issue:

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68 Magruder Brief, at 58:28-59:8.
69 *Ibid.*, at 57:9-15. Billing statements should define ALL charges. This is not defined on EPCOR's statements.
70 EPCOR Brief, at 4:12-15:10
71 Staff Brief, at 6:7-18.
72 RUCO Brief, at 2:3-3:5; EPCOR Brief, at 2:3-3:5; 9:14-.

*"Moreover, ratepayers should not have to pay for errors and unexplained and unsupported accumulated depreciation debit balances which increase rate base and have done so in some instances for over ten years and will continue to be in rate base at a significant cost to the ratepayer unless and until the Commission does something about it. This is a not just one or two isolated instances, this is entry after entry establishing a clear pattern of improper and/or inappropriate accounting."* [RUCO Brief, at 2:8-13]

RUCO recommends the collection of excess depreciation stop and ratepayers be credited for the excess.[73] RUCO indicated the abnormal debit balance was $3,170,346 due to accumulated depreciation. RUCO recommends the Commission order a *Depreciation Study* to be reflected in the next rate case.[74] RUCO has concerns with the Company's internal accounting controls, lack of compliance with NARAC USOA and A.A.C., timeless of reporting, and accumulated deferred income tax account.[75] RUCO's Brief states that the Company has failed to provide data needed for rate cases and has established a pattern of not providing supporting rate case filings that support its investments for its plant in service to meet its revenue requirement and rate design is flawed.[76]

4. Other parties did not discuss to this issue.

Magruder Reply: The unjustified profit obtained by the Company by depreciating an asset beyond its value must be corrected and all prior overcharges returned to ratepayers as a part of the resultant Commission's Order.[77]

This issue appears to be a systemic financial failure. It is respectively recommended that an outside audit be conducted and reported to the Commission, and that the Company considers implementing improved business processes by achieving an ISO 9000 certification for Quality Management and certification under ISO 14000 for Environmental Management.[78]

## C. NEW METER AND SERVICE LINE VARIATIONS.

No parties, other than Magruder, discussed why a meter or a service line installation has different cost in two water service areas than in the other two service areas.[79]

Magruder Reply: This issue was raised earlier without responses.[80] The cost of a meter and service line installation at any location should be the same and the schedules corrected.

73 RUCO Brief, at 3:4-5.
74 *Ibid.*, at 16:4-17:3.
75 *Ibid.*, at 46:9-19.
76 *Ibid.*, at 44:2-14.
77 Magruder Brief, at 57:17-35
78 Magruder Brief, at 48:21-49:21; 57:34-35, 71:31-35; Magruder Direct Testimony at 36:18-33; 43:19-26, 53-54.
79 Magruder Brief, at 58:1-22.

**D. PROHIBIT NEW WELLS IN AMA SERVICE AREAS.**

For a service area within an AMA, the Company can apply to ADWR (A.R.S. §45-454) to prohibit new exempt wells (≤35 gallons/minute) from being drilled within a boundary around the Company's service area. This prevents the Company's wells from going dry, loss of water sold by the Company, and removes the water quality and safety hazards of using private wells.

1. EPCOR and Staff Briefs did not respond to this issue.

2. SCVCC Brief. "Any growth in the Tubac service area has been offset by some residents opting to put in private wells."[81]

3. Other parties did not discuss to this issue.

Magruder Reply: This issue was raised earlier in these processing without responses.[82] It appears the Company may have to be ordered to consider applying to ADWR to prohibit any new exempt wells within a boundary around all Company's service AMA areas.

**E. TUBAC WATER STORAGE TANK ISSUES.**

During the course of these proceedings, the Staff recommended this case remain open so that the capital costs of an additional possible 100,000-gallon or larger water storage tank be constructed in the Tubac service area and a resultant ratebase be increased with this new service area surcharge. The amount of this surcharge is unknown.

1. EPCOR Brief recommends the Company use its own funds (not debt) to ensure the project is completed property and timely.

2. Staff Brief recommends this case to remain open until 1 July 2016 so the cost of this tank can be added to rate base as an unknown surcharge in the Tubac service area.

3. SCVCC Brief included new evidence from a prior docket showing one well was out of service for an extended period of time. However, it was fixed, produces water to meet quality standards and returned to service. SCVCC provided evidence this well's capacity will "provide sufficient capacity without the need for additional storage."[83] SCVCC requested any requirement for additional storage be delayed and separated from the current case, so that adequate consideration can be given to the issues of need, capacity, location and cost."[84]

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[80] Magruder Surrebuttal Testimony, at 4:5-15; 11:33-12:16, Table 1, "Refundable Meter and Service Line Installation Charges." This table based on Final Schedules H in Magruder Brief, at 58:11-15; Table 9.

[81] SCVCC Brief, at 9:25-26.

[82] Magruder Direct Testimony, 29:8-12, 26; Magruder Brief, at 10:16-18; 58:24-33; 63:34-25. This also was raised in the "last rate case" (ACC Docket No. W/WS-01303A-09-0277).

[83] SCVCC Brief, at 7:26-8:1. This quote is from the AAWC Closing Brief in Docket No. WS-01303A-09-0152, contained in the SCVCC Brief a copy of an Amended Staff Report of 1 June 2009, at 12-13, in that docket.

[84] *Ibid.*, at 8:17-21.

5. Other parties Briefs did not respond to this issue.

Magruder Reply: This party agrees with the SCVCC that the additional storage issue is very "debatable." A deferred decision is necessary. The case should not be left open for an unknown capital asset that may not be necessary. This project needs additional review as shown by SSVCC before the Commission "orders" completion of a water storage tank by the end of 2015 (or mid-2016), as proposed by the Staff. The Magruder Brief discussed other funding mechanisms than company-funds. The SCVCC with the County Board of Supervisors, Commissioners, WIFA, and our Congresswoman obtained WIFA loan and other funding for a Tubac Arsenic Treatment Plant, at an interest rate about half of the Company's. Local efforts with the ATP project funding saved an estimated $1M from the rate base. This process takes time and no parties had indicated there is any urgency for this project.[85]

Magruder recommends a new water storage tank, just like the dozens of others owned by the Company, be added to the rate base in a subsequent rate case and reflected in the Company-wide revenue requirements when EPCOR rates are consolidated statewide.[86]

## F. CORPORATE ALLOCATIONS IMPACTS AND REASONABLENESS.

This issue was raised in the SSVCC filings and Brief and shows these unreasonable allocations result in a significant impact on the smaller service areas. For example, the Tubac "corporate allocation" burden is as much as $148,000 for the many and various higher layers of EPCOR corporate administrative overhead and that this exceeds the Staff's calculated Operating Income Deficiency. When such "overhead" expenses are removed, as with the adjacent Baca Float Water Company, the Tubac customer cost become competitive.

The question asked by the SCVCC is when should these cost stop? These additional corporate "layers" are simply internal EPCOR "investors" and their returns on investment risk should be in terms of dividends and investment gains and not as unreasonable ratepayer costs.[87]

Magruder Reply. SSVCC presents an excellent argument for removal of these corporate allocations. Investors receive their return on investment based on earned income, not by "taxing" every corporate level. It is positively recommended that such corporate administrative allocations should be removed from all service areas.

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[85] Exhibit Magruder-10. The *Nogales International* reported that the City of Nogales received a WIFA loan, a low interest loan and a grant for a new water storage tank, a process that saves ratepayers higher interest.

[86] Magruder Brief, at 63:9-10; 65:34-35.

[87] SCVCC Brief, at 5:21-6:5.

## V. CONCLUSION.

In Summary, nothing in the Briefs by other parties has changed the Conclusions and Recommendations in the Magruder Brief or prior Magruder Testimonies with the addition of the above SSVCC arguments and recommendation to remove corporate allocations at the service area level.

For all of the above reasons, the Commission should adopt all of the Magruder recommendations.

RESPECTFULLY SUBMITTED this 30th day of April 2015.

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