ORIGINAL

OPEN MEETING ITEM

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COMMISSIONERS
DOUG LITTLE – Interim Chairman
BOB STUMP
BOB BURNS
TOM FORESE

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ARIZONA CORPORATION COMMISSION

2016 JAN 19 P 2: 28

AZ CORP COMMISSION
DOCKET CONTROL

DATE: JANUARY 19, 2016

DOCKET NO.: W-04286A-15-0339

TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Yvette B. Kinsey. The recommendation has been filed in the form of an Opinion and Order on:

ARROYO WATER COMPANY, INC.
(EMERGENCY RATES)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and thirteen (13) copies of the exceptions with the Commission's Docket Control at the address listed below by **4:00** p.m. on or before:

JANUARY 28, 2016

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Open Meeting to be held on:

FEBRUARY 2, 2016 AND FEBRUARY 3, 2016

For more information, you may contact Docket Control at (602) 542-3477 or the Hearing Division at (602) 542-4250. For information about the Open Meeting, contact the Executive Director's Office at (602) 542-3931.

Arizona Corporation Commission
DOCKETED
JAN 19 2016
DOCKETED BY

JODI A. JERICH
EXECUTIVE DIRECTOR

This document is available in alternative formats by contacting Shaylin Bernal, ADA Coordinator, voice phone number 602-542-3931, E-mail SABernal@azcc.gov

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

DOUG LITTLE – Interim Chairman
BOB STUMP
BOB BURNS
TOM FORESE
VACANT

IN THE MATTER OF THE APPLICATION OF ARROYO WATER COMPANY, INC. FOR APPROVAL OF AN EMERGENCY INCREASE IN RATES.	DOCKET NO. W-04286A-15-0339 DECISION NO. _____ **OPINION AND ORDER**

DATE OF HEARING:	December 7, 2015
PLACE OF HEARING:	Phoenix, Arizona
ADMINISTRATIVE LAW JUDGE:	Yvette B. Kinsey
APPEARANCES:	Michael Armstead, on behalf of Arroyo Water Company, Inc.; and Bridget Humphrey, Staff Attorney, Legal Division, on behalf of the Utilities Division of the Arizona Corporation Commission.

BY THE COMMISSION:

On September 28, 2015, Arroyo Water Company, Inc. ("Arroyo" or "Company") filed an application with the Arizona Corporation Commission ("Commission") for approval of an emergency rate increase in the amount of $72,000, or a 158.14 percent increase over the Company's reported 2014 revenues of $45,528. The application states the Company is insolvent, its water system is in need of repairs, and the system has immediate emergencies.

On September 30, 2015, by Procedural Order, a procedural conference was scheduled to commence on October 15, 2015, to discuss scheduling and other procedural issues associated with the emergency rate case application.

On October 15, 2015, a procedural conference was held as scheduled. The Commission's Utilities Division ("Staff") appeared through counsel and Mr. Michael Armstead, the Company's owner, appeared on behalf of Arroyo. Discussions were held related to scheduling a hearing on the application, the timing for filing the Staff Report, and responses thereto.

On October 22, 2015, Staff filed a Request to Transfer ("Request"), stating that Arroyo's emergency rate case application had been filed using an incorrect company identification number and requesting that the application be transferred to the above-captioned docket. Staff also requested that the Company's name be corrected to read Arroyo Water Company, Inc. rather than Arroyo Water Company, LLC.

On November 3, 2015, a Procedural Order was issued scheduling a hearing to commence in this matter on December 7, 2015, and establishing other procedural requirements and deadlines, including a requirement for Arroyo to provide specific notice to its customers by November 13, 2015, and to file its certification of notice as well as any response to the Staff Report by November 30, 2015. Further, Staff's Request to transfer Arroyo's rate application to this docket and to correct the Company's name was granted.

On November 16, 2015, Staff filed its Staff Report, recommending approval of Staff's alternative emergency rate increase.

On that same date, Arroyo filed its Certification of Mailing the Public Notice to customers.

On December 7, 2015, a full evidentiary hearing was held before a duly authorized Administrative Law Judge of the Commission. Staff appeared through counsel and Mr. Michael Armstead appeared on behalf of Arroyo. Arroyo and Staff presented documentary evidence and testimony. No members of the public were present to give comments on the application. At the conclusion of the hearing, the matter was taken under advisement pending submission of a Recommended Opinion and Order to the Commission.

* * * * * * * * * *

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

FINDINGS OF FACT

1. Arroyo is an Arizona Class E utility that provides water service to approximately 122 customers in a community known as Tonto Basin, which is located near Payson, Arizona in Gila

County.[1] Arroyo's Certificate of Convenience and Necessity ("CC&N") encompasses approximately 1,925 acres.[2]

2. On September 28, 2015, Arroyo filed an application with the Commission for approval of an emergency rate increase in the amount of $72,000 or a 158.14 percent increase over the Company's reported 2014 revenues of $45,528. The application states the Company is insolvent, its water system is in need of repairs, and the system has immediate emergencies.

3. Notice of the application was given in accordance with the Procedural Order issued on November 3, 2015.

4. According to the Company's representative, Arroyo was recently acquired by Management Systems, LLC through a stock purchase transaction on July 1, 2015.[3] Management Systems, LLC is owned by Mr. Michael Armstead, who has more than 11 years' experience in water and wastewater utility operations.[4]

5. Staff stated that the Company's water system consists of a single well; two well pumps, with a combined yield of 90 gallons per minute ("GPM"); one 11,000 gallon storage tank; three booster pumps; one 2,500 gallon pressure tank; and a distribution system.[5] Staff also stated the system has a single master meter located downstream of its storage tank.[6]

6. Based on Arroyo's 2014 Annual Report, the Company had a seasonal peak usage of 1,451,502 gallons sold, for an average of 378 gallons per day ("GPD"), per connection.[7] Staff believes that the Company's current well (with an estimated yield of 90 gallons per minute) can adequately serve Arroyo's current customers as well as reasonable growth.[8] Staff stated that based on the Company's reported 2014 water use data and well capacity analysis, Staff believes no minimum storage is required on the system to meet seasonal peak demand.[9] However, Staff was unable to determine the actual well production because Staff believes there is a leak at the bottom of

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[1] Exhibit S-3, Engineering Report at 1.
[2] *Id.*
[3] Statements made by Mr. Michael Armstead during a Procedural Conference held on October 15, 2015.
[4] Exhibit S-1.
[5] Exhibit S-3, Engineering Report at 1.
[6] *Id.*
[7] *Id.*
[8] *Id.*
[9] *Id.*

the storage tank, and the Company's well meter, located downstream, is unable to determine Arroyo's water loss.[10] Therefore, Staff recommends that the Company install a two-inch master meter between the well pump and inlet to the storage tank in order to calculate the Company's water loss.[11]

7. According to an ADEQ Compliance Status Report, dated October 2, 2015, Company has no major deficiencies and the Company's water system is currently delivering water that meets water quality standards as required by 40 C.F.R. 14 and Arizona Administrative Code Title 18, Chapter 4.[12]

8. The Company's water system is not located in an Arizona Department of Water Resources ("ADWR") Active Management Area ("AMA"). ADWR has determined that the Company's water system is not in compliance with ADWR requirements due to the Company's failure to file its Annual Reports and a System Water Plan.[13]

9. Arroyo has no delinquent compliance items with the Commission.[14]

10. Arroyo has an approved Curtailment Tariff on file with the Commission.[15] The Company does not have an approved Backflow Prevention Tariff.[16]

11. The Company's application indicated that its current rates do not provide sufficient revenues to pay for needed repairs, plant additions, and that the Company is insolvent.[17] The Company's application stated there is a need to replace its existing water storage to obtain a minimum of 113,000 gallons of storage, install additional mainline to alleviate hydraulic loading and to maintain adequate water pressure; and the need to replace various electrical controls.[18] The Company did not provide cost estimates for the repairs.[19]

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[10] Exhibit S-3, Engineering Report at 2.
[11] *Id.*
[12] *Id.*
[13] Exhibit S-3, Engineering Report at 2.
[14] *Id.*
[15] *Id.*
[16] *Id.*
[17] Exhibit S-2 at 8.
[18] *Id.*
[19] *Id.*

12. Staff stated that most of the items listed in the Company's application are long-lived plant items. Staff concluded that the Company's request for emergency rates in the amount of $72,000 was intended to cover the cost of long-lived plant additions or replacement of plant rather than for the current on-going operational needs of the Company.[20] Staff also stated that requests for emergency rate increases should only address current operational needs.[21] Staff stated that due to the long-term nature of these investments, Staff believes they would be more appropriately funded through long-term financing and that the Company should file a finance application.[22] According to Staff, under the Company's proposal the monthly bill per customer would increase by $49.00.[23]

13. Staff stated emergency or interim rates are appropriate when any or all of the following conditions exists: a sudden change that causes hardship to a company; a company is insolvent; or a company's ability to maintain service (pending a formal rate determination) is in serious doubt. Staff also states that these criteria have been affirmed by Arizona Courts.[24]

14. Staff stated that the Company's application provided scant information related to its revenues and expenses. Staff stated that the Company has not filed an Annual Report with the Commission since 2007, but provided a 2014 Annual Report that showed the Company had revenues of $45,528, and expenses of $52,317, for an operating loss of $6,789.[25] Upon Staff's request, the Company also provided a print-out showing details of transactions made by the Company for the year ending December 31, 2014 ("Detailed Report").[26] Staff stated that there were discrepancies between the revenues and expenses recorded in the 2014 Annual Report and that of the Detailed Report.[27] Staff stated the Company's Detailed Report showed revenues of $40,607.67, expenses of $10,756.43, and a net income of $29,851.24.[28] Staff concluded that the Detailed Report was a more reliable indicator of the Company's operational needs.[29]

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[20] Exhibit S-3 at 2.
[21] *Id.*
[22] *Id.*
[23] *Id.* at 3.
[24] *See, Scates v. Arizona Corporation Commission*, 118 Ariz. 531 (Ct. App. 1978) and *Residential Utility Consumer Office v. Arizona Corporation Commission*, 199 Ariz. 588 (2001).
[25] Exhibit S-3 at 3.
[26] *Id.*
[27] *Id.*
[28] *Id.*
[29] *Id.*

15. In addition to the expenses listed in the Company's Detailed Report, Staff determined that the Company has the following additional categories of on-going expenses:

a.	Purchased Power	$ 5,000.00
b.	Chemicals	$ 100.00
c.	Repairs and Maintenance	$ 6,100.00
d.	Office Supplies and Expense	$ 1,464.00
e.	Outside Services	$12,000.00
f.	Water Testing	$ 1,030.00
g.	Rents & Telephone	$ 7,200.00
h.	Transportation Expense	$ 1,200.00
i.	Past Due Property Taxes[30]	$ 6,371.00
j.	Property Taxes (current)	$ 1,738.00
k.	Additional Cash Flow	$ 6,000.00[31]

16. Staff's recommended adjustments to revenues and expenses will generate additional funding in the amount of $16,402.[32]

17. Based on the above information, Staff concluded that the Company is operationally insolvent and that an emergency increase in revenues in the amount of $16,402 is required.[33] Staff recommends that the additional amount be recovered through an emergency interim surcharge in the amount of $11.20 per customer, per month, rather than the Company's proposed increase in its current tiered rates.[34] Staff's estimated emergency increase in revenues reflects an increase of 51.50 percent, over Staff's adjusted revenues of $31,846.[35]

18. Staff disagrees with the Company's proposed increase in its tiered rates. Staff explained that tiered rates are calculated using historical water usage data by tiers, that bill count information is not required in an interim emergency rate application, and that without bill count information there is no way to predict the revenues that will be generated by the Company's proposed rate design.[36] Staff stated that it believes the interim monthly surcharge, calculated on a fixed monthly amount, will allow the Company to have a more predictable cash flow and sufficient revenue to cover operating and maintenance expenses as well as contingencies.[37]

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[30] One-half of the amount due.
[31] Exhibit S-3 at 4.
[32] *Id.*
[33] Exhibit S-3 at 4.
[34] *Id.*
[35] *Id.*
[36] *Id.* at 5.
[37] *Id.*

19. According to Staff, emergency rate case procedures require that the Company provide a bond sufficient to cover a refund of the interim rates.[38] Staff stated that the bond requirement typically serves as a means to ensure a refund of the interim rates to ratepayers if it is later determined that the interim rates were not necessary or only partially necessary.[39] However, Staff believes that the entire amount of the emergency rate increase does not need to be covered by a bond and therefore Staff recommends the Company be required to obtain a bond or Irrevocable Standby Letter of Credit in the amount of $10.00.[40]

20. Staff recommends:

a. Approval of an emergency interim rate surcharge of $11.20 per connection, per month.

b. The interim rates approved in this case remain interim until permanent rates are established in the Company's next rate case filing.

c. No change to the Company's current commodity charges, miscellaneous service charges, and service and meter installation charges.

d. Arroyo file semi-annually proof that it has made its delinquent property taxes payments until the obligation is paid in full.[41]

e. Arroyo obtain a bond or an Irrevocable Standby Letter of Credit in the amount of $10.00.

f. Arroyo file a full rate case application no later than 24 months after the effective date of the interim emergency rates, using the most recent test year.

g. Arroyo maintain records as required for a permanent rate application (including details of water usage, copies of all invoices and other cost documentation supporting the rates requested).

h. Arroyo file with Docket Control, within 90 days of the effective date of this Decision, as a compliance item in this docket, documentation demonstrating that a wellhead meter has been installed between the well pump and the inlet to the Company's storage tank.

21. The Company's witness stated that the Company believes Staff's recommended interim surcharge amount of $11.20 will not generate sufficient revenues for the Company to manage

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[38] Exhibit S-3 at 4-5.
[39] *Id.*
[40] *Id.*
[41] The Company is six years delinquent on its property taxes and Staff has included funding in emergency rates to pay these past due taxes.

operations and to make necessary repairs.[42] In its application the Company proposed an inverted three tiered rate design, which would have increased commodity rates and monthly minimum charges based on volume and meter size.[43] The Company argued that Staff's proposed interim surcharge would not generate sufficient revenues to cover the Company's operational expenses during its peak summer month of July because power costs will double.[44] However, the Company's witness conceded that predicting revenues generated from volumetric rates would be difficult to calculate at this time because the Company does not have "good numbers" showing the Company's actual operating expenses.[45] The witness also conceded that based on the Company's documentation, Arroyo could only identify approximately $10,000 in operating expenses, and that Staff took into consideration other operational expenses Staff believed appropriate and calculated those additional operating expenses in setting its recommended emergency interim surcharge. Staff recommends an increase of $16,402 over Staff's adjusted current revenues for a total of $48,248.[46]

22. Based on our review of the record in this case, and subject to Staff's recommendations as set forth above, we find that approval of Staff's recommended emergency interim surcharge in the amount of $11.20 per customer, per month, is reasonable and in the public interest. We also find Staff's recommended interim surcharge is an appropriate method to generate a predictable cash flow for the Company until new permanent rates can be established for Arroyo. The evidence presented in this case shows that the Company's current rates are insufficient to produce the cash flow necessary to cover the Company's current operating expenses, needed plant repairs, or to manage contingencies. We find that the emergency interim surcharge will provide the Company with predictable revenues, which is important to the Company's ability to maintain reliable service for its customers.

23. Staff's recommendations are reasonable and will be adopted.

CONCLUSIONS OF LAW

1. Arroyo is a public service corporation within the meaning of Article XV of the

[42] Tr. at 10.
[43] Exhibit S-2 at 4.
[44] Tr. at 12.
[45] Tr. at 13.
[46] Exhibit S-3 at 4.

Arizona Constitution and A.R.S. § 250.

2. The Commission has jurisdiction over Arroyo and the subject matter of the application.

3. Notice of the application was provided as prescribed by law.

4. Arroyo is facing an emergency within the definition set forth in AG Opinion No. 71-17.

5. The emergency interim surcharge approved herein is reasonable and in the public interest subject to Staff's recommendations as set forth herein.

ORDER

IT IS THEREFORE ORDERED that Arroyo Water Company, Inc. is authorized to charge a monthly emergency interim surcharge in the amount of $11.20 per connection, as conditioned on the following ordering paragraphs.

IT IS FURTHER ORDERED that the monthly emergency interim surcharge approved herein shall be interim and subject to refund until permanent rates are established in Arroyo Water Company, Inc.'s next rate case.

IT IS FURTHER ORDERED that Arroyo Water Company, Inc. shall, prior to implementing the monthly emergency interim surcharge approved herein, provide to the Commission's Business Office either a performance bond or Irrevocable Standby Letter of Credit in the amount of $10.00.

IT IS FURTHER ORDERED that Arroyo Water Company, Inc. shall, on the same date the performance bond or Irrevocable Standby Letter of Credit is provided to the Commission's Business Office, file with the Commission's Docket Control, as a compliance item in this docket, an original and 13 copies of a notice stating that the performance bond or Irrevocable Standby Letter of Credit has been provided to the Commission's Business Office.

IT IS FURTHER ORDERED that the emergency interim surcharge shall become effective on March 1, 2016, or on the first day of the month following Arroyo Water Company, Inc.'s compliance with the requirements to provide either a performance bond or Irrevocable Standby Letter of Credit in the amount of $10.00 to the Commission's Business Office and to file notice thereof, whichever is later.

IT IS FURTHER ORDERED that Arroyo Water Company, Inc. shall, within 30 days after the effective date of this Decision, mail or deliver notice of the approved monthly emergency interim surcharge to its customers, in a form and manner acceptable to Staff, by means of an insert in Arroyo Water Company's next regularly scheduled billing.

IT IS FURTHER ORDERED that Arroyo Water Company, Inc. shall, by February 29, 2016, file with the Commission's Docket Control, as a compliance item in this docket, a revised tariff reflecting the approved monthly emergency interim surcharge.

IT IS FURTHER ORDERED that Arroyo Water Company, Inc. shall, no later than 24 months after the effective date of this Decision, in a new docket, file with the Commission's Docket Control an original and 13 copies of a full permanent rate case application prepared using the most recent test year.

IT IS FURTHER ORDERED that the monthly emergency interim surcharge approved herein shall be interim and that funds collected through the emergency surcharge rate are subject to true-up and refund pending the Decision resulting from the permanent rate case application Arroyo Water Company, Inc. is required to file pursuant to this Decision.

IT IS FURTHER ORDERED that Arroyo Water Company, Inc.'s existing commodity charges, miscellaneous service charges, and service and meter installation charges shall remain in effect until further Order of the Commission.

IT IS FURTHER ORDERED that Arroyo Water Company, Inc. shall file semi-annually, with Docket Control, as a compliance item in this docket, proof that it has been making regular payments on its delinquent property taxes, until such time as the Company's obligation is paid in full.

IT IS FURTHER ORDERED that Arroyo Water Company, Inc. shall maintain its records as required for a permanent rate application (including details of water usage, copies of all invoices and other cost documentation supporting the rates requested).

IT IS FURTHER ORDERED that on a going-forward basis, Arroyo Water Company, Inc. shall maintain its accounting records in accordance with the National Association of Regulatory Utility Commissioners standards.

IT IS FURTHER ORDERED that Arroyo Water Company, Inc. shall file with Docket Control, within 90 days of the effective date of this Decision, as a compliance item in this docket, documentation demonstrating that a wellhead meter has been installed between the well pump and the inlet to the Company's storage tank.

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

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN COMMISSIONER

COMMISSIONER COMMISSIONER COMMISSIONER

IN WITNESS WHEREOF, I, JODI JERICH, Executive Director of the Arizona Corporation Commission, have hereunto set my hand and caused the official seal of the Commission to be affixed at the Capitol, in the City of Phoenix, this _____ day of _____ 2016.

JODI JERICH
EXECUTIVE DIRECTOR

DISSENT _____

DISSENT _____
YK:ru(tv)

SERVICE LIST FOR: ARROYO WATER COMPANY, INC.

DOCKET NO.: W-04286A-15-0339

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