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**BEFORE THE ARIZONA CORPORATION**

Arizona Corporation Commission

COMMISSIONERS

DOCKETED

DOUG LITTLE – Chairman  
BOB STUMP  
BOB BURNS  
TOM FORESE  
ANDY TOBIN

FEB 11 2016

DOCKETED BY *KE*

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. 75452

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.

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

6 On November 3, 2015, a Procedural Order was issued scheduling a hearing to commence in  
 7 this matter on December 7, 2015, and establishing other procedural requirements and deadlines,  
 8 including a requirement for Arroyo to provide specific notice to its customers by November 13, 2015,  
 9 and to file its certification of notice as well as any response to the Staff Report by November 30,  
 10 2015. Further, Staff’s Request to transfer Arroyo’s rate application to this docket and to correct the  
 11 Company’s name was granted.

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

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

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

21 \* \* \* \* \*

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

24 **FINDINGS OF FACT**

25 1. Arroyo is an Arizona Class E utility that provides water service to approximately 122  
 26 customers in a community known as Tonto Basin, which is located near Payson, Arizona in Gila  
 27  
 28

1 County.<sup>1</sup> Arroyo's Certificate of Convenience and Necessity ("CC&N") encompasses approximately  
2 1,925 acres.<sup>2</sup>

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

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

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

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

17 6. Based on Arroyo's 2014 Annual Report, the Company had a seasonal peak usage of  
18 1,451,502 gallons sold, for an average of 378 gallons per day ("GPD"), per connection.<sup>7</sup> Staff  
19 believes that the Company's current well (with an estimated yield of 90 gallons per minute) can  
20 adequately serve Arroyo's current customers as well as reasonable growth.<sup>8</sup> Staff stated that based  
21 on the Company's reported 2014 water use data and well capacity analysis, Staff believes no  
22 minimum storage is required on the system to meet seasonal peak demand.<sup>9</sup> However, Staff was  
23 unable to determine the actual well production because Staff believes there is a leak at the bottom of

24 <sup>1</sup> Exhibit S-3, Engineering Report at 1.

25 <sup>2</sup> *Id.*

26 <sup>3</sup> Statements made by Mr. Michael Armstead during a Procedural Conference held on October 15, 2015.

27 <sup>4</sup> Exhibit S-1.

28 <sup>5</sup> Exhibit S-3, Engineering Report at 1.

<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> *Id.*

1 the storage tank, and the Company's well meter, located downstream, is unable to determine  
 2 Arroyo's water loss.<sup>10</sup> Therefore, Staff recommends that the Company install a two-inch master  
 3 meter between the well pump and inlet to the storage tank in order to calculate the Company's water  
 4 loss.<sup>11</sup>

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

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

13 9. Arroyo has no delinquent compliance items with the Commission.<sup>14</sup>

14 10. Arroyo has an approved Curtailment Tariff on file with the Commission.<sup>15</sup> The  
 15 Company does not have an approved Backflow Prevention Tariff.<sup>16</sup>

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

22  
 23  
 24 <sup>10</sup> Exhibit S-3, Engineering Report at 2.

25 <sup>11</sup> *Id.*

26 <sup>12</sup> *Id.*

27 <sup>13</sup> Exhibit S-3, Engineering Report at 2.

28 <sup>14</sup> *Id.*

<sup>15</sup> *Id.*

<sup>16</sup> *Id.*

<sup>17</sup> Exhibit S-2 at 8.

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

1           12. Staff stated that most of the items listed in the Company's application are long-lived  
 2 plant items. Staff concluded that the Company's request for emergency rates in the amount of  
 3 \$72,000 was intended to cover the cost of long-lived plant additions or replacement of plant rather  
 4 than for the current on-going operational needs of the Company.<sup>20</sup> Staff also stated that requests for  
 5 emergency rate increases should only address current operational needs.<sup>21</sup> Staff stated that due to the  
 6 long-term nature of these investments, Staff believes they would be more appropriately funded  
 7 through long-term financing and that the Company should file a finance application.<sup>22</sup> According to  
 8 Staff, under the Company's proposal the monthly bill per customer would increase by \$49.00.<sup>23</sup>

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

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

23 \_\_\_\_\_  
<sup>20</sup> Exhibit S-3 at 2.

24 <sup>21</sup> *Id.*

25 <sup>22</sup> *Id.*

26 <sup>23</sup> *Id.* at 3.

27 <sup>24</sup> *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).

28 <sup>25</sup> Exhibit S-3 at 3.

29 <sup>26</sup> *Id.*

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> *Id.*

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

|    |  |                           |
|----|--|---------------------------|
| 3  | a. Purchased Power                       | \$ 5,000.00               |
| 4  | b. Chemicals                             | \$ 100.00                 |
| 5  | c. Repairs and Maintenance               | \$ 6,100.00               |
| 6  | d. Office Supplies and Expense           | \$ 1,464.00               |
| 7  | e. Outside Services                      | \$12,000.00               |
| 8  | f. Water Testing                         | \$ 1,030.00               |
| 9  | g. Rents & Telephone                     | \$ 7,200.00               |
| 10 | h. Transportation Expense                | \$ 1,200.00               |
| 11 | i. Past Due Property Taxes <sup>30</sup> | \$ 6,371.00               |
| 12 | j. Property Taxes (current)              | \$ 1,738.00               |
| 13 | k. Additional Cash Flow                  | \$ 6,000.00 <sup>31</sup> |

14           16.    Staff's recommended adjustments to revenues and expenses will generate additional  
15 funding in the amount of \$16,402.<sup>32</sup>

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

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

<sup>30</sup> One-half of the amount due.

<sup>31</sup> Exhibit S-3 at 4.

<sup>32</sup> *Id.*

<sup>33</sup> Exhibit S-3 at 4.

<sup>34</sup> *Id.*

<sup>35</sup> *Id.*

<sup>36</sup> *Id.* at 5.

<sup>37</sup> *Id.*

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

8           20.     Staff recommends:

- 9           a.     Approval of an emergency interim rate surcharge of \$11.20 per connection, per  
 10 month.
- 11           b.     The interim rates approved in this case remain interim until permanent rates  
 12 are established in the Company's next rate case filing.
- 13           c.     No change to the Company's current commodity charges, miscellaneous  
 14 service charges, and service and meter installation charges.
- 15           d.     Arroyo file semi-annually proof that it has made its delinquent property taxes  
 16 payments until the obligation is paid in full.<sup>41</sup>
- 17           e.     Arroyo obtain a bond or an Irrevocable Standby Letter of Credit in the amount  
 18 of \$10.00.
- 19           f.     Arroyo file a full rate case application no later than 24 months after the  
 20 effective date of the interim emergency rates, using the most recent test year.
- 21           g.     Arroyo maintain records as required for a permanent rate application  
 22 (including details of water usage, copies of all invoices and other cost  
 23 documentation supporting the rates requested).
- 24           h.     Arroyo file with Docket Control, within 90 days of the effective date of this  
 25 Decision, as a compliance item in this docket, documentation demonstrating  
 26 that a wellhead meter has been installed between the well pump and the inlet to  
 27 the Company's storage tank.

28           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

<sup>38</sup> Exhibit S-3 at 4-5.

<sup>39</sup> *Id.*

<sup>40</sup> *Id.*

<sup>41</sup> The Company is six years delinquent on its property taxes and Staff has included funding in emergency rates to pay these past due taxes.

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

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

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

### CONCLUSIONS OF LAW

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

26 <sup>42</sup> Tr. at 10.

27 <sup>43</sup> Exhibit S-2 at 4.

<sup>44</sup> Tr. at 12.

<sup>45</sup> Tr. at 13.

28 <sup>46</sup> Exhibit S-3 at 4.

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

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

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

5 4. Arroyo is facing an emergency within the definition set forth in AG Opinion No. 71-  
6 17.

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

9 **ORDER**

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

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

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

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

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

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

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

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

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

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

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

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

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

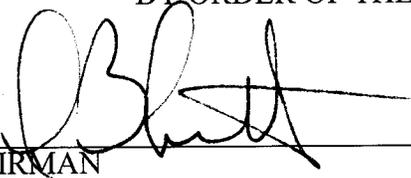
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IT IS FURTHER ORDERED that Arroyo Water Company, Inc. shall file with Docket Control, within 90 days of the effective date of this Decision, as a compliance item in this docket, documentation demonstrating that a wellhead meter has been installed between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

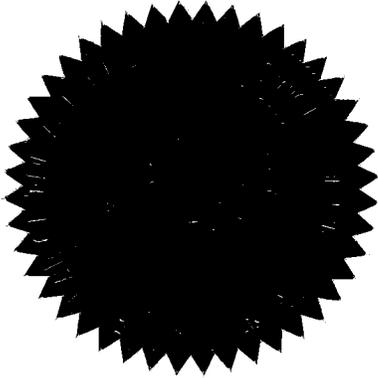
  
CHAIRMAN

  
COMMISSIONER

  
COMMISSIONER

  
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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 11th day of February 2016.

  
JODI JERICH  
EXECUTIVE DIRECTOR

DISSENT \_\_\_\_\_

DISSENT \_\_\_\_\_  
YK:ru(tv)

1 SERVICE LIST FOR: ARROYO WATER COMPANY, INC.

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

3 Michael Armstead  
4 ARROYO WATER COMPANY LLC  
5 211 W. Saddle Lane  
6 Payson, AZ 85541

7 Janice Alward, Chief Counsel  
8 Legal Division  
9 ARIZONA CORPORATION COMMISSION  
10 1200 West Washington Street  
11 Phoenix, AZ 85007

12 Thomas Broderick, Director  
13 Utilities Division  
14 ARIZONA CORPORATION COMMISSION  
15 1200 West Washington Street  
16 Phoenix, AZ 85007

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