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BEFORE THE ARIZONA CORPORATION COMMISSION

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COMMISSIONERS

KRISTIN K. MAYES, Chairman
GARY PIERCE
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BOB STUMP

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AZ CORP COMMISSION
DOCKET CONTROL

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**NOTICE OF FILING
REJOINDER TESTIMONY AND
REJOINDER SCHEDULES**

Arizona-American Water Company ("Arizona-American") hereby files testimony in the above-captioned case from the following five witnesses:

- Ian C. Crooks
- Linda J. Gutowski
- Sheryl L. Hubbard
- Bente Villadsen
- John C. (Jake) Lenderking

Arizona Corporation Commission

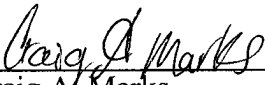
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KIC

- Arizona-American also files the attached rejoinder schedules.

RESPECTFULLY SUBMITTED on March 11, 2009.



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Courtney Appelhans

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman
GARY PIERCE
PAUL NEWMAN
SANDRA D. KENNEDY
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IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

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**REJOINDER TESTIMONY
OF
IAN C. CROOKS
ON BEHALF OF
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MARCH 11, 2009**

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1 **EXECUTIVE SUMMARY**

2 Mr. Crooks testifies as follows:

3 Mr. Crooks answers the eleven questions posed by Mr. Olea in his rebuttal testimony concerning
4 Arizona-American's proposal to amend its Water Facilities Hook-Up Fee WHU-1, for its Agua
5 Fria Water District. The responses to questions 5, 9 and 10 discuss the core issues. Generally,
6 most of the other changes in Arizona-American's proposed tariff were to conform the existing
7 tariff to the Off-Site Water Hook-up Fee tariff ("ACC HUF Template"), dated January 8, 2009,
8 as posted on the Commission's website.

9
10 Arizona-American believes the term "Common Facilities" is more descriptive and less subject to
11 confusion or misinterpretation than is "Off-Site Facilities." The physical location of water
12 facilities constructed and/or funded by the HUF does not necessarily determine whether the
13 facilities are for the exclusive benefit of a particular development or are for the benefit of
14 multiple developments.

15
16 Arizona-American is proposing to split within a single tariff the current unified hook-up fee into
17 two components, the original 2004 HUF amount as "Component A" and the incremental increase
18 in the current 2007 HUF as "Component B". Component A will continue to be used to pay for
19 Arizona-American's existing and future investment in Common Facilities and will be eligible for
20 offset against Applicant built Common Facilities. Component B will be solely used to pay for
21 Arizona-American's White Tanks Surface Water Treatment Facility ("WTSWTF") investment
22 and will not be eligible for offset against Applicant built Common Facilities. If this change is
23 not made, the cash receipts to Arizona-American needed to pay for the WTSWTF will be
24 delayed out many years.

1 I

2 II **INTRODUCTION**

3 Q. **PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND TELEPHONE**
4 **NUMBER.**

5 A. My name is Ian C. Crooks. My business address is 19820 N. 7th Street, Suite 201,
6 Phoenix, Arizona 85024, and my telephone number is 623-445-2404.

7 Q. **BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

8 A. I am employed by Arizona-American Water Company (“Arizona-American”) as
9 Engineering Manager of Developer Services for Arizona and New Mexico.

10 Q. **PLEASE BRIEFLY OUTLINE YOUR RESPONSIBILITIES IN ARIZONA AS**
11 **THE ENGINEERING MANAGER OF DEVELOPER SERVICES.**

12 A. I am responsible for the developer agreements (“LXA/MXA”), design, planning,
13 construction, budgeting, and compliance related to development activity.

14 Q. **PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND.**

15 A. I received a Bachelor of Science degree from Pennsylvania State University in
16 environmental engineering.

17 Q. **HAVE YOU HAD ANY OTHER FORMAL TRAINING?**

18 A. I am currently certified as an ADEQ Grade 2 Water Distribution System Operator and I
19 have completed several masters-degree level courses.

20 Q. **PLEASE DESCRIBE YOUR PROFESSIONAL EXPERIENCE.**

21 A. I joined Arizona-American in October 2006. I was previously employed from 2005 to
22 2006 by Ryan Homes, a home builder in Pennsylvania, as the Land Development
23 Manager. Before that, I was employed by Pennsylvania-American Water Company as
24 Sr. Engineer for the Coatesville, Pennsylvania district. Prior to that, I was employed

1 from 1996 in the same role and as IT Manager for the City of Coatesville Authority,
2 which was acquired by Pennsylvania-American Water Company. Before that, I was
3 Engineering Supervisor for Erie City Water Authority. Throughout my career I've
4 gained extensive experience in water and wastewater operations, management, and
5 administration.

6 **Q. ARE YOU A REGISTERED PROFESSIONAL ENGINEER?**

7 A. Yes, I am a registered Professional Engineer in the states of Arizona and Pennsylvania.

8 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THIS COMMISSION?**

9 A. No.

10 **Q. WHAT IS THE PURPOSE OF YOUR REJOINDER TESTIMONY?**

11 A. The purpose of my rejoinder testimony is to answer the eleven questions posed by Mr.
12 Olea in his Surrebuttal testimony concerning Arizona-American's proposal to amend its
13 Water Facilities Hook-Up Fee WHU-1, for its Agua Fria Water District. In general, I
14 now sponsor the details of a proposal which was first presented in Mr. Broderick's
15 Rebuttal testimony which started on page 3, line 22 thru page 4, line 26.

16 **Q. HOW IS YOUR TESTIMONY ORGANIZED?**

17 A. I will answer Mr. Olea's eleven questions in order, although questions 5, 9 and 10 are the
18 core issues.

19 **III ANSWERS TO QUESTIONS POSED BY STEVEN M. OLEA**

20 **Q. 1. WHAT IS THE PURPOSE OF COMBINING THE APPLICABILITY AND**
21 **PURPOSE PORTIONS OF THE TARIFF AND CHANGING THE WORDING?**

22 A: Arizona-American based the proposed revised Water Facilities Hook-up Fee WHU-1
23 tariff ("AAW Proposed HUF") on the Off-Site Water Hook-up Fee tariff ("ACC HUF
24 Template"), dated January 8, 2009, as posted on the Commission's website. Arizona-

1 American assumes the structure and language of the ACC HUF Template is to be used as
2 the base for new HUF tariffs. In addition, the ACC HUF Template clarified policies and
3 vague language contained in Arizona-American's existing Water Facilities Hook-up Fee
4 WHU-1 tariff. Comparing the AAW Proposed HUF to the ACC HUF Template
5 addresses this question and several of Mr. Olea's following questions.

6 The Applicability and Purpose is combined in the ACC HUF Template. Arizona-
7 American is proposing only minor changes to this paragraph to be consistent with
8 subsequent changes in the AAW Proposed HUF.

9 **Q: 2. WHAT IS THE PURPOSE OF CHANGING THE WORDING IN THE FIRST**
10 **PARAGRAPH UNDER DEFINITIONS?**

11 A: Please see my response to question 1. No changes were made to the wording of the first
12 paragraph between the AAW Proposed HUF and the ACC HUF Template.

13 **Q: 3. WHAT IS THE PURPOSE OF ADDING APPLICANT TO THE**
14 **DEFINITIONS?**

15 A: Please see my response to question 1. The Applicant definition was part of the ACC
16 HUF Template.

17 **Q: 4. WHAT IS THE PURPOSE OF CHANGING THE WORDING IN THE**
18 **DEFINITION OF MAIN EXTENSION AGREEMENT ("MXA")?**

19 A: Please see my response to question 1. The definition of Main Extension Agreement
20 ("MXA") is part of the ACC HUF template. Arizona-American made only minor
21 changes to this paragraph to be consistent with subsequent changes in the AAW Proposed
22 HUF tariff.

1 **Q: 5. WHAT IS THE PURPOSE OF REPLACING THE TERM OFF-SITE**
2 **FACILITIES WITH COMMON FACILITIES AND CHANGING THE**
3 **WORDING?**

4 A: The purpose is to clarify that physical location of water facilities constructed and/or
5 funded by the HUF does not necessarily determine whether the facilities are for the
6 exclusive benefit of a particular development or are for the benefit of multiple
7 developments. The term "Off-Site Facilities", as used in the ACC HUF Template
8 appears to reference facilities that, despite their physical location, are to benefit multiple
9 developments. For that reason, Arizona-American believes the term "Common
10 Facilities" is more descriptive and less subject to confusion or misinterpretation than is
11 "Off-Site Facilities."

12 **Q: 6. WHAT IS THE PURPOSE OF CHANGING THE WORDING IN THE**
13 **DEFINITION OF SERVICE CONNECTION?**

14 A: Please see my response to question 1. No changes were made to the definition of Service
15 Connection between the AAW Proposed HUF and the ACC HUF Template.

16 **Q: 7. WHAT IS THE PURPOSE OF CHANGING THE WORDING IN THE**
17 **DEFINITION OF SERVICE CONNECTION?**

18 A: This is a repeat of question 1.6. Please see my answer to that question.

19 **Q: 8. IN THE FIRST PARAGRAPH UNDER TIME OF PAYMENT, WHY IS**
20 **PAYMENT REQUIRED 15 DAYS AFTER THE MXA IS APPROVED AND NOT**
21 **AT THE TIME OF THE PAYMENT FOR THE MXA?**

22 A: Please see my response to question 1. The change was part of the ACC HUF Template.
23 Arizona-American made only minor changes to this paragraph to be consistent with
24 subsequent changes in the AAW Proposed HUF tariff.

1 **Q: 9. WHY IS THE COMPANY PROPOSING THAT ONLY COMPONENT A BE**
2 **ELIGIBLE FOR OFFSET? DOES THIS MEAN THAT THE MXAS ENTERED**
3 **INTO BY THE COMPANY WILL NOT REQUIRE AN APPLICANT TO**
4 **PROVIDE ANY SOURCE OF WATER, SINCE AN APPLICANT WILL**
5 **ALREADY BE PROVIDING FOR ITS SOURCE OF WATER UNDER**
6 **COMPONENT B (THE PORTION PAYING FOR THE WHITE TANKS**
7 **SURFACE WATER TREATMENT FACILITY)?.**

8 **A:** The White Tanks surface water treatment facility will reduce the need as much as
9 possible for new wells and related infrastructure to meet growing demand - filling a
10 significant portion of that demand with renewable surface water - but, it will not
11 eliminate the need for new ground water entirely. In certain cases, the individual
12 developer (i.e., applicant) will continue to be required to provide a source of water and
13 related infrastructure. The benefits of the White Tanks surface water treatment facility to
14 the Applicant, depending on the Applicant's development water demands, timing and
15 location within the service area, include the following: (1) no requirement for a water
16 source at all; (2) water source required but only to meet average day demands versus
17 maximum day demand; and (3) no requirement for a redundant water source (i.e. second
18 well).

19 Under the current hook-up fee tariff, the hook-up fee is a unified fee varying by meter
20 size. That unified fee was developed by combining the original 2004 hook-up fee and the
21 increase to the hook-up fee approved in 2007 to pay for the White Tanks surface water
22 treatment facility. While the Company internally bifurcates the accounting of the hook-
23 up fee to track the amount received for the White Tanks surface water treatment facility,
24 the overall fee is administered as a single fee to the customer. Under this single fee
25 administration of the hook-up fee, the offset of the cost of applicant-provided common
26 facilities is resulting in the offsets being applied against the entire amount of the hook-up

1 fee, including the portion of the hook-up fee intended to pay for the White Tanks surface
2 water treatment facility. The Company believes the correct application of the common
3 facilities offset is that the offsets be applicable only to the portion of the hook-up fee that
4 represents the original hook-up fee, and that the offsets are not to be applicable to that
5 portion of the hook-up fee that is intended to pay for the White Tanks surface water
6 treatment facility. Because most development occurring in the Agua Fria district requires
7 the developer to provide some level of contributed infrastructure, this unintended
8 complete offset is delaying the cash receipts to the Company to pay for the White Tanks
9 surface water treatment plant. (Please see example below.)

10 To address this issue and to make it transparent for developers, the Company is proposing
11 to split the current unified hook-up fee into two components. The original 2004 HUF
12 amount will be "Component A" and the incremental increase to pay for the White Tanks
13 surface water treatment facility will be "Component B". Component A will continue to
14 be used to pay for the Company's existing and future investment in common facilities
15 and will be eligible for offset against Applicant-provided common facilities. Component
16 B will be solely used to pay for the Company's White Tanks surface water treatment
17 facility investment and will not be eligible for offset against Applicant-provided common
18 facilities.

19 In some cases, namely those instances where the developer is required to provide
20 common facilities with a cost in excess of the total anticipated amount of the Component
21 A portion of the hook-up fees, the Company will continue to provide a "true up" payment
22 to the developer. This true-up payment will effectively cap the developer's cost for
23 common facilities (other than the White Tanks surface water treatment facility) at the
24 aggregate Component A hook-up fee. Thus, by itself, the bifurcation of the hook-up fee
25 that is being proposed will affect only the Company's cash flow from the hook-up fees; it

1 will not increase the total obligations of developers under the hook-up fees and with
 2 respect to contributed infrastructure.

3 Shown below is a development example to illustrate the cash flow difference between the
 4 current HUF tariff and the AWW Proposed HUF tariff.

5 **XYZ Development**

6 Lots: 1,000, assume 125 lots per year, 8 year build-out

7
 8 Meter Size: Assume 3/4" for all lots

9
 10 Common Facility Cost: \$1,500,000 in HUF offsets/credits

11
 12 Current HUF 3/4" fee: \$4,920 * 1,000 meters = \$4,920,000

13
 14 AWW Proposed HUF 3/4" fee: Component A:
 15 \$1,725 * 1,000 meters = \$1,725,000
 16 Component B: \$3,195 * 1,000 meters = \$3,195,000
 17 Total \$4,920,000

	Year 1	Year 2	Year 3	Year 4
Current HUF				
Offset Credit	\$ 615,000	\$ 615,000	\$ 270,000	\$ 0
Offset Credit Remaining Bal.	\$ 885,000	\$ 270,000	\$ 0	\$ 0
HUF Paid	\$ 0	\$ 0	\$ 345,000	\$ 615,000
Cumulative Cash to AAW	\$ 0	\$ 0	\$ 345,000	\$ 960,000

	Year 5	Year 6	Year 7	Year 8
Offset Credit Applied	\$ 0	\$ 0	\$ 0	\$ 0
Offset Credit Remaining Bal.	\$ 0	\$ 0	\$ 0	\$ 0
HUF Paid	\$ 615,000	\$ 615,000	\$ 615,000	\$ 615,000
Cumulative Cash to AAW	\$1,575,000	\$2,190,000	\$2,805,000	\$3,420,000

	Year 1	Year 2	Year 3	Year 4
AAW Proposed HUF				
Offset Credit (Component A)	\$ 215,625	\$ 215,625	\$ 215,625	\$ 215,625
Offset Credit Remaining Bal.	\$1,284,375	\$1,068,750	\$ 853,125	\$ 637,500
HUF Paid (Component A)	\$ 0	\$ 0	\$ 0	\$ 0
HUF Paid (Component B)	\$ 399,375	\$ 399,375	\$ 399,375	\$ 399,375
Cumulative Cash to AAW	\$ 399,375	\$ 798,750	\$1,198,125	\$1,597,500

	Year 5	Year 6	Year 7	Year 8
Offset Credit (Component A)	\$ 215,625	\$ 215,625	\$ 206,250	\$ 215,625
Offset Credit Remaining Bal.	\$ 421,875	\$ 206,250	\$ 0	\$ 0
HUF Paid (Component A)	\$ 0	\$ 0	\$ 9,375	\$ 215,625
HUF Paid (Component B)	\$ 399,375	\$ 399,375	\$ 399,375	\$ 399,375
Cumulative Cash to AAW	\$1,996,875	\$2,396,250	\$2,805,000	\$3,420,000

1 **Q: 10. THE PROPOSED TARIFF STATES (SECTION IV.D.), “THE COMPANY**
2 **AND APPLICANT MAY AGREE TO CONSTRUCTION OF ADDITIONAL**
3 **FACILITIES, WHETHER ON-SITE OR OFF-SITE OF THE APPLICANT’S**
4 **DEVELOPMENT, THAT ARE REQUIRED TO SERVE ONLY THE**
5 **APPLICANT’S DEVELOPMENT, BUT WHICH ARE NOT DISTRIBUTION**
6 **MAINS UNDER R14-2-401 AND WHICH ARE NOT SUBJECT TO REFUND**
7 **UNDER R14-2-406(D).” WHAT TYPE OF FACILITIES IS THE COMPANY**
8 **REFERRING TO THAT WOULD NOT BE REFUNDABLE UNDER**
9 **COMMISSION RULES?**

10 A: The Company is referring to water facilities such as storage tanks, booster pumps,
11 treatment facilities and transmission mains that are required for, and constructed and built
12 for, the exclusive use of a particular development. These items are not Distribution
13 Mains subject to refund under R14-2-406(D). In cases where these items are required
14 only for a single development, and not as part of an overall master area development plan
15 encompassing multiple developments, the Company is proposing that such exclusive-use
16 facilities be treated as contributions, the cost of which will not be eligible for offset
17 against hook-up fees. The Company’s rationale for this proposed treatment is that the
18 facilities do not benefit any other properties. Therefore, the cost of the facilities should
19 be borne by only those property owners who will receive the benefit of the facilities.

20
21 For example, a storage tank may be required to serve only a particular development or it
22 may be required as part of a more comprehensive master area development to serve
23 multiple developments. The Company is proposing that only the latter instances be
24 treated as “Common Facilities” subject to offset against hook-up fee payments. In cases
25 where infrastructure is required and will be used only to serve a single development, the
26 Company is proposing that the cost of that infrastructure be treated as a contribution by

1 the developer not subject to offset against any hook-up fees. Therefore, in those cases
2 where a developer is required to contribute exclusive-use infrastructure without offset of
3 hook-up fees, the overall obligations of that developer to the Company will be increased
4 by the cost of such contributed infrastructure.

5 **Q: 11. UNDER LARGE SUBDIVISION PROJECTS (SECTION IV.F.), THE**
6 **COMPANY USES THE WORD “MAY” AND “SHOULD” IN SEVERAL**
7 **PLACES. WHY DID THE COMPANY NOT USE THE WORD “SHALL”**
8 **INSTEAD?**

9 A: Please see my response to Question 1. The “may” and “should” are directly from the
10 ACC HUF template. Arizona-American made only minor changes to this paragraph to be
11 consistent with subsequent changes in the AAW Proposed HUF tariff and to add
12 additional clarification.

13 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

14 A. Yes.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman
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BOB STUMP

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**REJOINDER TESTIMONY
OF
LINDA J. GUTOWSKI
ON BEHALF OF
ARIZONA-AMERICAN WATER COMPANY
DATED MARCH 11, 2009**

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1 **EXECUTIVE SUMMARY**

2
3 Linda J. Gutowski responds to Staff and RUCO surrebuttal testimony concerning rate-base
4 issues and depreciation expense.

5 **RATE BASE – UTILITY PLANT IN SERVICE**

6 **AGUA FRIA WATER DISTRICT**

7 In Rebuttal Adjustment LJG-1R, Arizona-American is reducing the cost of the Sierra Montana
8 2.2 MG Reservoir from an estimated amount to the actual cost. This adjustment reduces Plant in
9 Service by \$252,470.

10 Staff has failed to include an upward adjustment of \$18,581 for Agua Fria projects that were
11 originally added to Sun City West Water district in error.

12 **HAVASU WATER DISTRICT**

13 Arizona-American moves the Step 2 ACRM Deferral allowed in Decision No. 70626 from
14 Utility Plant in Service to Deferred Debits. This does two things – puts the deferral where it is
15 booked, and reduces depreciation expense for Arizona-American by removing it from Plant.

16 Staff removed the Gateway Water Plant from Havasu, but erroneously left the Gateway Sewer
17 Plant in Havasu.

18 **MOHAVE WATER DISTRICT**

19 Staff still left the Mira Monte project plant out of plant in service, despite being provided the
20 invoices.

21 **PARADISE VALLEY WATER DISTRICT**

22 Both Staff and RUCO once again have incorrectly included the deferred Well No. 12 project in
23 rate base.

24 **SUN CITY WEST WATER DISTRICT**

25 Staff failed to remove \$18,581 in Agua Fria project costs that were erroneously recorded in Sun
26 City West Water District's rate base

27 **MOHAVE WASTEWATER DISTRICT**

28 Even though the Company has demonstrated that most of the construction costs were to upgrade
29 the existing capacity, both Staff and RUCO still recommend disallowances under the false
30 assumption that all construction costs were to expand capacity. There should not be any
31 disallowances of new plant which upgraded existing capacity.

32 **RATE BASE – ACCUMULATED DEPRECIATION**

33 **ALL DISTRICTS**

34 RUCO still claims without support that Arizona-American cannot change its accounting
35 methodology.

36 **RATE BASE – ADVANCES IN AID OF CONSTRUCTION**

37 **HAVASU WATER DISTRICT**

38 The advances associated with the Gateway Water Plant need to be removed from Havasu
39 Water's rate base and included in Mohave Water's rate base.

40 **RATE BASE – CONTRIBUTIONS IN AID OF CONSTRUCTION**

1 AGUA FRIA WATER DISTRICT

2 Staff and RUCO continue to include the advances and contributions related to plant that is in
3 CWIP. Arizona-American does not receive cash from developers, it receives plant. There is
4 nothing to offset existing plant in rate base, until the new plant leaves CWIP to rate base.

5
6 Staff failed to accept an adjustment of \$28,019 of Accumulated Amortization of Contributions in
7 Aid of Construction ("CIAC") that should be moved from Mohave Water to Agua Fria Water.
8 The CIAC was moved, but the associated reduction for accumulated amortization was not.

9 RATE BASE – DEFERRED DEBITS

10 HAVASU WATER DISTRICT

11 Arizona-American moved the Step 2 ACRM deferral out of Utility Plant in Service and into a
12 Regulatory Asset.

13 SUMMARY OF ARIZONA-AMERICAN'S REJOINER RATE BASE POSITIONS

	<u>Rate Base</u>
Agua Fria	\$92,049,310
Havasu	\$3,887,188
Mohave Water	\$10,235,260
Paradise Valley	\$37,398,279
Sun City West Water	\$38,382,791
Tubac Water	\$1,457,349
Mohave Wastewater	\$5,134,633

14
15 DEPRECIATION EXPENSE

16 For corporate plant, Staff incorrectly uses different depreciation rates for allocations of the same
17 plant to different districts.

18
19 Staff failed to include the following amounts in the following districts for the amortization of
20 regulatory expenses which were approved in Decision 67093:

	Amortization Exp
Agua Fria Water	\$2,918
Havasu Water	\$ 834
Mohave Water	\$9,384
Paradise Valley	\$ 72
Sun City West	\$5,841
Tubac	\$ 0
Mohave Wastewater	\$ 0

21
22 Arizona-American has supported its 15-year program of meter change-outs, so an average
23 vintage life of 6.6% is appropriate.

24
25 Arizona-American inadvertently included the Depreciation Expense of the Citizens' Acquisition
26 Adjustment in Agua Fria Water for \$230,973 and in Havasu Water for \$13,852 and has now
27 removed this expense.

1
2 Staff should have amortized Havasu Water District ACRM O&M over 12 years for an annual
3 amortization expense of \$7,916.

1 **I INTRODUCTION AND QUALIFICATIONS**

2 **Q. PLEASE STATE YOUR NAME, ADDRESS, AND TELEPHONE NUMBER.**

3 A. My name is Linda J. Gutowski. My business address is 19820 N. 7th Street, Suite 201,
4 Phoenix, Arizona 85024, and my telephone number is 623-445-2401.

5 **Q. ARE YOU THE SAME LINDA J. GUTOWSKI WHO PREVIOUSLY**
6 **SUBMITTED DIRECT AND REBUTTAL TESTIMONY IN THIS DOCKET?**

7 A. Yes.

8 **Q. WHAT IS THE PURPOSE OF YOUR REJOINDER TESTIMONY?**

9 A. I will respond to Staff and RUCO Surrebuttal testimony concerning rate-base issues.
10 Please note that I have organized my rejoinder testimony to address each of the rate base
11 topics separately by district (Sections II-VIII). Where I am silent on a topic, I continue to
12 support my positions taken in Direct testimony and as revised in Rebuttal testimony.
13 Then, I discuss depreciation expense (Section X).

14 **II RATE BASE – UTILITY PLANT IN SERVICE**

15 **A. AGUA FRIA WATER DISTRICT**

16 **Q. DO YOU HAVE ANY ADJUSTMENTS TO MAKE TO ARIZONA-AMERICAN'S**
17 **REBUTTAL?**

18 A. Yes. In Rebuttal Adjustment LJG-1R, Arizona-American is reducing the cost of the
19 Sierra Montana 2.2 MG Reservoir from an estimated amount to the actual cost. This
20 adjustment reduces Plant in Service by \$252,470. Inadvertently, this amount did not get
21 subtracted from the total. Please see Schedule B-2 Rejoinder attached.

22 **Q. ARE THERE ANY OBSERVATIONS YOU WOULD LIKE TO MAKE ABOUT**
23 **THE OTHER PARTIES' POSITIONS THAT YOU HAVE NOT ALREADY**
24 **ADDRESSED IN REBUTTAL?**

1 A. Yes. Staff has failed to include an upward adjustment of \$18,581 for Agua Fria projects
2 that were originally added to Sun City West Water district in error.

3 **B. HAVASU WATER DISTRICT**

4 **Q. WHAT IS ADJUSTMENT LJG-1RJ FOR HAVASU WATER DISTRICT?**

5 A. I am moving the Step 2 ACRM Deferral allowed in Decision No. 70626 from Utility
6 Plant in Service to Deferred Debits. This does two things – reflects the deferral where it
7 is recorded in the Company’s books and records, and reduces depreciation expense for
8 Arizona-American by removing it from Plant. Ms. Hubbard amortized the deferral in her
9 rebuttal exhibit SLH-13R, and by including the investment in Plant, I was duplicating the
10 expense. This adjustment does not change the amount of the Company’s proposed Rate
11 Base.

12 **Q. ARE THERE ANY OBSERVATIONS YOU WOULD LIKE TO MAKE ABOUT**
13 **THE OTHER PARTIES’ POSITION THAT YOU HAVE NOT ALREADY**
14 **ADDRESSED IN REBUTTAL?**

15 A. Yes. Staff removed the Gateway Water Plant from Havasu, but erroneously left the
16 Gateway Sewer Plant in Havasu.

17 **C. MOHAVE WATER DISTRICT**

18 **Q. DO YOU HAVE ANY COMMENTS ABOUT STAFF’S UTILITY PLANT FOR**
19 **THE MOHAVE WATER DISTRICT?**

20 A. Yes. I earlier attached to my rebuttal testimony the invoices for the Mira Monte project
21 that were missing when Mr. Becker performed his audit. Staff still left this plant out in
22 surrebuttal, (incorrectly) claiming a lack of invoices.

23 **D. PARADISE VALLEY WATER DISTRICT**

1 **Q. CAN YOU COMMENT ON THE TREATMENT OF THE WELL NO. 12**
2 **REHABILITATION PROJECT IN THE SURREBUTTAL TESTIMONY OF**
3 **BOTH STAFF AND RUCO?**

4 A. Yes. In RUCO's direct testimony, it removed the rehabilitation of Well No. 12 project,
5 as it is not going forward at this time. Arizona-American accepted that adjustment in its
6 rebuttal testimony. Both Staff and RUCO once again have included the project in rate
7 base. RUCO states that it is taking it out, but its exhibit does not remove it. Staff just
8 does not address the issue in its direct or surrebuttal testimony.

9 **E. SUN CITY WEST WATER DISTRICT**

10 **Q. DID STAFF INCLUDE THE \$18,581 IN AGUA FRIA PROJECT COSTS THAT**
11 **WERE ERRONEOUSLY RECORDED IN SUN CITY WEST WATER**
12 **DISTRICT'S RATE BASE?**

13 A. No.

14 **F. TUBAC WATER DISTRICT**

15 **Q. ARE THERE ANY PLANT-IN-SERVICE ISSUES FOR THE TUBAC WATER**
16 **DISTRICT?**

17 A. No. Arizona-American, Staff and RUCO are in agreement.

18 **G. MOHAVE WASTEWATER DISTRICT**

19 **Q. WHAT HAS HAPPENED WITH THE WISHING WELL TREATMENT PLANT**
20 **IN MOHAVE WASTEWATER DISTRICT?**

21 A. Staff has removed all of it, and RUCO has removed exactly half of it.

22 **Q. WHY IS RUCO'S ADJUSTMENT HALF OF PROJECT?**

23 A. Mr. Coley says that RUCO will think about our rebuttal testimony, specifically Mr.
24 Gross's testimony which breaks out the project between improvements to the (then)

1 existing capacity and expansion of the capacity. Mr. Gross testifies that of the \$4.2
2 million project cost, improvements to the wastewater treatment plant account for \$2.8
3 million, while expansion of the wastewater treatment plant cost \$1.4 million. Meanwhile,
4 RUCO removed 50 percent of the entire \$4.2 million. I highlight RUCO's position
5 because if RUCO's recommendation is adopted and 50 percent of the expansion is to be
6 removed from this case, it would be more accurate if RUCO removed only \$0.7 million –
7 which is one-half of the cost of the expansion.

8 **Q. WHAT IS STAFF'S REASONING FOR DELETING THE ENTIRE PROJECT?**

9 A. Staff quotes criteria in their direct and surrebuttal testimony for determining whether to
10 include post test year plant in rate base.

11 **Q. CAN YOU DISCUSS THESE CRITERIA ONE AT A TIME?**

12 A. Yes. The number one criterion that Staff states is, "When the magnitude of the
13 investment relative to the utility's total investment is such that not including the post test
14 year plant in the cost of service would jeopardize the utility's financial health." As a
15 result of this statement, Arizona-American asked Staff for their definition of "jeopardize
16 the utility's financial health" in Arizona-American Data Request No. 1.2. Staff could
17 provide no answer except to reiterate the statement above. See the attached Data Request
18 response under Exhibit LYG-1RJ. At \$4.2 million this project is 4.7 times the pre-
19 existing rate base of less than \$0.9 million. In the past, Staff has said that a times interest
20 earned ratio of less than one is not sustainable, yet Arizona-American's ratio is 0.7 times.

21 Criterion 2.b says "The net impact on revenue and expenses for the post test year plant is
22 known and insignificant, or is revenue neutral". Arizona-American again asked Staff for
23 their definition of "revenue neutral", and their response is attached in Exhibit LYG-1RJ.
24 It doesn't expand their interpretation about what they would define as revenue neutral.

1 To Arizona-American, "revenue neutral" means the post test year plant is serving
2 existing customers rather than new customers. The plant was improved out of a
3 desperate need, as explained by Mr. Gross, to upgrade the facilities. Therefore, although
4 the increase at 46%, net of operational savings, is large, the project is revenue neutral.

5 The final criterion is 2.c. "The post test year plant is prudent and necessary for the
6 provision of services and reflects appropriate, efficient, effective and timely decision-
7 making." Since the plant was regularly at 90% capacity and some mornings over 100%
8 capacity, the investment was, in fact, prudent and necessary to provide adequate service
9 and accordingly, this criterion is also satisfied.

10 The Wishing Well Treatment Plant was planned and built in a timely fashion. It is
11 appropriate to include it in rate base. All of the criteria Staff laid out on page 7 of Mr.
12 Becker's Surrebuttal testimony have been satisfied.

13 **Q. WHAT DID STAFF HAVE TO SAY ABOUT MEETING THESE CRITERIA?**

14 **A.** They said they recommend disallowance and did not give any further explanation.

15 **III RATE BASE – ACCUMULATED DEPRECIATION**

16 **A. ALL DISTRICTS**

17 **Q. RUCO HAS RECOMPUTED DEPRECIATION EXPENSE FOR ALL DISTRICTS**
18 **CLAIMING THAT THEY ARE OF THE "OPINION" THAT ARIZONA-**
19 **AMERICAN HAS NO RIGHT TO CHANGE FROM ONE ACCEPTABLE**
20 **METHOD OF DEPRECIATION TO ANOTHER ACCEPTABLE METHOD**
21 **WITHOUT GETTING COMMISSION APPROVAL THROUGH AN**
22 **ACCOUNTING ORDER; DO YOU AGREE?**

1 A. No. Arizona-American is not aware of any such requirement from the Commission.
2 RUCO does not point to any Commission rule requiring approval by the Commission and
3 without such a rule, Arizona-American simply does not agree.

4 **IV RATE BASE – ADVANCES IN AID OF CONSTRUCTION**

5 **A. HAVASU WATER DISTRICT**

6 **Q. DO YOU HAVE ANY ADJUSTMENTS FOR ADVANCES IN HAVASU WATER**
7 **DISTRICT?**

8 A. Yes. The adjustments proposed in my rebuttal testimony to reclassify the Gateway Water
9 plant and accumulated depreciation from Havasu to Mohave Water failed to reclassify the
10 associated advances. The advances associated with the Gateway Water Plant need to be
11 removed from Havasu Water's rate base and included in Mohave Water's rate base. The
12 amount is a reduction to Havasu Advances and an increase to Mohave Water's Advances
13 of \$656,267. This adjustment is reflected on Schedule B-2-Rejoinder as accepting Staff
14 RB # 5.

15 **V RATE BASE – CONTRIBUTIONS IN AID OF CONSTRUCTION**

16 **A. AGUA FRIA WATER DISTRICT**

17 **Q. DO YOU HAVE ANY COMMENTS ABOUT THE PARTIES' POSITION ON**
18 **CONTRIBUTIONS IN AGUA FRIA WATER DISTRICT?**

19 A. Yes. In my rebuttal testimony, I identified \$28,019 of Accumulated Amortization of
20 Contributions in Aid of Construction ("CIAC") that should be moved from Mohave
21 Water to Agua Fria Water. The CIAC was moved, but the associated reduction for
22 accumulated amortization was not. In my rebuttal, I show an increase (debit) to the
23 amortization of CIAC's in Mohave Water, thereby increasing the net CIAC's in Mohave
24 Water, and an increase (credit) to the amortization of CIAC's in Agua Fria, thereby
25 lowering the net CIAC's in Agua Fria. Staff did not accept this adjustment to the

1 Accumulated Amortization. The information was provided to Staff in our response to
2 Staff's DR GTM 18.7, 2nd supplement.

3 **Q. DO STAFF AND RUCO CONTINUE TO INCLUDE THE ADVANCES AND**
4 **CONTRIBUTIONS RELATED TO PLANT THAT IS IN CWIP?**

5 A. Yes. Both Staff and RUCO are under the mistaken impression that Arizona-American
6 receives funds for AIAC and CIAC. Arizona-American does not receive cash – we
7 receive plant. We take in wells, pumps, tanks, mains, meters, etc. The developer builds
8 the plant using his funds, and advances it or contributes it. It is recorded in CWIP and the
9 offset is to either Advances or Contributions. When the project is completed, it is
10 transferred from CWIP to Utility Plant in Service. But until it does, the engineering
11 estimate is used to create the entry in CWIP and the offset entry. There are no “funds”
12 available to build other components or other plant in service as Staff and RUCO believe.
13 Contrary to their allegations, Arizona-American does not accrue AFUDC on developer
14 advanced or contributed projects. When the plant is in Utility Plant in Service, then it is
15 appropriate to deduct the associated AIAC and CIAC when calculating rate base.
16 However, when the plant is still in CWIP, it is improper to deduct the associated AIAC
17 and CIAC because the associated plant is in CWIP which is not in rate base. The
18 amounts at issue here are:

District	CIAC	AIAC
Agua Fria Water	\$3,432,286	
Havasu Water	\$10,845	
Mohave Water	\$94,452	\$291,909
Paradise Valley	\$322,588	
Sun City West Water	\$17,318	
Tubac Water		\$20,266
Mohave Wastewater	\$65,395	
Total	\$3,942,884	\$312,175

1 RUCO and Staff are simply incorrect on this issue.

2 **Q. WHAT ABOUT RUCO'S ARGUMENT THAT ARIZONA-AMERICAN SHOULD**
3 **TO BE TREATED THE WAY ALL UTILITIES IN ARIZONA ARE?**

4 A. In Arizona Water Company (Decision No. 68302, November 14, 2004) the Commission
5 approved what the Staff accepted - a reduction in AIAC for outside-funded projects that
6 remained in CWIP at the end of the test year that were excluded from rate base. In that
7 case, Arizona Water's Coolidge and Casa Grande water districts had outside-funded
8 projects in CWIP. Both districts' rate base included adjustments to reduce AIACs for the
9 CWIP excluded from rate base. By comparing Arizona Water's Schedules B-2 and Staff
10 Exhibit REL-3 in Surrebuttal , one can see the amount allowed in Advances for the
11 Coolidge District and the Casa Grande District. Copies of these papers are attached as
12 Exhibit LJG-3RJ.

13 **VI RATE BASE – DEFERRED DEBITS**

14 **Q. WHY HAVE YOU INCREASED THE DEFERRED DEBITS IN HAVASU**
15 **WATER DISTRICT?**

16 A. I have moved the Step 2 ACRM deferral out of Utility Plant in Service and into a
17 Regulatory Asset.

18 **VII RATE BASE – CASH WORKING CAPITAL (**

19 Please see Ms. Hubbard's rejoinder testimony for changes to Cash Working Capital.)

20 **A. SUMMARY OF REJOINDER RATE BASE POSITIONS.**

21 **Q. PLEASE SUMMARIZE ARIZONA-AMERICAN'S REJOINDER RATE BASE**
22 **POSITION FOR EACH DISTRICT.**

23 A. The table below summarizes Arizona-American's rejoinder position.

	<u>Rate Base</u>
Agua Fria	\$92,049,310
Havasu	\$3,887,188
Mohave Water	\$10,235,260
Paradise Valley	\$37,398,279
Sun City West Water	\$38,382,791
Tubac Water	\$1,457,349
Mohave Wastewater	\$5,134,633

1 **VIII DEPRECIATION EXPENSE**

2 **A. ALL DISTRICTS**

3 **Q. DOES ARIZONA-AMERICAN HAVE ANY REJOINDER COMMENTS FOR**
4 **ANNUAL DEPRECIATION EXPENSE?**

5 A. Yes. For corporate plant, Mr. McMurry uses different depreciation rates for allocations
6 of the same plant to different districts. Arizona American cannot depreciate a desk at its
7 Corporate offices using different depreciation rates for each of its 13 districts. The plant
8 can be allocated, but the depreciation rates should be same. If you associate the
9 depreciation rate to the plant in Corporate, and then allocate both the plant and the
10 depreciation expense; the results will be more reasonable.

11 **Q. DID STAFF LEAVE OUT THE AMORTIZATION OF REGULATORY ASSETS**
12 **PREVIOUSLY APPROVED?**

13 A. Yes. Staff should have included the following amounts in the following districts for the
14 amortization which was approved in Decision 67093:

District	Amortization Exp
Agua Fria Water	\$2,918
Havasu Water	\$ 834
Mohave Water	\$9,384

Paradise Valley	\$ 72
Sun City West	\$5,841
Tubac	\$ 0
Mohave Wastewater	\$ 0

1 **Q. DID RUCO INCLUDE THESE AMORTIZATIONS?**

2 A. Yes.

3 **Q. WHAT HAPPENS IF STAFF CONTINUES TO LEAVE OUT THE**
4 **AMORTIZATION?**

5 A. These Regulatory Assets - allowed in the last case - will have to be written off.

6 **Q. DO YOU RECOMMEND ANY COMMON CHANGES TO DEPRECIATION**
7 **RATES THAT WOULD APPLY TO ALL DISTRICTS?**

8 A. Yes. Staff has made their adjustments and recommendations to most of the rates. But,
9 concerning Account 334100, Meters, Staff has not agreed to the 15-year program of
10 meter change-outs proposed by Mr. Day. Ms. Hains testifies that Staff does not have any
11 studies to prove that we have ever been on this cycle. Attached as Exhibit LJG-2RJ is a
12 new study utilizing information since 2004 from our Utility Plant Accounting system. It
13 addresses meter retirements for every water district we have, from 2004 to the present.
14 This data represents the vintage life of over 3,900 meters replaced in our water districts.
15 The average vintage life is 15 years, or 6.6%.

16 **Q. DO YOU HAVE ANY CORRECTIONS TO ANY DISTRICTS FOR**
17 **DEPRECIATION EXPENSE?**

18 A. Yes. We inadvertently included the Depreciation Expense of the Citizens' Acquisition
19 Adjustment in Agua Fria Water for \$230,973 and in Havasu Water for \$13,852.
20 Adjustment to remove these expenses is reflected in Ms. Hubbard's Rejoinder Schedules
21 C-2 for Agua Fria and Havasu as ADJ SLH-1RJ. Staff did not include these amounts and

1 we agree with leaving them out. Both of these adjustments will decrease our depreciation
2 expense in those districts.

3 **Q. WHAT HAPPENS WITH THE DEFERRAL OF THE ACRM O&M FOR**
4 **HAVASU DISTRICT?**

5 A. I put the \$94,996 into Utility Plant and depreciated it. Meanwhile, Ms. Hubbard
6 amortized the \$94,996 over 12 years for an annual amortization expense of \$7,916
7 reflected as ADJ SLH-13R in her rebuttal Schedule C-2 for Havasu. I am moving this
8 deferral from Utility Plant in Service to a regulatory asset (Deferred Debit) and removing
9 the associated depreciation expense. I am showing it in Rate Base as a Deferred Debit, as
10 that is where it is currently booked. Ms. Hubbard's rebuttal exhibit reflects the
11 amortization of this regulatory asset and no further adjustment is necessary. Mr.
12 McMurray did not include any amortization of the deferral.

13 **Q. DOES THIS CONCLUDE YOUR REJOINDER TESTIMONY?**

14 A. Yes.

EXHIBIT LJ – 1RJ

**STAFF'S RESPONSE TO THE FIRST SET OF DATA REQUESTS FROM ARIZONA-
AMERICAN WATER COMPANY
Docket Nos. W-01303A-08-0227; SW-01303A-08-0227
January 30, 2009**

- 1.2 Please provide Staff's definition of the phrase "jeopardize the utility's financial health" as appearing in Becker page 20, line 15 in sufficient specificity that the company can characterize its financial health in its rebuttal testimony using Staff's definition. If the definition refers to financial ratios, please provide the amount or range of the ratio that would be considered in jeopardy by Staff.

RESPONSE: This phrase is taken from the context of Staff's discussion regarding when it is appropriate to recognize test year plant. Please refer to Mr. Becker's testimony, wherein he stated:

"Staff had traditionally recognized two such cases:

1. When the magnitude of the investment relative to the utility's total investment is such that not including the post test year plant in the cost of service would jeopardize the utility's financial health; and
2. When conditions such as the following exist:
 - a. The cost of the post test year plant is significant and substantial,
 - b. The net impact on revenue and expenses for the post test year plant is known and insignificant, or is revenue neutral,
 - c. The post test year plant is prudent and necessary for the provision of services and reflects appropriate, efficient, effective and timely decision-making."

RESPONDENT: Gerald W. Becker

**STAFF'S RESPONSE TO THE FIRST SET OF DATA REQUESTS FROM ARIZONA-
AMERICAN WATER COMPANY
Docket Nos. W-01303A-08-0227; SW-01303A-08-0227
January 30, 2009**

- 1.3 Please provide Staff's definition of revenue neutral as it is used in Becker, page 21, line 8 as it is unclear and appears possibly circular in reference to, for example, White Tanks, for which no additional water is sold once it comes on line, but rather it reduces usage by existing water sources.

RESPONSE: To clarify, the \$25 million post test year adjustment for White Tanks is not being included in rate base because it is CWIP and it is not used and useful.

RESPONDENT: Gerald W. Becker

EXHIBIT LJG – 2RJ

Study of Retirement of Meters, Acct 334100, from 2004 to present
 [Leaving out years 1 through 5 as an anomaly]

Agua Fria Water - Study of Retirement of Meters from 2004 to 2007

		31,882		
# of Customers in TY Ended 12/31/07				
Vintage Year	# of Meters	Vintage Yr Dep Rate	Weighted Avg Rate	
8	1	12.5%	13%	
11	18	9.1%	164%	
12	25	8.3%	208%	
13	36	7.7%	278%	
14	1	7.1%	7%	
15	32	6.7%	213%	
54	25	1.9%	46%	
	<u>138</u>			

Anthem Water - Study of Retirement of Meters from 2004 to 2007

		8,637		
# of Customers Year Ended 12/31/07				
Vintage Year	# of Meters	Vintage Yr Dep Rate	Weighted Avg Rate	
8	16	12.5%	200%	
13	0	7.7%	0%	
	<u>16</u>			

Havasu Water - Study of Retirement of Meters from 2004 to 2007

		1,518		
# of customers in TY Ended 12/31/07				
Vintage Year	# of Meters	Vintage Yr Dep Rate	Weighted Avg Rate	
13	9	7.7%	69%	
15	31	6.7%	207%	
16	10	6.3%	63%	
54	3	1.9%	6%	
	<u>53</u>			

Mohave Water - Study of Retirement of Meters from 2004 to 2007

		15,919		
# of customers in TY Ended 12/31/07				
Vintage Year	# of Meters	Vintage Yr Dep Rate	Weighted Avg Rate	
9	2	11.1%	22%	
10	1	10.0%	10%	
15	287	6.7%	1913%	
16	4	6.3%	25%	
17	457	5.9%	2688%	
18	438	5.6%	2433%	
19	489	5.3%	2574%	
20	179	5.0%	895%	
21	121	4.8%	576%	
	<u>1,978</u>			

Paradise Valley Water - Study of Retirement of Meters from 2004 to 2007

of customers in TY Ended 12/31/07

4,740

Vintage Year	# of Meters		
6	12	16.7%	203%
7	38	14.3%	543%
8	43	12.5%	538%
9	52	11.1%	578%
10	26	10.0%	260%
11	35	9.1%	318%
12	23	8.3%	192%
13	249	7.7%	1915%
14	210	7.1%	1500%
15	18	6.7%	120%
16	8	6.3%	50%
17	96	5.9%	565%
18	7	5.6%	39%
19	9	5.3%	47%
20	6	5.0%	30%
21	6	4.8%	29%
22	6	4.5%	27%
23	5	4.3%	22%
24	4	4.2%	17%
25	3	4.0%	12%
26	7	3.8%	27%
27	2	3.7%	7%
28	3	3.6%	11%
29	4	3.4%	14%
30	2	3.3%	7%
31	6	3.2%	19%
32	3	3.1%	9%
33	8	3.0%	24%
34	1	2.9%	3%
39	1	2.6%	3%
45	1	2.2%	2%
46	5	2.2%	11%
47	3	2.1%	6%
48	5	2.1%	10%
49	2	2.0%	4%
50	1	2.0%	2%
64	2	1.6%	3%

912

EXHIBIT LJG – 3RJ

ORIGINAL
NEW APPLICATION

1 ARIZONA WATER COMPANY
2 Robert W. Geake (No. 009695)
3 Vice President and General Counsel
4 3805 N. Black Canyon Highway
5 Phoenix, Arizona 85015-5351
6 Telephone: (602) 240-6860

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2004 SEP -8 P 3: 25

7 FENNEMORE CRAIG
8 A Professional Corporation
9 Norman D. James (No. 006901)
10 Jay L. Shapiro (No. 014650)
11 3003 North Central Avenue
12 Suite 2600
13 Phoenix, Arizona 85012-2913
14 Telephone: (602) 916-5000

AZ CORP COMMISSION
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15 Attorneys for Arizona Water Company

W-01445A-04-0650

BEFORE THE ARIZONA CORPORATION COMMISSION

12 IN THE MATTER OF THE APPLICATION) DOCKET NO. W-01445A-04-_____
13 OF ARIZONA WATER COMPANY, AN)
14 ARIZONA CORPORATION, FOR) APPLICATION
15 ADJUSTMENTS TO ITS RATES AND)
16 CHARGES FOR UTILITY SERVICE)
AND FOR CERTAIN RELATED)
APPROVALS)

17
18 Arizona Water Company, an Arizona corporation (the "Company"), hereby applies for an
19 order approving certain adjustments to its rates and charges for utility service provided by the
20 Company's Western Group, which includes five separate water systems in Arizona, and in
21 support thereof, states as follows:

22 1. The Company is an Arizona corporation engaged in providing water for public
23 purposes in portions of Cochise, Coconino, Gila, Maricopa, Navajo, Pima, Pinal and Yavapai
24 Counties, Arizona, pursuant to certificates of public convenience and necessity granted by the
25 Arizona Corporation Commission (the "Commission"). At the present time, the Company
26 operates 18 water systems that serve approximately 72,000 customers.

27 2. The Company's central business office is located at 3805 North Black Canyon
28 Highway, Phoenix, Arizona 85015-5351. Its mailing address is Post Office Box 29006, Phoenix,

ORIGINAL 1

**ORIGINAL COST RATE BASE PROFORMA ADJUSTMENTS
END OF TEST YEAR 2003
WESTERN GROUP**

Line No.	Description	Actual Test Year (a)	Casa Grande Pro Forma Adjustments				Adjusted Test Year (c)	
			(1)	(2)	(3)	(4)		(5)
1.	Gross Plant In Service	\$48,030,396						
2.	less: Accumulated Depreciation	(12,087,978)						\$51,566,199
3.	Net Plant In Service	35,942,418			15,761	3,525,803		(12,072,217)
4.	Construction Work In Progress	146,293	0	0	15,761	3,525,803	0	39,483,982
5.	Total Net Plant	36,088,711	(145,362)	0	15,761	3,525,803	(931)	0
	Less:							
6.	Advances for Construction	(8,892,375)					931	(8,891,444)
7.	Contributions in Aid of Construction:							
8.	Gross	(7,754,812)						(7,754,812)
9.	Accumulated Amortization	1,381,441			(32,621)			1,348,820
10.	Net Contributions in Aid Of Construction	(6,373,371)	0	0	(32,621)	0	0	(6,405,992)
11.	Deferred Income Tax	(3,387,966)						(3,387,966)
12.	Add: Total Working Capital Allowance (b)	250,254						250,254
13.	Total Rate Base Components & Adjustments	\$17,685,253	(145,362)	0	(16,860)	3,525,803	0	\$21,048,834

Supporting Schedules:
 (a) E-5 & AWC books & records
 (b) B-5, line 5
Recap Schedules:
 (c) B-1

(1) Construction Placed In Service/Elimination of CWIP from Rate Base
 (2) Depreciation on Post Test Year Plant Additions
 (3) Depreciation Expense/CJAC Annualization
 (4) Deferred CAP M&I Charges
 (5) Outside-funded CWIP

**ORIGINAL COST RATE BASE PROFORMA ADJUSTMENTS
END OF TEST YEAR 2003
WESTERN GROUP**

Line No.	Description	Actual Test Year (a)	Coolidge			Adjusted Test Year (c)				
			(1)	(2)	(3)		(4)	(5)	(6)	
1.	Gross Plant In Service	\$6,083,129				1,046,011				\$7,129,140
2.	less: Accumulated Depreciation	(2,249,826)			(21,871)					(2,271,697)
3.	Net Plant In Service	3,833,303	0	0	(21,871)	1,046,011	0			4,857,443
4.	Construction Work In Progress	127,831	(11,335)	0	(21,871)	1,046,011	(118,496)			0
5.	Total Net Plant	3,961,134	(11,335)	0	(21,871)	1,046,011	(118,496)		0	4,857,443
Less:										
6.	Advances for Construction	(523,140)					116,496			(406,644)
7.	Contributions in Aid of Construction:									
8.	Gross	(437,102)								(437,102)
9.	Accumulated Amortization	76,495			(1,525)					74,970
10.	Net Contributions in Aid Of Construction	(360,607)	0	0	(1,525)	0	0	0	0	(362,132)
11.	Deferred Income Tax	(504,369)								(504,369)
12.	Add: Total Working Capital Allowance (b)	32,202								32,202
13.	Total Rate Base Components & Adjustments	\$2,605,220	(11,335)	0	(23,396)	1,046,011	0	0	0	\$3,616,500

Supporting Schedules:
 (a) E-5 & AWC books & records
 (b) B-5, line 5
 Recap Schedules:
 (c) B-1

(1) Construction Placed In Service/Elimination of CWIP from Rate Base
 (2) Depreciation on Post Test Year Plant Additions
 (3) Depreciation Expense/CIAC Annualization
 (4) Deferred CAP M&I Charges
 (5) Outside-funded CWIP

1 **III. ORIGINAL COST RATE BASE**

2 Based on the foregoing discussion, we adopt an adjusted original cost rate base ("OCRB") for
3 the Western Group of \$23,254,087. By system, the OCRB is as follows: Casa Grande, \$17,495,567;
4 Coolidge, \$2,713,030; White Tank, \$1,898,133; Ajo, \$837,088; and Stanfield, \$310,269.

5 **IV. FAIR VALUE RATE BASE**

6 The Company did not submit reconstruction cost new less depreciation ("RCND") schedules,
7 but stipulated in its application to the use of its OCRB as its fair value rate base ("FVRB")
8 (Application at 3). We therefore adopt \$23,254,087 as the FVRB for Arizona Water's Western
9 Group. By system, the FVRB is as follows: Casa Grande, \$17,495,567; Coolidge, \$2,713,030;
10 White Tank, \$1,898,133; Ajo, \$837,088; and Stanfield, \$310,269.

11 **V. OPERATING INCOME**

12 **A. Revenue Annualization**

13 There is no dispute that an adjustment to the test year annualizing revenues and expenses to
14 recognize the effects of the number of customers served by the Western Group at the end of the test
15 year is appropriate. According to the Company, the test year end number of customers was 20,266,
16 and during the test year, the Company served an average of 19,596 customers, a difference of 670
17 customers (Hubbard Dt. at 25). The Company compared the year-end number of customers to the
18 number of customers at the beginning of the test year to calculate the average number of test year
19 customers (Tr. at 760). The Company's calculation is based on the number of residential customers,
20 as this class of customers constitutes 96 percent of the growth in customers in the Western Group
21 (*id.*). The Company bases its expense annualization adjustment on costs per customer for customer
22 accounts expense and transmission and distribution expenses (including operations and maintenance
23 costs), and on costs per gallon for source of supply, pumping and water treatment expenses (Hubbard
24 Rb. at 24).
25
26
27
28

RATE BASE - ORIGINAL COST

LINE NO.	(A) COMPANY AS FILED	(B) STAFF ADJUSTMENTS	(C) STAFF AS ADJUSTED
1	Plant in Service	\$ 7,129,140	\$ 6,083,129
2	Less: Accumulated Depreciation	(2,271,697)	(2,271,697)
3	Net Plant in Service	<u>\$ 4,857,443</u> x	<u>\$ 3,811,432</u>
LESS:			
4	Advances in Aid of Construction (AIAC)	(406,644) x	(406,644)
5	Contributions in Aid of Construction (CIAC)	\$ (437,102)	\$ (437,102)
6	Less: Accumulated Amortization	74,970	74,970
7	Net CIAC	<u>(362,132) x</u>	<u>(362,132)</u>
8	Total Advances and Contributions	(768,776)	(768,776)
9	Customer Deposits	-	-
10	Meter Advances	-	-
11	Deferred Income Tax Credits	(504,369) x	(504,369)
ADD:			
12	Working Capital	32,202 x	(26,267) x
13	Phoenix Office Allocation	197,345 x	197,345
14	Meter Shop Allocation	3,665 x	3,665
15		-	-
16		-	-
17		-	-
18	Total Rate Base	<u>\$ 3,817,510</u>	<u>\$ 2,713,030</u>

RATE BASE - ORIGINAL COST

LINE NO.	(A) COMPANY AS FILED	(B) STAFF ADJUSTMENTS	(C) STAFF AS ADJUSTED
1	Plant in Service	\$ 51,556,199	\$ 47,206,022
2	Less: Accumulated Depreciation	(12,072,217)	(12,072,217)
3	Net Plant in Service	<u>\$ 39,483,982</u> x	<u>\$ 35,133,805</u>
LESS:			
4	Advances in Aid of Construction (AIAC)	(8,891,444)	(8,891,444)
5	Contributions in Aid of Construction (CIAC)	\$ (7,754,812)	\$ (7,754,812)
6	Less: Accumulated Amortization	<u>1,348,820</u>	<u>1,348,820</u>
7	Net CIAC	<u>(6,405,992)</u>	<u>(6,405,992)</u>
8	Total Advances and Contributions	(15,297,436)	(15,297,436)
9	Customer Deposits	-	-
10	Meter Advances	-	-
11	Deferred Income Tax Credits	(3,387,966)	(3,387,966)
ADD:			
12	Working Capital	250,254	(43,550) x
13	Phoenix Office Allocation	930,536	930,536
14	Meter Shop Allocation	17,282	17,282
15		-	-
16		-	-
17		-	-
18	Total Rate Base	<u>\$ 21,996,652</u>	<u>\$ 17,352,671</u>

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman
GARY PIERCE
PAUL NEWMAN
SANDRA D. KENNEDY
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**REJOINDER TESTIMONY
OF
SHERYL L. HUBBARD
ON BEHALF OF
ARIZONA-AMERICAN WATER COMPANY
MARCH 11, 2009**

**REJOINDER TESTIMONY
OF
SHERYL L. HUBBARD
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ARIZONA-AMERICAN WATER COMPANY
MARCH 11, 2009**

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1 **EXECUTIVE SUMMARY**

2 Sheryl L. Hubbard testifies as follows:

3 **WORKING CAPITAL:**

4 Arizona-American has incorporated revised service and billing lags in the calculation of
5 the revenue lag filed in conjunction with this rejoinder testimony.

6 Average daily revenues and average accounts receivable balance should both be
7 computed on a comparable basis or 365 daily balances. Based on these computations,
8 Arizona-American has recalculated revenue lags and cash-working capital for each
9 district.

10 **MISCELLANEOUS EXPENSE**

11 Staff failed to include Ms. Hains' water-testing expenses in its proposed Miscellaneous
12 Expenses or in any other expense in its direct case or surrebuttal case presentations.

13 **PROPERTY TAXES AND INCOME TAXES**

14 Based on the cash-working capital adjustment and the inclusion of water-testing expense,
15 Arizona-American recalculates property tax and income tax expense.

1 **I. INTRODUCTION AND QUALIFICATIONS**

2 **Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND TELEPHONE**
3 **NUMBER.**

4 A. My name is Sheryl L. Hubbard. My business address is 19820 N. 7th Street, Suite 201,
5 Phoenix, Arizona 85024, and my business phone is 623-445-2419.

6 **Q. DID YOU FILE DIRECT TESTIMONY AND REBUTTAL TESTIMONY IN THIS**
7 **PROCEEDING?**

8 A. Yes, I did.

9 **II. PURPOSE OF TESTIMONY**

10 **Q. WHAT IS THE PURPOSE OF YOUR REJOINDER TESTIMONY IN THIS**
11 **CASE?**

12 A. My rejoinder testimony is organized by subject matter primarily focusing on adjustments
13 to Arizona-American's cash working capital calculations and Adjusted Test Year
14 Operating Income proposed by witnesses for the Arizona Corporation Commission Staff
15 ("Staff") and the Residential Utility Consumer Office ("RUCO").

16 **III. SPONSORED SCHEDULES AND EXHIBITS**

17 **Q. PLEASE IDENTIFY THE SCHEDULES YOU ARE SPONSORING.**

18 A. I am sponsoring the following schedules for each district:

- 19 • Schedule B-6 Rejoinder - Arizona-American Computation of Cash Working Capital
20 • Schedule C-2 Rejoinder - Arizona-American Income Statement Pro Forma
21 Adjustments
22 • Schedule C-3 Rejoinder - Arizona-American Computation of Gross Revenue
23 Conversion Factor

1 **Q. PLEASE IDENTIFY THE EXHIBITS YOU ARE SPONSORING.**

2 A. I am sponsoring the following exhibit, which are attached to this rebuttal testimony.

- 3 • Exhibit SLH-RJ1 – Excerpt from Accounting for Public Utilities – Revenue Lag

4 **IV. WORKING CAPITAL**

5 **Q. HAVE YOU REVIEWED THE TESTIMONY OF RUCO’S WITNESS TIMOTHY**
6 **J. COLEY REGARDING THE REVENUE LAG PORTION OF THE CASH**
7 **WORKING CAPITAL CALCULATION?**

8 A. Yes, I have.

9 **Q. MR. COLEY TESTIFIES THAT THE COMPANY FAILED TO REFLECT**
10 **CORRECTIONS TO THE SERVICE AND BILLING LAG PORTION OF THE**
11 **REVENUE LAG CALCULATION AS PROVIDED IN RESPONSE TO DATA**
12 **REQUEST RUCO 2.02 IN ITS REBUTTAL PRESENTATION. WHAT IS YOUR**
13 **RESPONSE?**

14 A. The Company admits an oversight in its rebuttal filing to recalculate the cash working
15 capital due to the use of incorrect service and billing lags in its direct case filing. The
16 revised service and billing lags have been incorporated in the calculation of the revenue
17 lag filed in conjunction with this rejoinder testimony.

18 **Q. TO PROVIDE AN “APPLES TO APPLES” COMPARISON, MR. COLEY USES**
19 **254 DAYS TO CALCULATE THE AVERAGE DAILY REVENUE IN HIS**
20 **REVENUE LAG CALCULATION. DO YOU AGREE WITH MR. COLEY’S USE**
21 **OF 254 DAYS TO CALCULATE THE AVERAGE DAILY REVENUE?**

22 A. No, I do not. Water consumption by the Company’s customers occurs on a daily basis
23 and the associated average daily revenue should be calculated using a full year or 365
24 days. I would, however, acknowledge that the average accounts receivable balance
25 should also be computed on a comparable basis or 365 daily balances which is consistent

1 with how the Company's lead-lag studies have been performed in the past. By using the
2 accounts receivable balance on Friday for the following Saturday and Sunday balances
3 (and Monday bank holidays where applicable), a 365 day average can be computed. Use
4 of 365 days is recognized in the public utility industry for calculating the revenue lag as
5 referenced in Exhibit SLH-RJ1 which is attached to this testimony. Using this
6 recognized method, the revenue lags for all of the districts are affected and the revised
7 revenue lags are shown below in Table 1.

8 **Table 1 – Revenue Lags**

District	Agua Fria Water	Havasus Water	Mohave Water	Paradise Valley Water	Sun City West Water	Tubac Water	Mohave Wastewater
Revenue Lag	47.90683	48.44106	48.15644	47.97433	47.56935	49.65788	46.42606

9 **Q. HAVE YOU REFLECTED THE REVISED REVENUE LAGS IN THE**
10 **CALCULATION OF THE CASH WORKING CAPITAL FOR ALL SEVEN OF**
11 **THE DISTRICTS IN THIS PROCEEDING?**

12 A. Yes, except for Tubac Water. The revenue lag for Tubac Water increases as a result of
13 using a 365 average accounts receivable balance and since there are no other adjustments
14 proposed by the Company for Tubac in this rejoinder filing, the Company will be content
15 with the cash working capital requested in its rebuttal filing.

16 **Q. WHAT IS ARIZONA-AMERICAN'S REVISED REQUEST FOR CASH**
17 **WORKING CAPITAL?**

18 A. The following tables summarize Arizona-American's revised request for the cash-
19 working-capital component of working capital for each water and wastewater district:

Table 2 – Cash Working Capital Component of Working Capital

District	Agua Fria Water	Havasu Water	Mohave Water	Paradise Valley Water	Sun City West Water	Tubac Water	Mohave Wastewater
Cash Working Capital	\$ 12,206	\$53,338	\$ 187,330	\$ 41,544	\$ 85,384	\$ 21,683	(\$ 3,481)

V. ADJUSTED OPERATING INCOME

Q. WHAT IS ARIZONA-AMERICAN'S ADJUSTED OPERATING INCOME BY DISTRICT IN THIS PROCEEDING?

A. The following tables summarize Arizona-American's rejoinder position for Adjusted Operating Income for each water and wastewater district seeking rate increases in this proceeding:

Table 3 – Adjusted Operating Income

District	Agua Fria Water	Havasu Water	Mohave Water	Paradise Valley Water	Sun City West Water	Tubac Water	Mohave Wastewater
Adjusted Operating Income	\$ 2,875,032	\$ 54,601	\$ 298,400	\$ 2,042,407	\$ 736,260	(\$ 40,106)	\$ 116,410

A OPERATING EXPENSES

Q. WHAT ARE ARIZONA-AMERICAN'S REQUESTED TOTAL OPERATING EXPENSES BY DISTRICT?

A. The following tables summarize adjusted test year operating expenses for each district:

Table 4 – Operating Expenses

District	Agua Fria Water	Havasu Water	Mohave Water	Paradise Valley Water	Sun City West Water	Tubac Water	Mohave Wastewater
Operating Expenses	\$15,943,581	\$1,122,920	\$ 4,815,231	\$ 6,178,179	\$ 5,121,006	\$ 467,006	\$ 679,751

1 **B MISCELLANEOUS EXPENSE**

2 **1 WATER TESTING EXPENSE**

3 **Q. DID STAFF INCORPORATE MS. HAINS RECOMMENDED LEVEL OF**
4 **WATER TESTING EXPENSE IN ITS SURREBUTTAL FILING?**

5 A. As far as I can tell, Staff did not include Ms. Hains' water-testing expenses in its
6 proposed Miscellaneous Expenses or in any other expense in its direct case or surrebuttal
7 case presentations.

8 **Q. ARE MS. HAINS RECOMMENDED WATER TESTING EXPENSES**
9 **REFLECTED IN ARIZONA-AMERICAN'S REJOINDER FILING?**

10 A. Yes. The water testing expenses proposed by Ms. Hains were included in the Company's
11 rebuttal adjustments and are still included in the Company's proposed operating expenses
12 in this rejoinder filing.

13 **C PROPERTY TAXES**

14 **Q. ARE THERE ANY CHANGES NECESSARY TO ARIZONA-AMERICAN'S**
15 **PROPOSED PROPERTY TAXES?**

16 A. The proposed adjustments to property taxes reflected in the Company's rejoinder
17 presentation are merely conforming adjustments to reflect proposed changes that affect
18 the revenue requirement.

1 **D INCOME TAXES**

2 **Q. ARE THERE ANY CHANGES NECESSARY TO ARIZONA-AMERICAN'S**
3 **PROPOSED INCOME TAXES?**

4 **A.** The proposed adjustments to income taxes reflected in the Company's rejoinder
5 presentation are merely conforming adjustments to reflect proposed changes that affect
6 the revenue requirement.

7 **Q. DOES THIS CONCLUDE YOUR REJOINDER TESTIMONY IN THIS CASE?**

8 **A.** Yes, it does.

EXHIBIT SLH-RJ1

ACCOUNTING FOR PUBLIC UTILITIES

Volume 1

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if information is available on the record of a proceeding as to wholesale customer revenue lags and expense lags for fossil fuel expenses and purchased power expenses, the FERC has approved separately computed allowances for fuel and purchased power in conjunction with a simple 45-day allowance for other O&M expenses. There have been numerous exceptions to these general principles due to a variety of case-specific circumstances, so it is almost impossible to generalize accurately. If a fully developed and reliable lead-lag study has been presented in the case, the results of that would have been used instead.

A common complaint has been that lead-lag studies are expensive to prepare. This economic burden may be cut down, however, if the commission will accept the fact that, absent significant changes in receipt patterns for revenue or payment patterns of expenses, the lead-lag days determined in a specific analysis will not change and the resulting lead or lag days can be applied to the dollars of revenues, expenses, etc., in future cases. (See the following sections for a discussion of these considerations.)

[2] Lead-Lag Study

The primary purpose of a lead-lag study is to accurately establish the amount of investors' funds used in sustaining utility operations from the time expenditures are made in providing services to the time revenues are received as reimbursement for these services. The lead-lag study requires comprehensive analysis of the test year transactions to determine the "net lag days" for:

- (1) the time lag between services rendered and the receipt of revenues for such services; and
- (2) the time lag between the recording of labor, materials, etc., costs and the payment of such costs.

For example, if service period revenues are recovered 40 days after services are rendered and service period expenses are paid 30 days after services are rendered, the net expense recovery lag is ten days (i.e., investor funding is required for ten days of service period costs). The net lag days are multiplied by the average daily operating expenses of the test year to produce the cash working capital used in maintaining daily operations.

Typically, the funding of operations necessitated by the lag between expense payment and revenue recovery does not fully measure the investor funding requirements of cash working capital. For example, the banks from which the expense payment checks are drawn usually require the maintenance of minimum balances. Any of these funding requirements must be supported by investors, and must be added to the revenue/expense lag amounts produced by the lead-lag analysis.

Some regulators have limited the cash working capital component to "current cash outlay" requirements by concluding that the term "cash working capital" limits its application. In these cases, expenses such as provisions for depreciation have been considered as "non-cash" expenses and omitted from the lead-lag study. If such a constraint is imposed, and the cash working capital provision is limited to a measure of current operating cash requirements, other rate base components must be restated.

This condition will be discussed in more detail in subsequent sections.

The cost *recording* date is a critical point of reference in measuring investor capital funding of operating costs. Typically, costs are recorded when known to exist, and when the amounts are known or estimable. There are, however, occasions when services are provided to a utility in one period but not invoiced until a later period. In these circumstances, the costs may not be recorded until the invoice is received. In the cost of service approach to ratemaking these costs do not exist until recorded and are not recoverable from the ratepayers until that time. In these instances the service period is considered to be the period in which recorded, and the payment delay should reflect the time lag between recording and payment.

As previously stated, the cash working capital produced by the lead-lag study must be compatible with the other rate base components to which it is added to express the total amount of investor capital used in providing utility services. To achieve this compatibility, the lead-lag analysis must be customized to fit the particular conditions in which the rate base is being developed. As is widely accepted, the rate base is intended to provide a measure of investor capital used in providing service. To the extent that there are deficiencies in specific rate base components, such deficiencies must be remedied. Whether by a direct adjustment or through the inclusion of the expense recordings giving rise to the deficiency is not important. The corrections must be made, and it is fully appropriate to do so in the lead-lag analysis. Otherwise, the corrections should be made to the affected components to avoid understatement of the actual investor funding requirements. When appropriately constructed, the lead-lag study functions as a vehicle to correct deficiencies inherent in other rate base components.

The remainder of this chapter discusses considerations in preparing lead-lag studies and provides illustrations of the calculations to be made. In performing the calculation of a lead-lag study, generally the first item considered is the determination of the lag in the receipt of revenues.

[3] Revenue Lag

For companies with hundreds of thousands or even millions of customers, determination of the revenue lag appears to be very burdensome. Once the time frame is segregated into specific components, however, the task becomes much less onerous. The first component of the total time frame of the revenue lag is the service period—the time from the previous meter reading to the current meter reading date. Individuals familiar with cycle reading processes recognize that monthly periods range anywhere from 27 to 33 days depending upon the meter reading cycle schedule. If a meter is read 12 times in a year, it can be determined that the average time between meter readings is 30.4 days. Further, assuming that service is rendered evenly throughout these meter reading periods, the average service period to meter reading is a 15.2 day lag. See the first line of Figure 5-1 for this calculation. Stated another way, after the meter reading it is approximately 30 days until the next meter reading date. Service rendered after the first meter reading has a 30-day lag, and that continues to decline until service rendered the day the meter is next read has a zero-day lag.

Averaging those 30-plus days together produces the 15.2 day average service period lag.

Figure 5-1
Calculation of Number of Days
from Service to Collection

<u>Line No.</u>	<u>Description</u>	<u>Number of Days</u>
	<u>Total Company</u>	
1	Service period to date meter is read (365 ÷ 12 = 30.4 ÷ 2)	15.2
2	Reading date to date billing is prepared	5.0
3	Billing date to date collection is received	22.1
4	Total	<u>42.3</u>

The second time frame to be considered is from the meter reading date until the time the bill is prepared and rendered. This varies among utilities, but most companies have a specific schedule showing when meters are read and billings prepared. Those schedules are on file and maintained in an orderly fashion. Absent significant problems, such as delays in meter reading or billing due to strikes or computer down time, it is relatively simple to take the billings for 12 months (generally 20 to 22 cycles per month) and determine the average period from reading date to billing date. (See Line 2 of Figure 5-1.)

Determination of the third period to be measured—the time from the billing date to the date collections are received—is more complicated due to the large number of customer payment patterns that must be analyzed. Occasionally, statistical samples have been selected and individual analyses prepared of a large number of customers' bills for an entire historical year. However, these studies have provoked much discussion as to the validity of the samples, and they have consumed a significant amount of review and hearing time.

The easiest way to determine the average collection lag (billing to collection) is to use an overall system-wide basis. This can be done if the utility either produces a daily accounts receivable balance or has the information to produce such a number with a computer used to gather the data. In some cases, this can even be done manually. Once the average daily balance of accounts receivable is known, dividing the daily balance of accounts receivable by the average daily revenues produces the average number of days of revenue in the average receivable balance. This number is the average collection lag, typically in the 18- to 30-day range. Some practitioners are concerned that in a period of increasing rates, such a calculation over time may tend to slightly understate the collection lag, because the starting receivable balance is based on previous lower rates, and each time rates are increased, it takes time for the receivable balance to reflect the new rates properly. However, the effect is typically less than one tenth or one fifth of a day and therefore, in most cases, it has been ignored.

In the measurement process, the receivable balance and the average revenues must be presented on the same basis. Many states have a sales tax added to the revenues

billed. In those cases, revenues must have the sales tax added before the comparison of receivables to revenues is made. Any other differences in what is included either in revenues or receivables should be considered before making the calculation.

When the comparison of average daily revenues to average daily receivables is used to calculate the collection lag, the effects of budget billing or similar plans are already considered in the calculated answer. If the budget billing customer has paid more than the value of service received the resulting credit is reflected in the daily receivable balance. If the customer has paid less than the value of service received, the larger receivable balance is included. The effects of budget billing are therefore incorporated into the collection lag when the average revenue to average receivable comparison is made.

Using this procedure for calculating the collection lag also eliminates the need for any special treatment of bad debts. The receivable balance is included until it is written off. When the bad debt expense item is considered, the average time frame is measured from when a provision for bad debts is charged to expense until it is used to reduce the receivable balance. This calculation is most easily made by dividing the average day's expense provision for bad debts into the average balance in the reserve for bad debts.

Figure 5-1 is an example of an exhibit filed in a rate proceeding to show the calculation of a lead time from the rendering of service to receipt of revenues. In the case presented, it should be noted that adding the service period, the reading to billing, and collection lags produces a revenue lag of 42.3 days.

More detailed analyses of revenue lags by classes of customers can be made if the receivable balances and revenue amounts can be segregated. Normally, this has not been the case, however, because few companies have segregated their receivable balances by customer classes. As a result, a total company calculation of cash working capital is completed and an allocation to separate classes of customers is made using the standard methodologies used to allocate working capital. An exception to this general statement is that a company typically can segregate wholesale revenues and receivables and, in some cases, present a calculation of cash working capital for FERC jurisdictional customers.

[4] Expense Lag

[a] Operating and Maintenance Lag

After determining the lead time from rendering service to receipt of revenues, determining the lag time in payment of expenses is the next step. Figure 5-2 presents an example of the kind of exhibit that might be presented to show the lag time from when services are rendered and expenses incurred until payments are made. For an electric company, the major expense item is fuel cost. Typically, this would be the first item in the exhibit. In measuring lag time in payment of the fuel expense, fuel costs would generally be segregated by type—coal, natural gas, oil, or nuclear. Added together, these items produce the total electric fuel expense. A typical fuel expense lag calculation is presented in Figure 5-3. In measuring lag time for each of these types of fuel, individual analyses of the purchases from each of the suppliers of the various types of fuel must be prepared. Because fuel cost is such a large percentage of total

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman
SANDRA D. KENNEDY
PAUL NEWMAN
GARY PIERCE
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, ANTHEM WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WASTEWATER DISTRICT, ANTHEM WASTEWATER DISTRICT, AND MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**REJOINDER TESTIMONY
OF
BENTE VILLADSEN
ON BEHALF OF
ARIZONA-AMERICAN COMPANY
MARCH 10, 2009**

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1 **I. EXECUTIVE SUMMARY**

2 Dr. Bente Villadsen, a Principal at *The Brattle Group*, is filing Rejoinder testimony in
3 response to the surrebuttal testimony submitted by Mr. David C. Parcell on behalf of
4 Arizona Corporation Commission Staff and by Mr. William A. Rigsby on behalf of the
5 Residential Utility Consumer Office. She has previously filed Direct and Rebuttal
6 testimony in this proceeding.

7 Both Mr. Parcell and Mr. Rigsby critique Dr. Villadsen's use of American Water's recent
8 debt issue as a benchmark for Arizona-American's cost of equity. It provides recent
9 market information on the cost of capital for the company and therefore highly relevant
10 for the determination of the company's cost of capital.

11 The ongoing financial crisis has had and continues to have a broad impact on utilities'
12 access to and cost of capital. The drop in stock prices is likely caused by numerous
13 factors including earnings expectations, investor risk aversion, and the equity risk
14 premium. Mr. Parcell's surrebuttal mistakenly considers only earnings expectations.

15 Both the Parcell Surrebuttal and the Rigsby Surrebuttal disagree with Dr. Villadsen's
16 critique of their implementation of the DCF and CAPM methodology. However, neither
17 provided textbook or other convincing support for the disputed methods. Therefore, Dr.
18 Villadsen continues to believe her rebuttal critique was merited.

1 **II. INTRODUCTION AND SUMMARY**

2 **Q1. PLEASE STATE YOUR NAME AND ADDRESS FOR THE RECORD.**

3 A1. My name is Bente Villadsen. My business address is *The Brattle Group*, 44 Brattle Street,
4 Cambridge, MA 02138.

5 **Q2. DID YOU PREVIOUSLY FILE TESTIMONY IN THIS PROCEEDING?**

6 A2. Yes, I filed direct testimony (“Villadsen Direct”) on behalf of Arizona-American Water
7 Company (“Arizona-American” or the “Company”) in April 2008 and rebuttal testimony
8 (“Villadsen Rebuttal”) in February 2009 regarding the estimate of the cost of equity for
9 Arizona-American’s districts.

10 **Q3. WHAT IS THE PURPOSE OF YOUR REJOINDER TESTIMONY?**

11 A3. Arizona-American has asked me to review and respond to the surrebuttal testimony of Mr.
12 David C. Parcell (“Parcell Surrebuttal”), who filed testimony on behalf of the Arizona
13 Corporation Commission Staff (the “Staff”), and to the surrebuttal testimony of Mr.
14 William A. Rigsby (“Rigsby Surrebuttal”), who filed testimony on behalf of the
15 Residential Utility Consumer Office.

16 **Q4. DO YOU HAVE ANY PRELIMINARY COMMENTS?**

17 A4. Yes. In an effort to reduce the volume of the material filed in this proceeding, I shall
18 restrict my testimony to clarifications and brief comments on key issues raised in the
19 surrebuttal testimonies rather than a comprehensive discussion of all issues. The fact that
20 I do not respond to all issues raised in the Parcell or Rigsby Surrebuttals does not
21 necessarily imply that I agree with them.

22 **III. COMMENTS ON THE SURREBUTTAL TESTIMONIES**

23 **A. RELEVANCE OF CURRENT MARKET INFORMATION**

24 **Q5. BOTH THE PARCELL SURREBUTTAL AND THE RIGSBY SURREBUTTAL**
25 **CRITIQUE YOUR USE OF AMERICAN WATER’S ISSUANCE OF DEBT AT**

1 **10% AS AN INDICATOR OF THE CURRENT COST OF CAPITAL FOR THE**
2 **COMPANY. HOW DO YOU RESPOND?**

3 A5. Both the Parcell Surrebuttal and the Rigsby Surrebuttal appear to misunderstand my use
4 of the debt issuance by American Water. The Parcell Surrebuttal indicates that the
5 relevant measure against which to evaluate the Company's cost of equity is its embedded
6 cost of debt.¹ The Rigsby Surrebuttal states that it "disagree[s] that a single debt issuance
7 at a particular point in time should be the sole reason for increasing [the] recommended
8 cost of equity."² Recalling that the cost of capital "is the expected rate of return in capital
9 markets on alternative investments of equivalent risk,"³ recent information about the
10 Company's cost of debt becomes important.⁴ The 10% issue by American Water
11 provides recent info about the company's cost of issuing debt – embedded cost reflects
12 the cost of debt in the past, not the cost of issuing new debt now. Therefore, it does
13 provide insights into the current cost of capital for the Company. As the cost of equity is
14 higher than the cost of debt (at least for investment grade entities) it also provides a
15 benchmark against which to evaluate the cost of equity.

16 **Q6. THE PARCELL SURREBUTTAL STATES THAT THE ISSUANCE "TOOK**
17 **PLACE AT VIRTUALLY THE PEAK OF THE INTEREST LEVELS IN LATE**
18 **2008."**⁵ **HOW DO YOU RESPOND?**

19 A6. I agree that the sale took place at a time with very high yields on corporate and utility
20 bonds for which reason, the Villadsen Rebuttal cited the then current yield of this debt
21 issue⁶ rather than its original cost. While the yield on this debt has declined since it was

¹ Parcell Surrebuttal, p. 2.

² Rigsby Surrebuttal, p. 7.

³ Villadsen Direct, p. 5. See also Parcell Direct, p. 4 and Rigsby Direct, p. 5.

⁴ The 10% note in question was issued by American Water Works Capital Corp., but there is no reason to believe that the cost of debt capital for Arizona-American would not be similar.

⁵ Parcell Surrebuttal, p. 3.

⁶ Villadsen Rebuttal, p. 6.

1 first issued, it is still very high and in the range of 9¼ to 9½ percent.⁷ Therefore, the cost
2 of debt remains high and pertains to a much longer period than just at the “peak” or at a
3 “particular point in time.”⁸ Thus, while the cost of this debt does not provide insights into
4 the embedded cost of Arizona-American Water, it does provide a current benchmark on
5 the cost of debt capital for the company.

6 **Q7. DO YOU HAVE ANY COMMENTS ON THE PARCELL SURREBUTTAL'S**
7 **COMMENT THAT YOU SEEM “TO BE EQUATING THE DECLINE IN STOCK**
8 **PRICES WITH AN INCREASE IN THE COST OF EQUITY CAPITAL”?**⁹

9 A7. Yes. It certainly is true that stock prices have dropped substantially.¹⁰ It is also true that
10 expectations of future earnings have dropped. However, it is incorrect to draw the
11 conclusion that the fall in earnings expectations is the *only* cause of the fall in stock
12 prices. The fall in prices can be and likely is, in part, caused by increased risk aversion
13 among investors and/or a higher market risk premium. Simply pointing to the lowered
14 earnings expectations, as the Parcell Surrebuttal does, does not prove that the crisis has
15 left the market risk premium unaffected. As the market volatility has increased
16 substantially as documented in the Villadsen Rebuttal p. 11, it is clear that factors other
17 than a decline in earnings are in play. As noted in the Villadsen Rebuttal, the academic
18 literature agrees that during times of increased volatility and financial distress, the market
19 risk premium increases, so that the cost of equity capital increases.¹¹ Further, as the
20 Parcell Surrebuttal acknowledges, the cost of corporate and utility debt is up,¹² so unless
21 the premium investors require to invest in equity rather than debt has declined
22 substantially, the cost of equity must be up as well.

⁷ As of March 2, 3 and 5, the price on American Water’s 10% issue (EH622214 Corp) was 108.9, 104.9 and 107.95, respectively for a current yield of 9.2%, 9.5% and 9.3%, respectively. As of the time of my rebuttal testimony this yield was 9.7%. Source: Bloomberg.

⁸ Parcell Surrebuttal, p. 3 and Rigsby Surrebuttal, p. 7.

⁹ Parcell Surrebuttal, p. 4.

¹⁰ During the period September 2, 2008 to February 27, 2009, the Dow Jones Industrial Average Index dropped approximately 38.7% while the Dow Jones Utility Average Index dropped approximately 31.3%. Source: Bloomberg.

¹¹ Villadsen Rebuttal, pp. 10-13.

1 **B. IMPLEMENTATION OF ESTIMATION METHODS**

2 **Q8. ARE YOU PERSUADED BY THE PARCELL SURREBUTTAL ARGUMENT**
3 **THAT THE SINGLE-STAGE DCF MODEL IS MORE ACCURATE THAN THE**
4 **MULTI-STAGE MODEL?**¹³

5 A8. No, the Parcell Surrebittal's argument on this point is at odds with the assumptions behind
6 the single-stage DCF model. In particular, the single-stage DCF model computes the
7 current firm value as the present value of its future cash flows forever, not just over the
8 next few years, until the next rate proceeding. Accordingly, proper application of the
9 model requires an estimate of long-term growth rates. That such an estimate is hard to
10 obtain, something with which I agree, does not however imply that expected growth rates
11 over short horizons are preferable, if they are inconsistent with long-term expectations. It
12 simply means that the single-stage DCF model is an inappropriate tool for the industry at
13 this time, as I explain at length in Villadsen Direct.¹⁴

14 **Q9. THE PARCELL SURREBUTTAL ARGUES THAT INVESTORS MUST RELY**
15 **ON HISTORICAL EARNINGS MEASURES, BECAUSE THEY ARE**
16 **PUBLISHED BY VALUE LINE AND OTHER FINANCIAL PUBLICATIONS.**
17 **DO YOU AGREE?**

18 A9. No. While Value Line and other reputable publications do publish historical measures of
19 earnings, dividends and other measures of profitability, this does not imply that investors
20 use them to implement the DCF model. These measures convey important information
21 about a company's *past* performance, its management's ability, as well as the impact of
22 any number of risks and factors that do not affect the company's stock returns. Historical
23 measures of earnings growth can and do serve purposes other than estimating future
24 earnings growth, whereas analyst forecasts are by definition intended to capture the
25 expected future performance of a company's earnings. As discussed in the Villadsen
26 Direct and the Villadsen Rebuttal, to the extent that historical performance does contain

¹² Parcell Surrebittal, p. 3.

¹³ Parcell Surrebittal, pp. 6-7.

¹⁴ See pp. 31-32 of Villadsen Direct, as well as Section I of Appendix D.

1 information about future earnings, it is already reflected in analysts' forecasts. Unless
2 analysts ignore historical performance when they make their forecasts, averaging
3 historical and forecasted growth figures (or the cost-of-equity estimates based on the two
4 measures) entail a double-counting of the historical information.

5 **Q10. HOW DO YOU RESPOND TO THE PARCELL SURREBUTTAL'S CRITICISM**
6 **THAT "THE CASH FLOW TO INVESTORS IN A DCF FRAMEWORK IS**
7 **DIVIDENDS"?¹⁵**

8 A10. The DCF model requires estimates of the growth in cash flows to investors. It is simply
9 not true that dividends are the only channel through which equity investors receive cash
10 distributions on their investment. An obvious example is share repurchases, an event
11 which is not captured by only considering dividend growth rates. By contrast, earnings
12 offer a better measure of long-term cash flows to equity investors, because any kind of
13 cash distributions comes out of earnings – while there are temporary differences between
14 earnings and distributions to investors, they cannot persist forever (recall that the DCF
15 model assumes the same growth rates literally forever).¹⁶

16 **Q11. HOW DO YOU RESPOND TO RIGSBY REBUTTAL'S DEFENSE OF THE**
17 **MODIFICATION OF THE CALCULATION OF THE SUSTAINABLE GROWTH**
18 **RATE?¹⁷**

19 A11. The Rigsby Direct and the Rigsby Surrebuttal provide only one reference for its
20 implementation of the modified DCF methodology.¹⁸ No textbook, academic or
21 practitioner article, or major data provider is cited as recommended this very specific
22 implementation of the DCF model. Therefore, I continue to find it (1) relies on a non-
23 standard methodology and (2) biases the estimated cost of equity downward.

¹⁵ Parcell Surrebuttal, p. 8.

¹⁶ See Villadsen Direct Appendix D for a detailed discussion of this issue and of the DCF model's assumptions.

¹⁷ Rigsby Direct, pp. 11-12.

¹⁸ Testimony of Mr. Stephen Hill.

1 **Q12. THE RIGSBY DIRECT STATES THAT THE “BEST ARGUMENT” FAVORING**
2 **THE RELIANCE ON THE GEOMETRIC MRP IS THAT IT PROVIDES AN**
3 **ACCURATE MEASURE OF “THE EFFECTS OF COMPOUNDING OF THE**
4 **VALUE OF AN INVESTMENT WHEN RETURN VARIABILITY EXISTS.”¹⁹ DO**
5 **YOU AGREE?**

6 A12. No, the Rigsby Direct’s is simply wrong. It is true that the geometric mean of realized
7 returns is the best indicator of past performance, if one is interested in knowing what the
8 rate of return on one’s investment in the market has been over a historical sample period.
9 However, that is not what past returns are used for in the context of estimating the MRP –
10 rather, past returns are used to forecast expected future returns. For this purpose, basic
11 statistical theory shows that the appropriate mean is the arithmetic mean.²⁰ Mr. Rigsby is
12 correct that using the arithmetic average to evaluate the performance on one’s
13 investments would be a serious error, but so is using the geometric mean to estimate the
14 expected MRP, in the context of the example he uses on pp. 14-15 of Rigsby Surrebuttal.
15 These comments also pertain to the Parcell Surrebuttal’s discussion on p. 9, lines 6-11.
16 Arithmetic and geometric averages serve different purposes.

17 **Q13. WHAT ABOUT THE EVIDENCE CITED BY THE RIGSBY DIRECT IN FAVOR**
18 **OF RELYING ON THE GEOMETRIC MEAN?**

19 A13. First, it should be pointed out that the studies cited by Mr. Rigsby do not rely on the
20 simple argument discussed above, which he calls “the best.” Those studies raise issues
21 that have to do, as the Rigsby Direct points out, with possible autocorrelation in stock
22 returns, which I discussed in my rebuttal testimony.²¹ Second, without repeating the
23 evidence I discussed there, I would only repeat here that the Ibbotson SBBi yearbook
24 discusses the issue in the context of their MRP estimate based on historical returns, and
25 concludes that there is no evidence of autocorrelation in the equity risk premium.²²

¹⁹ Rigsby Surrebuttal, pp. 13-15.

²⁰ This point is explained very clearly in, for example, the *Ibbotson SBBi 2008 Valuation Yearbook*, pp. 77-79.

²¹ See footnote 64 on p. 27 of Villadsen Rebuttal.

²² *Ibbotson SBBi 2008 Valuation Yearbook*, p. 81.

1 **Q14. DID YOU IMPLY IN YOUR REBUTTAL TESTIMONY THAT THE PARCELL**
2 **DIRECT RELIED ONLY ON GEOMETRIC ESTIMATES OF THE MRP?**

3 A14. No. Table R 4 on page 27 of Villadsen Rebuttal makes it clear that is not the case, since
4 it compares estimates based only on arithmetic estimates against estimates based on both
5 geometric and arithmetic.

6 **C. RISKS OTHER THAN FINANCIAL RISK**

7 **Q15. IS IT TRUE THAT FINANCIAL RISK IS ONLY ONE OF MANY RISKS**
8 **UNIQUE TO A COMPANY, AND THEREFORE TO SINGLE IT OUT**
9 **AMOUNTS TO BIAS?²³**

10 A15. No, this is simply wrong, as can easily be judged by noting that every serious textbook
11 discusses financial risk adjustment as part of the standard cost-of-capital estimation.
12 However, while financial risk must be considered, the same is not true about the kinds of
13 risks unique to Arizona-American that the Parcell Surrebuttal discusses. It is a
14 fundamental insight of financial economics that *only systematic risk affects* the market
15 price of a company's assets. Risks unique to that company can be diversified by an
16 investor holding a large portfolio, and therefore are not reflected in stock prices.²⁴ This
17 justifies ignoring those risks when estimating the company's cost of equity.

18 **Q16. DOES THE FACT THAT YOU HAVE NOT COMMENTED ON ALL ISSUES IN**
19 **THE PARCELL OR RIGSBY SURREBUTTAL MEAN THAT YOU AGREE**
20 **WITH REMAINING POINTS?**

21 A16. No. Attention was simply restricted to key issues rather than a comprehensive discussion
22 of all issues.

23 **Q17. DOES THIS COMPLETE YOUR REJOINDER TESTIMONY?**

24 A17. Yes.

²³ Parcell Surrebuttal, pp. 5-6.

²⁴ I discussed this issue in detail in Appendix C of Villadsen Direct, pp. C-10 – C-12.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

KRISTIN K. MAYES, Chairman
GARY PIERCE
PAUL NEWMAN
SANDRA D. KENNEDY
BOB STUMP

IN THE MATTER OF THE APPLICATION OF ARIZONA -AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS AGUA FRIA WATER DISTRICT, HAVASU WATER DISTRICT, MOHAVE WATER DISTRICT, PARADISE VALLEY WATER DISTRICT, SUN CITY WEST WATER DISTRICT, AND TUBAC WATER DISTRICT

DOCKET NO. W-01303A-08-0227

IN THE MATTER OF THE APPLICATION OF ARIZONA-AMERICAN WATER COMPANY, AN ARIZONA CORPORATION, FOR A DETERMINATION OF THE CURRENT FAIR VALUE OF ITS UTILITY PLANT AND PROPERTY AND FOR INCREASES IN ITS RATES AND CHARGES BASED THEREON FOR UTILITY SERVICE BY ITS MOHAVE WASTEWATER DISTRICT

DOCKET NO. SW-01303A-08-0227

**REJOINDER TESTIMONY
OF
JOHN C. (JAKE) LENDERKING
ON BEHALF OF
ARIZONA-AMERICAN WATER COMPANY
MARCH 11, 2009**

**REJOINDER TESTIMONY
OF
JOHN C. (JAKE) LENDERKING
ON BEHALF OF
ARIZONA-AMERICAN WATER COMPANY
MARCH 11, 2009**

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1 **EXECUTIVE SUMMARY**

2 Mr. Lenderking testifies as follows:

3 Marshall Magruder cites a statutory provision that allows some water providers to prevent
4 exempt wells from being drilled within their service area. However, this provision does not
5 apply to Arizona-American's Tubac Water District. This statute clearly disallows exempt wells
6 within the lands served by a municipal provider with an assured water supply designation.
7 However, Arizona-American's Tubac Water District, which is considered to be a municipal
8 provider, has not received an assured water supply designation. Therefore, Arizona-American
9 cannot prevent exempt wells in its service area.

10
11 Certificates of assured water supply places the burden and costs of proving 100 years of water.
12 In Tubac this burden was placed on the developer.

13
14 While developers obtained many certificates of assured water supply in the Tubac Water District,
15 Arizona-American has been exploring the possibility of obtaining an assured water supply
16 designation. An issue which will impede Arizona-American's progress is the development of
17 new assured water supply rules by the Arizona Department of Water Resources. This may
18 substantially delay, or prevent Arizona-American from obtaining an assured water supply
19 designation.

1 **I** **INTRODUCTION**

2 **Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND TELEPHONE**
3 **NUMBER.**

4 A. My name is John C. (Jake) Lenderking. My business address is 19820 N. 7th Street, Suite
5 201, Phoenix, Arizona 85024, and my telephone number is 623-445-2410.

6 **Q. ARE YOU THE SAME JAKE LENDERKING WHO PREVIOUSLY SUBMITTED**
7 **DIRECT TESTIMONY IN THIS DOCKET?**

8 A. Yes.

9 **Q. WHAT IS THE PURPOSE OF YOUR REJOINDER TESTIMONY?**

10 A. The purpose of my rejoinder testimony is to discuss an issue raised by Mr. Magruder in
11 his rebuttal testimony concerning exempt wells.

12 **II** **RESPONSE TO MARSHALL MAGRUDER**

13 **Q. AT PAGE 11, LINE 4 OF HIS REBUTTAL TESTIMONY, MR. MAGRUDER**
14 **CLAIMS THAT ARIZONA-AMERICAN IS NOT COMPLYING WITH A.R.S.**
15 **§45-454C CONCERNING THE DRILLING OF EXEMPT WELLS. ARE MR.**
16 **MAGRUDER'S STATEMENTS REGARDING EXEMPT WELLS CORRECT?**

17 A. No. Mr. Magruder does correctly cite a statutory provision that allows some water
18 providers to prevent exempt wells from being drilled within their service area. However,
19 this provision does not apply to Arizona-American's Tubac Water District.

20 **Q. ON PAGE 12 LINE 8 MR. MAGRUDER ARGUES THAT THIS STATUTE DOES**
21 **APPLY, WHY DOES THIS STATUTE NOT APPLY TO ARIZONA-**
22 **AMERICAN'S TUBAC WATER DISTRICT?**

23 A. A.R.S. § 45-454 provides for the drilling of exempt wells. The portion to which Mr.
24 Magruder refers to is in paragraph C, which reads:

1 On or after January 1, 2006, an exempt well otherwise allowed by this section
2 may not be drilled on land if any part of the land is within one hundred feet of the
3 operating water distribution system of a municipal provider with an assured water
4 supply designation within the boundaries of an active management area
5 established on or before July 1, 1994, as shown on a digitized service area map
6 provided to the director by the municipal provider and updated by the municipal
7 provider as specified by the director. (Emphasis added.)

8 This statute clearly disallows exempt wells within the lands served by a municipal
9 provider with an assured water supply designation. However, Arizona-American's Tubac
10 Water District, which is considered to be a municipal provider, has not received an
11 assured water supply designation. Therefore, Arizona-American cannot prevent exempt
12 wells in its service area.

13 **Q. IF ARIZONA-AMERICAN'S TUBAC WATER DISTRICT DOES NOT HAVE AN**
14 **ASSURED WATER SUPPLY DESIGNATION, DOES THAT MEAN THAT NEW**
15 **SUBDIVISIONS ARE NOT MEETING THE ASSURED WATER SUPPLY**
16 **RULES?**

17 A. No, individual developers have been and continue to be responsible for obtaining
18 certificates of assured water supply for 100 years.

19 **Q. WHY DOES ARIZONA-AMERICAN NOT HAVE AN ASSURED WATER**
20 **SUPPLY DESIGNATION FOR ITS TUBAC WATER DISTRICT IF HAVING**
21 **ONE CAN PREVENT EXEMPT WELLS FROM BEING DRILLED?**

22 A. As mentioned above, the Tubac Water District developed by a different mechanism.
23 Developers have obtained certificates of assured water supply for 100 years for each
24 subdivision instead of the municipal water provider obtaining an assured water
25 designation for 100 years. Before the above statutory change and its commencement in
26 2006 the two mechanisms provided the same benefits. Additionally, using certificates of
27 assured water supply placed the burden and costs of proving 100 years of water on the

1 developer, but gaining an assured water supply designation places the burden and costs
2 on the water provider.

3 Although many certificates of assured water supply have been obtained in the Tubac
4 Water District, we have been exploring the possibility of obtaining an assured water
5 supply designation. A big issue which will impede Arizona-American's progress is the
6 development of new assured water supply rules by the Arizona Department of Water
7 Resources ("ADWR"). The assured supply designation application process is lengthy
8 and may span well over a year. Should ADWR complete the new assured water supply
9 rules before completing the assured water supply designation for the Tubac Water
10 District, ADWR would in all likelihood require that new rules then be followed and thus
11 restart the application process. This may substantially delay, or prevent Arizona-
12 American from obtaining an assured water supply designation.

13 **Q. DOES THIS CONCLUDE YOUR REJOINDER TESTIMONY?**

14 **A. Yes.**

A Schedules

**Agua Fria
Water**

Company Rejoinder

Line No.				
1	Original Cost Rate Base			\$ 92,049,310
2				
3	Adjusted Operating Income			3,016,852
4				
5	Current Rate of Return			3.28%
6				
7	Required Operating Income			\$ 7,732,142
8				
9	Required Rate of Return			8.40%
10				
11	Operating Income Deficiency			\$ 4,715,290
12				
13	Gross Revenue Conversion Factor			1.6553
14				
15	Increase in Gross Revenue Requirement			\$ 7,805,169
16				
17				
18	Customer	Present	Proposed	Dollar
19	Classification	Rates	Rates	Increase
20				Percent
21	Residential	\$13,633,335		0.00%
22	Commercial	3,920,854		0.00%
23	OPA	31,032		0.00%
24	Sale for Resale	123,440		0.00%
25	Private Fire	108,160		0.00%
26	Misc Irrigation Sales	96,636		0.00%
27				
28	Total Water Revenues	<u>\$17,913,457</u>	<u>\$25,718,626</u>	<u>\$ 7,805,169</u> <u>43.57%</u>
29				
30	Other Revenues	905,117	\$905,117	\$0 0.00%
31				
32	Total Revenues	<u>\$18,818,574</u>	<u>\$26,623,742</u>	<u>\$7,805,169</u> <u>41.48%</u>
33				
34				
35				
36				
37				
38				
39				
40	Supporting Schedules:			
41	B-1			
42	C-1			
43	H-1			
44				
45				
46				
47				
48				
49				
50	\\Schedules\2007 Agua Fria Water Sch. A-F.xls\			

B Schedules

Agua Fria
Water

Company Rejoinder					
Line No.	[A]	[B]	[C]	[D]	[E]
	Adjusted End of Test Year	Co Error in Rebuttal forgot to subtract Sierra M PTY	Adjust Working Capital	Total Rebuttal Pro Forma Adjustments	Rebuttal Adjusted End of Test Year
1	Gross Utility				
2	Plant in Service	\$ 211,163,735	\$ (252,470)	\$ (252,470)	\$ 210,911,265
3	CWIP for the White Tanks Project	25,000,000		-	25,000,000
4					
5	Less:				
6	Accumulated Depreciation	20,035,879		-	20,035,879
7					
8	Net Utility Plant				
9	in Service	\$ 216,127,856	\$ (252,470)	\$ -	\$ (252,470) \$ 215,875,386
10					
11	Less:				
12	Advances in Aid of				
13	Construction	98,233,813		-	98,233,813
14	Contributions in Aid of	-		-	-
15	Construction - Net	28,243,244		-	28,243,244
16	Imputed Regulatory Advances	-		-	-
17	Imputed Regulatory Contributions	796,965		-	796,965
18	Customer Meter Deposits	19,040		-	19,040
19	Deferred Income Taxes	(2,839,311)		-	(2,839,311)
20	Investment Tax Credits	-		-	-
21		-		-	-
22		-		-	-
23	Plus:				
24	Deferred Debits	208,401		-	208,401
25	Working capital	467,174	(47,899)	(47,899)	419,274
26	Utility Plant Acquisition Adjustment	-		-	-
27					
28	Total	\$ 92,349,679	\$ (252,470)	\$ (47,899)	\$ (300,369) \$ 92,049,310

33 ¹ RUCO RB Adjustment #5 is
 34 the same dollar amount.

39 Supporting Schedules:

40 B-5

41 E-1

42 08 AZ MEGA\Common\Workpapers\CZN AZAM

43 08 AZ MEGA\08 Agua Fria Water\Workpapers\R:

44 08 AZ MEGA\08 Agua Fria Water\Workpapers\R:

45 08 AZ MEGA\Common\Workpapers\Ariz Trial Ba

46 08 AZ MEGA\Common\Workpapers\Corp Rate B

47 08 AZ MEGA\Common\Workpapers\Corp Rate B

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50 \Schedules\2007 Agua Fria Water Sch. A-F.xls\

Company Rejoinder

Line		
<u>No.</u>		
1		
2	Working Cash Requirement	\$ 12,206
3	Material and Supplies Inventories	192,139 ¹
4	Prepayments	214,929
5		
6		
7	Total Working Capital Allowance, Rebuttal	<u>\$ 419,274</u>
8		
9	Total Adjusted Test Year Working Capital Allowance	\$ 467,174
10		
11	Increase (Decrease in Working Capital Allowance	<u>\$ (47,899)</u>
12		
13	Increase (Decrease in Working Capital Allowance	<u>\$ (47,899)</u>
14		
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43	Supporting Schedules:	Recap Schedules:
44	E-1	B-1
45	Workpapers & Supporting Documents:	
46	¹ Thirteen-month average	
47		
48		
49		
50	\\Schedules\2007 Agua Fria Water Sch. A-F.xls\	

AGUA FRIA WATER

Company Rejoinder

Line No.		Test Year Adjusted Results	Revenue Lag Days	Expense Lag Days	Net Lag Days	Lead/Lag Factor	Cash Working Capital Required
1	OPERATING EXPENSES						
2	P08 Labor	\$ 1,369,604	47.90683	12.0000	35.9068	0.0984	\$ 134,735
3	P09 Purchased Water	901,467	47.90683	86.8700	(38.9632)	(0.1067)	(96,230)
4	P10 Fuel & Power	1,954,815	47.90683	32.4200	15.4868	0.0424	82,942
5	P11 Chemicals	981,930	47.90683	28.4700	19.4368	0.0533	52,289
6	P12 Waste Disposal	-	47.90683	30.0000	30.0000	0.0822	-
7	P13 Management Fees	2,775,604	47.90683	(3.8800)	51.7868	0.1419	393,807
8	P14 Group Insurance	396,645	47.90683	(4.6445)	52.5513	0.1440	57,107
9	P15 Pensions	240,413	47.90683	45.0000	2.9068	0.0080	1,915
10	P17 Insurance Other Than Group	158,153	47.90683	45.0000	2.9068	0.0080	1,260
11	P18 Customer Accounting	370,806	47.90683	7.4600	40.4468	0.1108	41,090
12	P19 Rents	63,217	47.90683	(10.6818)	58.5886	0.1605	10,147
13	P27- Depreciation & Amortization		-	-	-	-	-
14	Other Operating Expenses ¹	1,283,596	47.90683	30.0000	17.9068	0.0491	62,973
15	TAXES						
16	P29 Taxes Other than Income	128,923	47.90683	15.6511	32.2557	0.0884	11,393
17	P29 Property Taxes	803,072	47.90683	212.5000	(164.5932)	(0.4509)	(362,138)
18	P30- Income Tax ²	3,176,810	47.90683	42.0402	5.8667	0.0161	51,061
19							
20	P56- Interest	2,678,635	47.90683	106.5200	(58.6132)	(0.1606)	(430,146)
21							
22							
23							
24							
25							
26							
27	WORKING CASH REQUIREMENT	<u>\$ 17,283,690</u>					<u>\$ 12,206</u>

¹All other Operating Expenses are assumed to be paid by the 15th of the month following the receipt of goods and services.

²At proposed rates.

C Schedules

**Agua Fria
Water**

Arizona American Water Company - Agua Fria Water
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-1RJ

Exhibit
 Schedule C-2 Rebuttal
 Page 2
 Witness: Hubbard

Line			
<u>No.</u>			
1	<u>Adjust Depreciation Expense to Reflect Test Year Adjusted Plant:</u>		
2			
3	Annualized Depreciation Expense on Test Year UPIS	\$	4,993,947
4	Depreciation Expense on Post-Test Year Plant Additions		50,405
5	Depreciation Expense on Acquisition Adjustment		-
6	Amortization of Regulatory Assets		2,918
7			
8			
9	Less: Amortization of Contributions		689,025
10	Amortization of Imputed Regulatory CIAC		197,344
11			
12	Total Depreciation Expense	\$	<u>4,160,901</u>
13			
14	Adjusted Test Year Depreciation Expense		<u>4,391,874</u>
15			
16	Increase (Decrease) in Depreciation Expense		<u>(230,973)</u>
17			
18	Adjustment to Revenues and/or Expenses	\$	<u>(230,973)</u>
19			
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45	Workpapers & Supporting Documents:		
46	\Schedules\2007 Agua Fria Water Sch. A-F.xls\		
47	\08 Agua Fria Water\Workpapers\Expenses\A of I - Agua Fria Water.xls		
48	\Common\Workpapers\Expenses\RegAssets04RateCase.xls		
49	\08 Agua Fria Water\Workpapers\Rate Base\Imputed AIAC and CIAC.xls		
50			

Arizona American Water Company - Agua Fria Water
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-2RJ

Exhibit
 Schedule C-2 Rejoinder
 Page 3
 Witness: Hubbard

Line No.		[A] Property Tax Expense For Conversion Factor	[B] Property Tax Expense
1	Adjust Property Taxes to Reflect Proposed Revenues:		
2			
3	Adjusted Revenues in year ended Dec. 2007	\$ 18,818,613	\$ 18,818,613
4	Adjusted Revenues in year ended Dec. 2007	18,818,613	18,818,613
5	Proposed Revenues	<u>\$ 18,818,613</u>	<u>\$ 26,623,782</u>
6	Average of three year's of revenue	\$ 18,818,613	\$ 21,420,336
7	Average of three year's of revenue, times 2	\$37,637,226	\$42,840,672
8	Add:		
9	Construction Work in Progress at 10%	1,422,630	1,422,630
10	Deduct:		
11	Net Book Value of Transportation Equipment	\$ -	\$ -
12			
13	Full Cash Value	\$ 39,059,856	\$ 44,263,302
14	Assessment Ratio	23%	23%
15	Assessed Value	8,983,767	10,180,559
16	Property Tax Rate	8.939151%	8.939151%
17			
18	Property Tax	803,072	910,056
19	Tax on Parcels	-	-
20			
21	Total Property Tax at Proposed Rates	\$ 803,072	\$ 910,056
22	Property Taxes in the test year-Rebuttal	<u>803,072</u>	<u>803,072</u>
23	Adjustment to Revenues and/or Expenses	<u>\$ 0</u>	<u>\$ 106,983</u>
24			
25			
26			
27			
28	Increase in Property Tax Due to Increase in Revenue Requirement (Line 23 Col [B])		\$ 106,983
29			
30	Increase in Revenue Requirement (From Sch. A1)		\$ 7,805,169
31			
32	Increase in Property Tax Per Dollar Increase in Revenue (Line 32/Line 34)		1.3707%
33			
34			
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43	Workpapers & Supporting Documents:		
44	\\Schedules\2007 Agua Fria Water Sch. A-F.xls\		
45	\\Common\Workpapers\Property Taxes\2007 pd in 07-08 AZ Tax Payment .xls		
46	\\08 Agua Fria Water\Workpapers\Expenses\A of 1 - Agua Fria Water.xls		
47			
48			
49			
50			

Line No.		Test Year Adjusted Results	Adjusted with Rate Increase
1	<u>Calculation of Income Taxes at Proposed Rates</u>		
2			
3			
4	Operating Income Before Inc. Taxes	\$ 3,229,467	\$ 10,908,952
5	Interest Expense	\$ 2,678,635	\$ 2,678,635
6	Arizona Taxable Income	<u>550,832</u>	<u>8,230,317</u>
7			
8	Less Arizona Income Tax	\$ 38,382	\$ 573,489
9	Arizona Income Tax Rate = 6.968%		
10			
11	Federal Income Before Taxes	\$ 550,832	\$ 8,230,317
12	Less Arizona Income Taxes	38,382	573,489
13	Federal Taxable Income	<u>\$ 512,450</u>	<u>\$ 7,656,829</u>
14			
15	Federal Income Taxes: 34.000%	\$ 174,233	\$ 2,603,322
16			
17			
18	Total Income Tax	<u>\$ 212,615</u>	<u>\$ 3,176,810</u>
19			
20	Tax Rate	<u>38.60%</u>	<u>38.60%</u>
21			
22	Effective Income Tax Rates		
23	State	6.968%	6.968%
24	Federal	31.63%	31.63%
25			
26			
27	Adjusted Test Year Income Taxes-Rebuttal	<u>\$ 120,088</u>	
28	Increase in Income Taxes	<u>92,527</u>	
29			
30	Adjustment to Revenues and/or Expense	<u>\$ 92,527</u>	
31			
32	Test Year Income Taxes, Rejoinder		<u>\$ 212,615</u>
33	Increase in Income Taxes		<u>2,964,195</u>
34			
35	Adjustment to Revenues and/or Expense		<u>2,964,195</u>
36			
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44			
45	Workpapers & Supporting Documents:		
46	\\Schedules\2007 Agua Fria Water Sch. A-F.xls\		
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Arizona American Water Company - Agua Fria Water
Test Year Ended December 31, 2007
Income Statement Adjustment SLH-4RJ

Exhibit
Schedule C-2 Rejoinder
Page 5
Witness: Hubbard

Line No.		
1	Interest Synchronization with Rate Base	
2		
3	Original Cost Rate Base (Sch. B-1, Ln. 24)	\$92,049,310
4	Weighted Cost of Debt from Schedule D-1	<u>2.91%</u>
5	Synchronized Interest Expense	<u>2,678,635</u>
6	Test Year Interest Expense	2,687,376
7		
8	Adjusted Test Year Interest Expense	<u>2,687,376</u>
9		
10	Increase (decrease) in Interest Expense	<u>\$ (8,741)</u>
11		
12	Adjustment to Revenues and/or Expense	<u>(8,741)</u>
13		
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45	Workpapers & Supporting Documents:	
46	\\Schedules\2007 Agua Fria Water Sch. A-F.xls\	
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Company Rejoinder

Line No.	Description	Percentage of Incremental Gross Revenues
1	Federal Income Taxes	31.63%
2		
3	State Income Taxes	6.97%
4		
5	Property Taxes Effective Rate = 1.3707% Combined 38.60%	
6		
7	Bad Debt Expense Effective Rate = 0.24% One Minus Combined 61.40%	0.84%
8		
9	Total Tax Percentage	39.59%
10		
11	Operating Income % = 100% - Tax Percentage	60.41%
12		
13		
14		
15		
16	1 = Gross Revenue Conversion Factor	
17	Operating Income %	1.6553
18		
19		
20		
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43	Supporting Schedules:	Recap Schedules:
44		A-1
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A Schedules

Havasu

Water

Company Rejoinder

Line
 No.

1	Original Cost Rate Base		\$	3,887,188
2				
3	Adjusted Operating Income			70,106
4				
5	Current Rate of Return			1.80%
6				
7	Required Operating Income		\$	326,524
8				
9	Required Rate of Return			8.40%
10				
11	Operating Income Deficiency		\$	256,418
12				
13	Gross Revenue Conversion Factor			1.6682
14				
15	Increase in Gross Revenue			
16	Requirement		\$	427,756
17				
18	Customer	Present	Proposed	Dollar
19	<u>Classification</u>	<u>Rates</u> ¹	<u>Rates</u>	<u>Increase</u>
20				<u>Percent</u>
21	Residential	\$1,023,138		0.00%
22	Commercial	131,273		0.00%
23				
24	Total Water Revenues	\$1,154,411	\$1,582,167	\$ 427,756
25				37.05%
26	Other Revenues	23,110	23,110	-
27				0.00%
28	Total Revenues	\$1,177,522	\$1,605,277	\$427,756
29				36.33%
30				
31		¹ Includes Step 2 ACRM in Present Rate Revenue.		
32				
33				
34				
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40	Supporting Schedules:			
41	B-1			
42	C-1			
43	H-1			
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49				
50	\\Schedules\2007 Havasu Water Sch. A-F.xls\			

B Schedules

Havasu Water

Arizona American Water Company - Havasu Water
 Test Year Ended December 31, 2007
 Original Cost Rate Base Proforma Adjustments

Exhibit
 Schedule B-2 Rejoinder
 Page 1
 Witness: Gutowski

Line No.	Company Rejoinder					
	[A] Rebuttal Adjusted End of Test Year	[B] Company LJG-1RJ Move ACRM Deferral	[C] Accept/Reject STAFF RB # 5 Advances Gateway	[D] Adjust Working Capital	[E] Total Rebuttal Pro Forma Adjustments	[F] Rebuttal Adjusted End of Test Year
1	Gross Utility					
2	Plant in Service	\$ 9,020,993	\$ (94,996)		\$ (94,996)	\$ 8,925,997
3		-			-	-
4	Less:					
5						
6	Accumulated Depreciation	1,307,146			-	1,307,146
7						
8	Net Utility Plant					
9	in Service	\$ 7,713,847	\$ -	\$ -	\$ (94,996)	\$ 7,618,851
10						
11	Less:					
12	Advances in Aid of					
13	Construction	3,217,334	(656,267)		(656,267)	2,561,067
14	Contributions in Aid of	-			-	-
15	Construction - Net	1,355,090			-	1,355,090
16	Imputed Regulatory Advances	-			-	-
17	Imputed Regulatory Contributions	113,427			-	113,427
18	Customer Meter Deposits	512			-	512
19	Deferred Income Taxes	(131,385)			-	(131,385)
20	Investment Tax Credits	-			-	-
21		-			-	-
22		-			-	-
23	Plus:					
24	Deferred Debits	9,673	94,996		94,996	104,669
25	Working capital	56,033		6,346	6,346	62,380
26	Utility Plant Acquisition Adjustment	-			-	-
27						
28	Total	\$ 3,224,575	\$ 94,996	\$ 656,267	\$ 6,346	\$ 662,613
29						
30						
31						
32						
33	¹ RUCO RB Adjustment #5 is					
34	the same dollar amount.					
35						
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38						
39	Supporting Schedules:					
40	B-5					
41	E-1					
42	08 AZ MEGA\08 Havasu Water\Work Papers\Rat					
43	08 AZ MEGA\08 Havasu Water\Work Papers\Rat					
44	08 AZ MEGA\Common\Workpapers\Corp Rate B:					
45	08 AZ MEGA\Common\Workpapers\Corp Rate B:					
46						
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48						
49						
50	\\Schedules\2007 Havasu Water Sch. A-F.xls\					

Company Rejoinder

Line		
<u>No.</u>		
1		
2	Working Cash Requirement	53,338
3	Material and Supplies Inventories	4,486 ¹
4	Prepayments	4,556
5		
6		
7	Total Working Capital Allowance	<u>\$ 62,380</u>
8		
9	Total Adjusted Test Year Working Capital Allowance-Rebuttal	\$ 56,033
10		
11	Increase (Decrease in Working Capital Allowance	<u>\$ 6,346</u>
12		
13	Increase (Decrease in Working Capital Allowance	<u>\$ 6,346</u>
14		
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43	Supporting Schedules:	Recap Schedules:
44	E-1	B-1
45	Workpapers & Supporting Documents:	
46	¹ Thirteen-month average	
47		
48		
49		
50	\\Schedules\2007 Havasu Water Sch. A-F.xls\	

HAVASU WATER

Company Rejoinder

Line No.	Test Year Adjusted Results	Revenue Lag Days	Expense Lag Days	Net Lag Days	Lead/Lag Factor	Cash Working Capital Required	
1	OPERATING EXPENSES						
2	\$ 202,482	48.44106	12.0000	36.4411	0.0998	\$ 20,216	
3	P08 Labor	-	48.44106	86.8700	(38.4289)	(0.1053)	
4	P09 Purchased Water	111,139	48.44106	32.4200	16.0211	0.0439	4,878
5	P10 Fuel & Power	96,165	48.44106	28.4700	19.9711	0.0547	5,262
6	P11 Chemicals	-	48.44106	30.0000	18.4411	0.0505	-
7	P12 Waste Disposal	164,457	48.44106	(3.8800)	52.3211	0.1433	23,574
8	P13 Management Fees	63,729	48.44106	(4.6445)	53.0856	0.1454	9,269
9	P14 Group Insurance	35,586	48.44106	45.0000	3.4411	0.0094	335
10	P15 Pensions	8,974	48.44106	45.0000	3.4411	0.0094	85
11	P17 Insurance Other Than Group	22,062	48.44106	7.4600	40.9811	0.1123	2,477
12	P18 Customer Accounting	5,059	48.44106	(10.6818)	59.1229	0.1620	819
13	P19 Rents		48.44106	-	48.4411	0.1327	-
14	P27- Depreciation & Amortization	103,211	48.44106	30.0000	18.4411	0.0505	5,215
15	Other Operating Expenses ¹						
16	TAXES						
17	P29 Taxes Other than Income	17,638	48.44106	15.6511	32.7900	0.0898	1,584
18	P29 Property Taxes	50,566	48.44106	212.5000	(164.0589)	(0.4495)	(22,728)
19	P30- Income Tax ²	134,155	48.44106	42.0402	6.4009	0.0175	2,353
20	P56- Interest	113,117		106.5200			
21							
22							
23							
24							
25							
26	WORKING CASH REQUIREMENT	<u>\$ 1,128,339</u>				<u>\$ 53,338</u>	

¹All other Operating Expenses are assumed to be paid by the 15th of the month following the receipt of goods and services.

²At proposed rates.

C Schedules

Havasu Water

Line			
<u>No.</u>			
1	<u>Adjust Depreciation Expense to Reflect Test Year Adjusted Plant:</u>		
2			
3	Annualized Depreciation Expense on Test Year UPIS	\$	286,651
4	Depreciation Expense on Post-Test Year Plant Additions		-
5	Depreciation Expense on Acquisition Adjustment		-
6	Amortization of Regulatory Assets (Decision No. 67093)		834
7			
8			
9	Less: Amortization of Contributions		6,011
10	Amortization of Imputed Regulatory CIAC		28,087
11			
12	Total Depreciation Expense	\$	<u>253,387</u>
13			
14	Adjusted Test Year Depreciation Expense		<u>278,639</u>
15			
16	Increase (decrease) in Depreciation Expense		<u>(25,252)</u>
17			
18	Adjustment to Revenues and/or Expenses	\$	<u>(25,252)</u>
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45	Workpapers & Supporting Documents:		
46	\\Schedules\2007 Havasu Water Sch. A-F.xls\		
47	\\Common\Workpapers\Expenses\RegAssets04RateCase.xls		
48	\\08 Havasu Water\Work Papers\Expenses\A of I - Havasu Water.xls		
49	\\08 Havasu Water\Work Papers\Rate Base\Imputed AIAC and CIAC.xls		
50			

Arizona American Water Company - Havasu Water
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-2RJ

Exhibit
 Schedule C-2 Rejoinder
 Page 3
 Witness: Hubbard

Line No.		[A] Property Tax Expense For Conversion Factor	[B] Property Tax Expense
1	Adjust Property Taxes to Reflect Proposed Revenues:		
2			
3	Adjusted Revenues in year ended Dec. 2007	\$ 1,177,522	\$ 1,177,522
4	Adjusted Revenues in year ended Dec. 2007	1,177,522	1,177,522
5	Proposed Revenues	<u>1,177,522</u>	<u>1,605,277</u>
6	Average of three year's of revenue	\$ 1,177,522	\$ 1,320,107
7	Average of three year's of revenue, times 2	\$2,355,044	\$2,640,214
8	Add:		
9	Construction Work in Progress at 10%	10,080	10,080
10	Deduct:		
11	Net Book Value of Transportation Equipment	<u>\$ -</u>	<u>\$ -</u>
12			
13	Full Cash Value	\$ 2,365,124	\$ 2,650,294
14	Assessment Ratio	<u>23%</u>	<u>23%</u>
15	Assessed Value	543,978	609,568
16	Property Tax Rate	9.295630%	9.295630%
17			
18	Property Tax	50,566	56,663
19	Tax on Parcels	-	-
20			
21	Total Property Tax at Proposed Rates	<u>\$ 50,566</u>	<u>\$ 56,663</u>
22	Property Taxes in the test year-Rebuttal	50,566	50,566
23	Adjustment to Revenues and/or Expenses	<u>\$ -</u>	<u>\$ 6,097</u>
24			
25			
26			
27			
28	Increase in Property Tax Due to Increase in Revenue Requirement (Line 23 Col [B])		\$ 6,097
29			
30	Increase in Revenue Requirement (From Sch. A1)		\$ 427,756
31			
32	Increase in Property Tax Per Dollar Increase in Revenue (Line 32/Line 34)		1.4253%
33			
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42			
43	Workpapers & Supporting Documents:		
44	\Schedules\2007 Havasu Water Sch. A-F.xls\		
45	\Common\Workpapers\Property Taxes\2007 pd in 07-08 AZ Tax Payment .xls		
46	\08 Agua Fria Water\Workpapers\Expenses\A of I - Agua Fria Water.xls		
47			
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Line No.		Test Year Adjusted Results	Adjusted with Rate Increase
1	<u>Calculation of Income Taxes at Proposed Rates</u>		
2			
3			
4	Operating Income Before Inc. Taxes	\$ 43,067	\$ 460,679
5	Interest Expense	\$ 113,117	\$ 113,117
6	Arizona Taxable Income	<u>(70,050)</u>	<u>347,561</u>
7			
8	Less Arizona Income Tax	\$ (4,881)	\$ 24,218
9	Arizona Income Tax Rate = 6.968%		
10			
11	Federal Income Before Taxes	\$ (70,050)	\$ 347,561
12	Less Arizona Income Taxes	(4,881)	24,218
13	Federal Taxable Income	<u>(65,169)</u>	<u>323,343</u>
14			
15	Federal Income Taxes: 34.000%	\$ (22,157)	\$ 109,937
16			
17			
18	Total Income Tax	<u>\$ (27,038)</u>	<u>\$ 134,155</u>
19			
20	Tax Rate	<u>38.60%</u>	<u>38.60%</u>
21			
22	Effective Income Tax Rates		
23	State	6.968%	6.968%
24	Federal	31.63%	31.63%
25			
26			
27	Adjusted Test Year Income Taxes-Rebuttal	<u>\$ (29,343)</u>	
28	Increase in Income Taxes	<u>2,304</u>	
29			
30	Adjustment to Revenues and/or Expense	<u>\$ 2,304</u>	
31			
32	Test Year Income Taxes, Rejoinder		\$ (27,038)
33	Increase in Income Taxes		161,193
34			
35	Adjustment to Revenues and/or Expense		<u>161,193</u>
36			
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44			
45	Workpapers & Supporting Documents:		
46	\\Schedules\2007 Havasu Water Sch. A-F.xls\		
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Arizona American Water Company - Havasu Water
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-4RJ

Exhibit
 Schedule C-2 Rejoinder
 Page 5
 Witness: Hubbard

Line			
No.			
1	<u>Interest Synchronization with Rate Base</u>		
2			
3	Original Cost Rate Base (Sch. B-1, Ln. 24)		\$3,887,188
4	Weighted Cost of Debt from Schedule D-1		<u>2.91%</u>
5	Synchronized Interest Expense		<u>113,117</u>
6	Test Year Interest Expense-Rebuttal	93,835	
7		<u> </u>	
8	Adjusted Test Year Interest Expense-Rebuttal		<u>93,835</u>
9			
10	Increase (decrease) in Interest Expense		<u>\$ 19,282</u>
11			
12	Adjustment to Revenues and/or Expense		<u>19,282</u>
13			
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45	Workpapers & Supporting Documents:		
46	\Schedules\2007 Havasu Water Sch. A-F.xls\		
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Company Rejoinder

Line No.	Description	Percentage of Incremental Gross Revenues
1	Federal Income Taxes	31.63%
2		
3	State Income Taxes	6.97%
4		
5	Property Taxes	38.60%
6	Effective Rate = 1.4253% One Minus Combined	61.40%
7	Bad Debt Expense	0.88%
8	Effective Rate = 0.95% One Minus Combined	61.40%
9	Total Tax Percentage	40.06%
10		
11	Operating Income % = 100% - Tax Percentage	59.94%
12		
13		
14		
15		
16	1 = Gross Revenue Conversion Factor	
17	Operating Income %	1.6682
18		
19		
20		
21		
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43	Supporting Schedules:	Recap Schedules:
44		A-1
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49		

A Schedules

Mohave

Water

Company Rejoinder

Line
 No.

1	Original Cost Rate Base			\$ 10,235,260
2				
3	Adjusted Operating Income			298,400
4				
5	Current Rate of Return			2.92%
6				
7	Required Operating Income			\$ 859,762
8				
9	Required Rate of Return			8.40%
10				
11	Operating Income Deficiency			\$ 561,362
12				
13	Gross Revenue Conversion Factor			1.6807
14				
15	Increase in Gross Revenue			
16	Requirement			\$ 943,485
17				
18	Customer	Present	Proposed	Dollar
19	Classification	Rates	Rates	Increase
20				Percent
21	Residential	\$ 3,816,354		0.00%
22	Commercial	915,183		0.00%
23	OPA	176,051		0.00%
24	Private Fire	25,081		0.00%
25				
26	Total Water Revenues	\$ 4,932,669	\$ 5,876,093	\$ 943,424
27				19.13%
28	Other Revenue	181,023	181,023	- 0.00%
29				
30	Total Water Revenues	\$5,113,692	\$6,057,116	\$943,424
31				18.45%
32				
33				
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39				
40	Supporting Schedules:			
41	B-1			
42	C-1			
43	H-1			
44				
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B Schedules

Mohave Water

Company Rejoinder						
Line No.	[A]	[B]	[C]	[D]	[E]	
	Adjusted End of Test Year	Accept STAFF RB # 7 Advances Gateway	Adjust Working Capital	Total Rebuttal Pro Forma Adjustments	Rebuttal Adjusted End of Test Year	
1	Gross Utility					
2	Plant in Service	\$ 29,553,954		\$ -	\$ 29,553,954	
3		-		-	-	
4	Less:					
5						
6	Accumulated Depreciation	13,129,988		-	13,129,988	
7						
8	Net Utility Plant					
9	in Service	\$ 16,423,966	\$ -	\$ -	\$ 16,423,966	
10						
11	Less:					
12	Advances in Aid of					
13	Construction	5,947,009	656,267	656,267	6,603,276	
14	Contributions in Aid of	-		-	-	
15	Construction - Net	135,062		-	135,062	
16	Imputed Regulatory Advances	-		-	-	
17	Imputed Regulatory Contributions	1,157,044		-	1,157,044	
18	Customer Meter Deposits	7,800		-	7,800	
19	Deferred Income Taxes	(1,360,455)		-	(1,360,455)	
20	Investment Tax Credits	-		-	-	
21		-		-	-	
22		-		-	-	
23	Plus:					
24	Deferred Debits	99,833		-	99,833	
25	Working capital	252,567	\$ 1,623	1,623	254,190	
26	Utility Plant Acquisition Adjustment	-		-	-	
27						
28	Total	\$ 10,889,904	\$(656,267)	\$ 1,623	\$(654,644)	\$ 10,235,260

¹ RUCO RB Adjustment #5
 is the same dollar amount.

Supporting Schedules:

B-5
E-1

- 08 AZ MEGA\08 Mohave Water\Work Papers\Ra
- 08 Mohave Water\Work Papers\Rate Base\ACC
- 08 AZ MEGA\Common\Workpapers\Corp Rate B
- 08 AZ MEGA\Common\Workpapers\Corp Rate B

Company Rebuttal

Line			
<u>No.</u>			
1			
2	Working Cash Requirement	\$	187,330
3	Material and Supplies Inventories		8,897 ¹
4	Prepayments		57,963
5			
6			
7	Total Working Capital Allowance	\$	254,190
8			
9	Total Adjusted Test Year Working Capital Allowance	\$	252,567
10			
11	Increase (Decrease in Working Capital Allowance	\$	1,623
12			
13	Increase (Decrease in Working Capital Allowance	\$	1,623
14			
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43	Supporting Schedules:		Recap Schedules:
44	E-1		B-1
45	Workpapers & Supporting Documents:		
46	¹ Thirteen-month average		
47			
48			
49			
50	\\Schedules\2007 Mohave Water Sch. A-F.xls\		

MOHAVE WATER

Company Rejoinder

Line No.		Test Year Adjusted Results	Revenue Lag Days	Expense Lag Days	Net Lag Days	Lead/Lag Factor	Cash Working Capital Required
1	OPERATING EXPENSES						
2	P08 Labor	\$ 887,205	48.15644	12.0000	36.1564	0.0991	\$ 87,885
3	P09 Purchased Water	44,384	48.15644	86.8700	(38.7136)	(0.1061)	(4,708)
4	P10 Fuel & Power	501,877	48.15644	32.4200	15.7364	0.0431	21,638
5	P11 Chemicals	7,846	48.15644	28.4700	19.6864	0.0539	423
6	P12 Waste Disposal	-	48.15644	30.0000	18.1564	0.0497	-
7	P13 Management Fees	929,574	48.15644	(3.8800)	52.0364	0.1426	132,525
8	P14 Group Insurance	209,312	48.15644	(4.6445)	52.8009	0.1447	30,279
9	P15 Pensions	127,879	48.15644	45.0000	3.1564	0.0086	1,106
10	P17 Insurance Other Than Group	51,991	48.15644	45.0000	3.1564	0.0086	450
11	P18 Customer Accounting	132,002	48.15644	7.4600	40.6964	0.1115	14,718
12	P19 Rents	15,559	48.15644	(10.6818)	58.8382	0.1612	2,508
13	P27-; Depreciation & Amortization		48.15644	-	48.1564	0.1319	-
14	Other Operating Expenses ¹	710,341	48.15644	30.0000	18.1564	0.0497	35,335
15	TAXES						
16	P29 Taxes Other than Income	75,809	48.15644	15.6511	32.5054	0.0891	6,751
17	P29 Property Taxes	221,817	48.15644	212.5000	(164.3436)	(0.4503)	(99,875)
18	P30-; Income Tax ²	353,240	48.15644	42.0402	6.1163	0.0168	5,919
19							
20	P56-; Interest	297,846	48.15644	106.5200	(58.3636)	(0.1599)	(47,626)
21							
22							
23							
24							
25							
26	WORKING CASH REQUIREMENT	<u>\$ 4,566,682</u>					<u>\$ 187,330</u>

¹All other Operating Expenses are assumed to be paid by the 15th of the month following the receipt of goods and services.

²At proposed rates.

C Schedules

Mohave Water

Line
No.

1 Adjust Depreciation Expense to Reflect Test Year Adjusted Plant:

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Workpapers & Supporting Documents:

\Schedules\2007 Mohave Water Sch. A-F.xls\

\08 Mohave Water\Work Papers\Expenses\A of I - Mohave Water.xls

\Common\Workpapers\Expenses\RegAssets04RateCase.xls

Line No.		[A] Property Tax Expense For Conversion Factor	[B] Property Tax Expense
1	Adjust Property Taxes to Reflect Proposed Revenues:		
2			
3	Adjusted Revenues in year ended Dec. 2007	\$ 5,113,631	\$ 5,113,631
4	Adjusted Revenues in year ended Dec. 2007	5,113,631	5,113,631
5	Proposed Revenues	<u>\$ 5,113,631</u>	<u>\$ 6,057,116</u>
6	Average of three year's of revenue	\$ 5,113,631	<u>\$ 5,428,126</u>
7	Average of three year's of revenue, times 2	\$10,227,262	\$10,856,252
8	Add:		
9	Construction Work in Progress at 10%	49,847	49,847
10	Deduct:		
11	Net Book Value of Transportation Equipment	<u>\$ -</u>	<u>\$ -</u>
12			
13	Full Cash Value	\$ 10,277,109	\$ 10,906,099
14	Assessment Ratio	23%	23%
15	Assessed Value	<u>2,363,735</u>	<u>2,508,403</u>
16	Property Tax Rate	9.384185%	9.384185%
17			
18	Property Tax	221,817	235,393
19	Tax on Parcels	-	-
20			
21	Total Property Tax at Proposed Rates	\$ 221,817	\$ 235,393
22	Property Taxes in the test year	221,817	221,817
23	Adjustment to Revenues and/or Expenses	\$ (0)	\$ 13,576
24			
25			
26			
27			
28	Increase in Property Tax Due to Increase in Revenue Requirement (Line 23 Col [B])		\$ 13,576
29			
30	Increase in Revenue Requirement (From Sch. A1)		\$ 943,485
31			
32	Increase in Property Tax Per Dollar Increase in Revenue (Line 32/Line 34)		1.4389%
33			
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43	Workpapers & Supporting Documents:		
44	\\Schedules\2007 Mohave Water Sch. A-F.xls\		
45	\\Common\Workpapers\Property Taxes\2007 pd in 07-08 AZ Tax Payment .xls		
46	\\08 Mohave Water\Workpapers\Expenses\A of I - Mohave Water.xls		
47			
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Line No.		Test Year Adjusted Results	Adjusted with Rate Increase
1	<u>Calculation of Income Taxes at Proposed Rates</u>		
2			
3			
4	Operating Income Before Inc. Taxes	\$ 298,748	\$ 1,213,002
5	Interest Expense	\$ 297,846	\$ 297,846
6	Arizona Taxable Income	<u>902</u>	<u>915,156</u>
7			
8	Less Arizona Income Tax	<u>\$ 63</u>	<u>\$ 63,768</u>
9	Arizona Income Tax Rate = 6.968%		
10			
11	Federal Income Before Taxes	\$ 902	\$ 915,156
12	Less Arizona Income Taxes	63	63,768
13	Federal Taxable Income	<u>\$ 839</u>	<u>\$ 851,388</u>
14			
15	Federal Income Taxes: 34.000%	<u>\$ 285</u>	<u>\$ 289,472</u>
16			
17			
18	Total Income Tax	<u>\$ 348</u>	<u>\$ 353,240</u>
19			
20	Tax Rate	<u>38.60%</u>	<u>38.60%</u>
21			
22	Effective Income Tax Rates		
23	State	6.968%	6.968%
24	Federal	31.63%	31.63%
25			
26			
27	Adjusted Test Year Income Taxes-Rebuttal	<u>\$ (7,005)</u>	
28	Increase in Income Taxes	<u>7,353</u>	
29			
30	Adjustment to Revenues and/or Expense	<u>\$ 7,353</u>	
31			
32	Test Year Income Taxes, Rejoinder		<u>\$ 348</u>
33	Increase in Income Taxes		<u>352,892</u>
34			
35	Adjustment to Revenues and/or Expense		<u>352,892</u>
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45	Workpapers & Supporting Documents:		
46	\\Schedules\2007 Mohave Water Sch. A-F.xls\		
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Arizona American Water Company - Mohave Water
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-4RJ

Exhibit
 Schedule C-2 Rejoinder
 Page 5
 Witness: Hubbard

Line			
<u>No.</u>			
1	<u>Interest Synchronization with Rate Base</u>		
2			
3	Original Cost Rate Base (Sch. B-1, Ln. 24)	\$10,235,260	
4	Weighted Cost of Debt from Schedule D-1	<u>2.91%</u>	
5	Synchronized Interest Expense	297,846	
6	Test Year Interest Expense-Rebuttal	316,896	
7			
8	Adjusted Test Year Interest Expense	<u>316,896</u>	
9			
10	Increase (decrease) in Interest Expense	<u>\$ (19,050)</u>	
11			
12	Adjustment to Revenues and/or Expense	<u>(19,050)</u>	
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45	Workpapers & Supporting Documents:		
46	\\Schedules\2007 Mohave Water Sch. A-F.xls\		
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Company Rejoinder

Line No.	Description	Percentage of Incremental Gross Revenues
1	Federal Income Taxes	31.63%
2		
3	State Income Taxes	6.97%
4		
5	Property Taxes Effective Rate = 1.4389% One Minus Combined	38.60%
6		61.40%
7	Bad Debt Expense Effective Rate = 1.66% One Minus Combined	0.88%
8		61.40%
9	Total Tax Percentage	<u>1.02%</u>
10		
11	Operating Income % = 100% - Tax Percentage	40.50%
12		
13		
14		
15		
16	1 = Gross Revenue Conversion Factor	
17	Operating Income %	59.50%
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43	Supporting Schedules:	Recap Schedules:
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A Schedules

Paradise

Valley Water

Company Rejoinder

Line No.				
	1 Original Cost Rate Base	\$	37,398,279	
	2			
	3 Adjusted Operating Income		2,039,180	
	4			
	5 Current Rate of Return		5.45%	
	6			
	7 Required Operating Income	\$	3,141,455	
	8			
	9 Required Rate of Return		8.40%	
	10			
	11 Operating Income Deficiency	\$	1,102,275	
	12			
	13 Gross Revenue Conversion Factor		1.6487	
	14			
	15 Increase in Gross Revenue			
	16 Requirement	\$	1,817,267	
	17			
	18 Customer	Present	Proposed	Dollar
	19 Classification	Rates ¹	Rates	Increase
	20			Percent
	21 Residential	\$ 6,373,788		0.00%
	22 Commercial	1,775,919		0.00%
	23 OPA	19,798		0.00%
	24 Private Fire	3,830		0.00%
	25 Sale for Resale	30,632		0.00%
	26			
	27 Total Water Revenues	\$ 8,203,967	\$10,021,233	\$ 1,817,267
	28			22.15%
	29 Other Revenue	16,619	16,619	- 0.00%
	30			
	31 Total Revenue	\$ 8,220,586	\$10,037,853	\$ 1,817,267
	32			22.11%
	33			
	34	¹ Includes Step 2 ACRM in Present Rate Revenue		
	35			
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	40 Supporting Schedules:			
	41 B-1			
	42 C-1			
	43 H-1			
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	50 \Schedules\2007 Paradise Valley Sch. A-F.xls\			

B Schedules

Paradise

Valley Water

		Company Rejoinder				
		[A]	[B]	[C]	[D]	[E]
Line No.		Adjusted End of Test Year	Intentionally Left Blank	Adjust Working Capital	Total Rebuttal Pro Forma Adjustments	Rebuttal Adjusted End of Test Year
1	Gross Utility					
2	Plant in Service	\$ 59,632,504			\$ -	\$ 59,632,504
3		-			-	-
4	Less:					
5						
6	Accumulated Depreciation	12,019,623			-	12,019,623
7						
8	Net Utility Plant					
9	in Service	\$ 47,612,881	\$ -	\$ -	\$ -	\$ 47,612,881
10						
11	Less:					
12	Advances in Aid of					
13	Construction	1,704,269			-	1,704,269
14	Contributions in Aid of	-			-	-
15	Construction - Net	7,250,116			-	7,250,116
16	Imputed Regulatory Advances	-			-	-
17	Imputed Regulatory Contributions	-			-	-
18	Customer Meter Deposits	12,600			-	12,600
19	Deferred Income Taxes	1,600,604			-	1,600,604
20	Investment Tax Credits	-			-	-
21		-			-	-
22		-			-	-
23	Plus:					
24	Deferred Debits	154,761			-	154,761
25	Working capital	236,007		\$(37,782)	(37,782)	198,225
26	Utility Plant Acquisition Adjustment	-			-	-
27						
28	Total	\$ 37,436,060	\$ -	\$(37,782)	\$ (37,782)	\$ 37,398,279

34 ¹ RUCO RB Adjustment #6
 35 is the same dollar amount.

40 Supporting Schedules:

41 B-5
 42 E-1

43 08 AZ MEGA\08 Paradise Valley\Work Papers\Rat
 44 08 AZ MEGA\08 Paradise Valley\Work Papers\Rat
 45 08 AZ MEGA\Common\Workpapers\Corp Rate Ba:
 46 08 AZ MEGA\Common\Workpapers\Corp Rate Ba:

50 \Schedules\2007 Paradise Valley Sch. A-F.xls\

Company Rejoinder

Line		
<u>No.</u>		
1		
2	Working Cash Requirement	\$ 41,544
3	Material and Supplies Inventories	38,726 ¹
4	Prepayments	117,955
5		
6		
7	Total Working Capital Allowance	<u>\$ 198,225</u>
8		
9	Total Adjusted Test Year Working Capital Allowance	\$ 236,007
10		
11	Increase (Decrease in Working Capital Allowance	<u>\$ (37,782)</u>
12		
13	Increase (Decrease in Working Capital Allowance	<u>\$ (37,782)</u>
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43	Supporting Schedules:	Recap Schedules:
44	E-1	B-1
45	Workpapers & Supporting Documents:	
46	¹ Thirteen-month average	
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50	\Schedules\2007 Paradise Valley Sch. A-F.xls\	

PARADISE VALLEY

Company Rejoinder

Line No.		Test Year Adjusted Results [a]	Revenue Lag Days [b]	Expense Lag Days [c]	Net Lag Days [d]	Lead/Lag Factor [e]	Cash Working Capital Required [f]
1	OPERATING EXPENSES						
2	P08 Labor	\$ 703,323	47.97433	12.0000	35.9743	0.0986	\$ 69,319
3	P09 Purchased Water	-	47.97433	86.8700	-	-	-
4	P10 Fuel & Power	693,068	47.97433	32.4200	15.5543	0.0426	29,535
5	P11 Chemicals	185,037	47.97433	28.4700	19.5043	0.0534	9,888
6	P12 Waste Disposal	-	47.97433	30.0000	17.9743	0.0492	-
7	P13 Management Fees	912,659	47.97433	(3.8800)	51.8543	0.1421	129,658
8	P14 Group Insurance	184,827	47.97433	(4.6445)	52.6188	0.1442	26,645
9	P15 Pensions	130,911	47.97433	45.0000	2.9743	0.0081	1,067
10	P17 Insurance Other Than Group	45,435	47.97433	45.0000	2.9743	0.0081	370
11	P18 Customer Accounting	123,742	47.97433	7.4600	40.5143	0.1110	13,735
12	P19 Rents	21,467	47.97433	(10.6818)	58.6561	0.1607	3,450
13	P27-: Depreciation & Amortization		47.97433	-	47.9743	0.1314	-
14	Other Operating Expenses ¹	663,736	47.97433	30.0000	17.9743	0.0492	32,686
15	TAXES						
16	P29 Taxes Other than Income	67,972	47.97433	15.6511	32.3232	0.0886	6,019
17	P29 Property Taxes	282,306	47.97433	212.5000	(164.5257)	(0.4508)	(127,251)
18	P30-: Income Tax ²	1,290,691	47.97433	42.0402	5.9342	0.0163	20,984
19							
20	P56-: Interest	1,088,290	47.97433	106.5200	(58.5457)	(0.1604)	(174,561)
21							
22							
23							
24							
25							
26	WORKING CASH REQUIREMENT	<u>\$ 6,393,466</u>					<u>\$ 41,544</u>

¹All other Operating Expenses are assumed to be paid by the 15th of the month following the receipt of goods and services.

²At proposed rates.

C Schedules

Paradise

Valley Water

Line			
<u>No.</u>			
1	<u>Adjust Depreciation Expense to Reflect Test Year Adjusted Plant:</u>		
2			
3	Depreciation Expense on Test Year UPIS	\$	1,937,180
4	Depreciation Expense on Post-Test Year Plant Additions (Well 17 only)		9,403
5	Amortization of Regulatory Assets		72
6	Amortization of Mummy Mountain Acquisition Costs (Dec 61307)		5,256
7			
8			
9	Less: Amortization of Contributions		382,752
10	Amortization of Imputed Regulatory CIAC		-
11			
12	Total Depreciation Expense	\$	<u>1,569,159</u>
13			
14	Adjusted Test Year Depreciation Expense		<u>1,563,903</u>
15			
16	Increase (Decrease) in Depreciation Expense		<u>5,256</u>
17			
18	Adjustment to Revenues and/or Expenses	\$	<u>5,256</u>
19			
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44			
45	Workpapers & Supporting Documents:		
46	\Schedules\2007 Paradise Valley Sch. A-F.xls\		
47	\08 Paradise Valley\Work Papers\Expenses\A of I - Paradise Valley.xls		
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Line No.		[A] Property Tax Expense For Conversion Factor	[B] Property Tax Expense
1	Adjust Property Taxes to Reflect Proposed Revenues:		
2			
3	Adjusted Revenues in year ended Dec. 2007	\$ 8,220,586	\$ 8,220,586
4	Adjusted Revenues in year ended Dec. 2007	8,220,586	8,220,586
5	Proposed Revenues	<u>\$ 8,220,586</u>	<u>\$ 10,037,853</u>
6	Average of three year's of revenue	\$ 8,220,586	\$ 8,826,341
7	Average of three year's of revenue, times 2	\$16,441,172	\$17,652,683
8	Add:		
9	Construction Work in Progress at 10%	143,802	143,802
10	Deduct:		
11	Net Book Value of Transportation Equipment	\$ -	\$ -
12			
13	Full Cash Value	\$ 16,584,973	\$ 17,796,484
14	Assessment Ratio	23%	23%
15	Assessed Value	3,814,544	4,093,191
16	Property Tax Rate	7.400793%	7.400793%
17			
18	Property Tax	282,306	302,929
19	Tax on Parcels	-	-
20			
21	Total Property Tax at Proposed Rates	\$ 282,306	\$ 302,929
22	Property Taxes in the test year-Rebuttal	282,306	282,306
23	Adjustment to Revenues and/or Expenses	\$ (0)	\$ 20,622
24			
25			
26			
27			
28	Increase in Property Tax Due to Increase in Revenue Requirement (Line 23 Col [B])		\$ 20,622
29			
30	Increase in Revenue Requirement (From Sch. A1)		\$ 1,817,267
31			
32	Increase in Property Tax Per Dollar Increase in Revenue (Line 32/Line 34)		1.1348%
33			
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43	Workpapers & Supporting Documents:		
44	\Schedules\2007 Paradise Valley Sch. A-F.xls\		
45	\Common\Workpapers\Property Taxes\2007 pd in 07-08 AZ Tax Payment .xls		
46	\08 Paradise Valley\Workpapers\Expenses\A of I - Paradise Valley.xls		
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Line No.		Test Year Adjusted Results	Adjusted with Rate Increase
1	<u>Calculation of Income Taxes at Proposed Rates</u>		
2			
3			
4	Operating Income Before Inc. Taxes	\$ 2,636,942	\$ 4,432,147
5	Interest Expense	\$ 1,088,290	\$ 1,088,290
6	Arizona Taxable Income	<u>1,548,653</u>	<u>3,343,857</u>
7			
8	Less Arizona Income Tax	<u>\$ 107,910</u>	<u>\$ 233,000</u>
9	Arizona Income Tax Rate = 6.968%		
10			
11	Federal Income Before Taxes	\$ 1,548,653	\$ 3,343,857
12	Less Arizona Income Taxes	107,910	233,000
13	Federal Taxable Income	<u>\$ 1,440,742</u>	<u>\$ 3,110,857</u>
14			
15	Federal Income Taxes: 34.000%	<u>\$ 489,852</u>	<u>\$ 1,057,691</u>
16			
17			
18	Total Income Tax	<u>\$ 597,763</u>	<u>\$ 1,290,691</u>
19			
20	Tax Rate	<u>38.60%</u>	<u>38.60%</u>
21			
22	Effective Income Tax Rates		
23	State	6.968%	6.968%
24	Federal	31.63%	31.63%
25			
26			
27	Adjusted Test Year Income Taxes-Rebuttal	<u>\$ 599,367</u>	
28	Increase in Income Taxes	<u>(1,604)</u>	
29			
30	Adjustment to Revenues and/or Expense	<u>\$ (1,604)</u>	
31			
32	Test Year Income Taxes, Rejoinder		<u>\$ 597,763</u>
33	Increase in Income Taxes		<u>692,929</u>
34			
35	Adjustment to Revenues and/or Expense		<u>692,929</u>
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45	Workpapers & Supporting Documents:		
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Line			
<u>No.</u>			
1	<u>Interest Synchronization with Rate Base</u>		
2			
3	Original Cost Rate Base (Sch. B-1, Ln. 24)		\$37,398,279
4	Weighted Cost of Debt from Schedule D-1		2.91%
5	Synchronized Interest Expense		1,088,290
6	Test Year Interest Expense	1,089,389	
7			
8	Adjusted Test Year Interest Expense		<u>1,089,389</u>
9			
10	Increase (decrease) in Interest Expense		<u>\$ (1,099)</u>
11			
12	Adjustment to Revenues and/or Expense		<u>(1,099)</u>
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45	Workpapers & Supporting Documents:		
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Company Rejoinder

Line No.	Description	Percentage of Incremental Gross Revenues
1	Federal Income Taxes	31.63%
2		
3	State Income Taxes	6.97%
4		
	Combined	38.60%
5	Property Taxes Effective Rate = 1.1348% One Minus Combined	61.40%
6		0.70%
7	Bad Debt Expense Effective Rate = 0.08% One Minus Combined	61.40%
8		<u>0.05%</u>
9	Total Tax Percentage	39.34%
10		
11	Operating Income % = 100% - Tax Percentage	60.66%
12		
13		
14		
15		
16	1 = Gross Revenue Conversion Factor	
17	Operating Income %	1.6487
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43	Supporting Schedules:	Recap Schedules:
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A Schedules

Sun City

West Water

Company Rejoinder

Line No.					
1	Original Cost Rate Base			\$ 38,382,791	
2					
3	Adjusted Operating Income			736,286	
4					
5	Current Rate of Return			1.92%	
6					
7	Required Operating Income			\$ 3,224,154	
8					
9	Required Rate of Return			8.40%	
10					
11	Operating Income Deficiency			\$ 2,487,869	
12					
13	Gross Revenue Conversion Factor			1.6467	
14					
15	Increase in Gross Revenue Requirement			\$ 4,096,767	
16					
17					
18	Customer	Present	Proposed	Dollar	Percent
19	Classification	Rates ¹	Rates	Increase	Increase
20					
21	Residential	\$ 5,008,780			0.00%
22	Commercial	765,287			0.00%
23	Private Fire	42,798			0.00%
24					
25	Total Water Revenues	<u>\$5,816,865</u>	<u>\$9,913,632</u>	<u>\$ 4,096,767</u>	<u>70.43%</u>
26					
27	Other Revenue	40,401	40,401	-	0.00%
28					
29					
30	Total Revenues	<u>\$5,857,266</u>	<u>\$9,954,033</u>	<u>\$4,096,767</u>	<u>69.94%</u>
31					

¹ Includes Step 2 ACRM in Present Rates.

Supporting Schedules:

- 41 B-1
- 42 C-1
- 43 H-1

B Schedules

Sun City

West Water

Company Rejoinder					
	[A]	[B]	[C]	[D]	[E]
Line No.	Adjusted End of Test Year	Adjust Working Capital	Intentionally Left Blank	Total Rejoinder Pro Forma Adjustments	Rejoinder Adjusted End of Test Year
1	Gross Utility				
2	Plant in Service	\$ 48,951,476		\$ -	\$ 48,951,476
3		-		-	-
4	Less:				
5					
6	Accumulated Depreciation	10,588,406		-	10,588,406
7					
8	Net Utility Plant				
9	in Service	\$ 38,363,070	\$ -	\$ -	\$ 38,363,070
10					
11	Less:				
12	Advances in Aid of				
13	Construction	1,175,373		-	1,175,373
14	Contributions in Aid of	-		-	-
15	Construction - Net	19,491		-	19,491
16	Imputed Regulatory Advances	-		-	-
17	Imputed Regulatory Contributions	392,368		-	392,368
18	Customer Meter Deposits	1,225		-	1,225
19	Deferred Income Taxes	(1,326,577)		-	(1,326,577)
20	Investment Tax Credits	-		-	-
21		-		-	-
22		-		-	-
23	Plus:				
24	Deferred Debits	114,798		-	114,798
25	Working capital	158,536	8,269	8,269	166,804
26	Utility Plant Acquisition Adjustment	-		-	-
27					
28	Total	\$ 38,374,522	\$ 8,269	\$ -	\$ 8,269
29					
30					
31	Error in Original Filing - No difference in RB				
32	Imputed Regulatory Advances				
33					
34					
35	¹ RUCO RB Adjustment #5 is				
36	the same dollar amount.				
37					
38	Supporting Schedules:				
39	B-5				
40	E-1				
41	08 AZ MEGA\08 Sun City West Water\Work Pap				
42	08 AZ MEGA\08 Sun City West Water\Work Pap				
43	08 AZ MEGA\Common\Workpapers\Corp Rate B				
44	08 AZ MEGA\Common\Workpapers\Corp Rate B				

Company Rejoinder

Line		
<u>No.</u>		
1		
2	Working Cash Requirement	\$ 85,389
3	Material and Supplies Inventories	56,510 ¹
4	Prepayments	24,906
5		
6		
7	Total Working Capital Allowance	<u>\$ 166,804</u>
8		
9	Total Adjusted Test Year Working Capital Allowance	\$ 158,536
10		
11	Increase (Decrease in Working Capital Allowance	<u>\$ 8,269</u>
12		
13	Increase (Decrease in Working Capital Allowance	<u>\$ 8,269</u>
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43	Supporting Schedules:	Recap Schedules:
44	E-1	B-1
45	Workpapers & Supporting Documents:	
46	¹ Thirteen-month average	
47		
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50	\Schedules\2007 Sun City West Water Sch. A-F.xls\	

SUN CITY WEST WATER

Company Rejoinder

Line No.		Test Year Adjusted Results	Revenue Lag Days	Expense Lag Days	Net Lag Days	Lead/Lag Factor	Cash Working Capital Required
1	OPERATING EXPENSES						
2	P08 Labor	\$ 689,649	47.56935	12.0000	35.5694	0.0975	\$ 67,207
3	P09 Purchased Water	(2,690)	47.56935	86.8700	(39.3006)	(0.1077)	290
4	P10 Fuel & Power	830,074	47.56935	32.4200	15.1494	0.0415	34,452
5	P11 Chemicals	227,889	47.56935	28.4700	19.0994	0.0523	11,925
6	P12 Waste disposal	4,704	47.56935	30.0000	17.5694	0.0481	226
7	P13 Management Fees	987,868	47.56935	(3.8800)	51.4494	0.1410	139,247
8	P14 Group Insurance	191,120	47.56935	(4.6445)	52.2139	0.1431	27,340
9	P15 Pensions	137,699	47.56935	45.0000	2.5694	0.0070	969
10	P17 Insurance Other Than Group	58,622	47.56935	45.0000	2.5694	0.0070	413
11	P18 Customer Accounting	133,476	47.56935	7.4600	40.1094	0.1099	14,667
12	P19 Rents	14,331	47.56935	(10.6818)	58.2512	0.1596	2,287
13	P27-2 Depreciation & Amortization		47.56935	-	47.5694	0.1303	-
14	Other Operating Expenses ¹	510,464	47.56935	30.0000	17.5694	0.0481	24,571
15	TAXES						
16	P29 Taxes Other than Income	65,832	47.56935	15.6511	31.9183	0.0874	5,757
17	P29 Property Taxes	185,086	47.56935	212.5000	(164.9306)	(0.4519)	(83,634)
18	P30-3 Income Tax ²	1,324,669	47.56935	42.0402	5.5292	0.0151	20,067
19							
20	P56-6 Interest	1,116,939	47.56935	106.5200	(58.9506)	(0.1615)	(180,395)
21							
22							
23							
24							
25							
26							
27	WORKING CASH REQUIREMENT	<u>\$ 6,475,733</u>					<u>\$ 85,389</u>

¹All other Operating Expenses are assumed to be paid by the 15th of the month following the receipt of goods and services.

²At proposed rates.

C Schedules

Sun City

West Water

Arizona American Water Company - Sun City West Water
 Test Year Ended December 31, 2007
 Income Statement Pro Forma Adjustments

Exhibit
 Schedule C-2 Rejoinder
 Page 1
 Witness: Hubbard

Line No.	Company Rejoinder										Rejoinder Adjusted with Rate Increase
	[A] Rebuttal Test Year Adjusted Results	[B] ADJ SLH-1RJ Depreciation Expense	[C] ADJ SLH-2RJ Property Tax Expense	[D] ADJ SLH-3RJ Income Tax Expense	[E] ADJ SLH-4RJ Interest Synchronization	[F] Total Rejoinder Pro Forma Adjustments	[G] Rejoinder Test Year Adjusted Results	[H] Rejoinder Proposed Rate Increase	[I] Rejoinder Adjusted with Rate Increase		
1	Revenues										
2	P02 Water Revenues	\$ 5,816,865									\$ 5,816,865
3	P04 Other Revenues	40,401									40,401
4											
5		\$ 5,857,266	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 4,096,767	\$ 4,096,767	\$ 9,954,033
6	Operating Expenses										
7	P08 Labor	\$ 689,649									\$ 689,649
8	P09 Purchased Water	(2,690)									(2,690)
9	P10 Fuel & Power	830,074									830,074
10	P11 Chemicals	227,889									227,889
11	P12 Waste Disposal	4,704									4,704
12	P13 Management Fees	987,868									987,868
13	P14 Group Insurance	191,120									191,120
14	P15 Pensions	137,699									137,699
15	P16 Regulatory Expense	25,543									25,543
16	P17 Insurance Other Than Group	58,622									58,622
17	P18 Customer Accounting	133,476									133,476
18	P19 Rents	14,331									14,331
19	P20 General Office Expense	57,226									57,226
20	P21 Miscellaneous	227,716							1,767		229,483
21	P25 Maintenance Expense	199,979									199,979
22	P27-2 Depreciation & Amortization	1,326,147									1,326,147
23	P29 General Taxes-Property Taxes	185,086		(0)					43,171		228,257
24	P29 General Taxes-Other	65,832									65,832
25	P30-3 Income Taxes	(239,199)		(93)					1,563,961		1,324,669
26											
27	Total Operating Expenses	\$ 5,121,073	\$ -	\$ (93)	\$ -	\$ -	\$ (93)	\$ 5,120,980	\$ 1,608,898	\$ 6,729,878	
28	Utility Operating Income	\$ 736,193	\$ -	\$ -	\$ -	\$ -	\$ 93	\$ 736,286	\$ 2,487,869	\$ 3,224,154	
29	Other Income & Deductions										
30	P39-4 Other Income & Deductions					241					
31	P56-6 Interest Expense	1,116,699									1,116,699
32	P48-5 Other Expense	(372)									(372)
33	P43 Gain/Loss Sale of Fixed Assets	90,780									90,780
34	Total Other Income & Deductions	\$ (1,025,547)	\$ -	\$ -	\$ -	\$ (241)	\$ (241)	\$ (1,025,787)	\$ -	\$ -	(1,025,787)
35	Net Profit (Loss)	\$ (289,354)	\$ -	\$ -	\$ -	\$ (241)	\$ (148)	\$ (289,501)	\$ 2,487,869	\$ 2,198,367	
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43	Supporting Schedules:										
44											
45	Workpapers & Supporting Documents:										
46	ISchedules\2007 Sun City West Water Sch. A-F.xls										
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Supporting Schedules:
 Workpapers & Supporting Documents:
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45 Workpapers & Supporting Documents:
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Arizona American Water Company - Sun City West Water
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-2RJ

Exhibit
 Schedule C-2 Rejoinder
 Page 3
 Witness: Hubbard

Line No.		[A] Property Tax Expense For Conversion Factor	[B] Property Tax Expense
1	Adjust Property Taxes to Reflect Proposed Revenues:		
2			
3	Adjusted Revenues in year ended Dec. 2007	\$ 5,857,266	\$ 5,857,266
4	Adjusted Revenues in year ended Dec. 2007	5,857,266	5,857,266
5	Proposed Revenues	<u>\$ 5,857,266</u>	<u>\$ 9,954,033</u>
6	Average of three year's of revenue	<u>\$ 5,857,266</u>	<u>\$ 7,222,855</u>
7	Average of three year's of revenue, times 2	\$11,714,532	\$14,445,710
8	Add:		
9	Construction Work in Progress at 10%	(5,086)	(5,086)
10	Deduct:		
11	Net Book Value of Transportation Equipment	<u>\$ -</u>	<u>\$ -</u>
12			
13	Full Cash Value	\$ 11,709,446	\$ 14,440,624
14	Assessment Ratio	<u>23%</u>	<u>23%</u>
15	Assessed Value	2,693,173	3,321,343
16	Property Tax Rate	6.872427%	6.872427%
17			
18	Property Tax	185,086	228,257
19	Tax on Parcels	-	-
20			
21	Total Property Tax at Proposed Rates	<u>\$ 185,086</u>	<u>\$ 228,257</u>
22	Property Taxes in the test year-Rebuttal	<u>185,086</u>	<u>185,086</u>
23	Adjustment to Revenues and/or Expenses	<u>\$ (0)</u>	<u>\$ 43,171</u>
24			
25			
26			
27			
28	Increase in Property Tax Due to Increase in Revenue Requirement (Line 23 Col [B])		\$ 43,171
29			
30	Increase in Revenue Requirement (From Sch. A1)		\$ 4,096,767
31			
32	Increase in Property Tax Per Dollar Increase in Revenue (Line 32/Line 34)		1.0538%
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43	Workpapers & Supporting Documents:		
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45	\\Common\Workpapers\Property Taxes\2007 pd in 07-08 AZ Tax Payment .xls		
46	\\08 Sun City West Water\Workpapers\Expenses\A of I - Sun City West Water.xls		
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Arizona American Water Company - Sun City West Water
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-3RJ

Exhibit
 Schedule C-2 Rejoinder
 Page 4
 Witness: Hubbard

Line No.		Test Year Adjusted Results	Adjusted with Rate Increase
1	<u>Calculation of Income Taxes at Proposed Rates</u>		
2			
3			
4	Operating Income Before Inc. Taxes	\$ 496,994	\$ 4,548,823
5	Interest Expense	\$ 1,116,939	\$ 1,116,939
6	Arizona Taxable Income	<u>(619,945)</u>	<u>3,431,884</u>
7			
8	Less Arizona Income Tax	\$ (43,198)	\$ 239,134
9	Arizona Income Tax Rate = 6.968%		
10			
11	Federal Income Before Taxes	\$ (619,945)	\$ 3,431,884
12	Less Arizona Income Taxes	<u>(43,198)</u>	<u>239,134</u>
13	Federal Taxable Income	<u>\$ (576,747)</u>	<u>\$ 3,192,750</u>
14			
15	Federal Income Taxes: 34.000%	<u>\$ (196,094)</u>	<u>\$ 1,085,535</u>
16			
17			
18	Total Income Tax	<u>\$ (239,292)</u>	<u>\$ 1,324,669</u>
19			
20	Tax Rate	<u>38.60%</u>	<u>38.60%</u>
21			
22	Effective Income Tax Rates		
23	State	6.968%	6.968%
24	Federal	31.63%	31.63%
25			
26			
27	Adjusted Test Year Income Taxes-Rebuttal	<u>\$ (239,199)</u>	
28	Increase in Income Taxes	<u>(93)</u>	
29			
30	Adjustment to Revenues and/or Expense	<u>\$ (93)</u>	
31			
32	Test Year Income Taxes, Rejoinder		\$ (239,292)
33	Increase in Income Taxes		<u>1,563,961</u>
34			
35	Adjustment to Revenues and/or Expense		<u>1,563,961</u>
36			
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45	Workpapers & Supporting Documents:		
46	\\Schedules\2007 Sun City West Water Sch. A-F.xls\		
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Arizona American Water Company - Sun City West Water
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-4RJ

Exhibit
 Schedule C-2 Rejoinder
 Page 5
 Witness: Hubbard

Line			
No.			
1	<u>Interest Synchronization with Rate Base</u>		
2			
3	Original Cost Rate Base (Sch. B-1, Ln. 24)		\$38,382,791
4	Weighted Cost of Debt from Schedule D-1		2.91%
5	Synchronized Interest Expense		<u>1,116,939</u>
6	Test Year Interest Expense-Rebuttal	1,116,699	
7			
8	Adjusted Test Year Interest Expense	<u>1,116,699</u>	
9			
10	Increase (decrease) in Interest Expense		<u>\$ 241</u>
11			
12	Adjustment to Revenues and/or Expense		<u>241</u>
13			
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45	Workpapers & Supporting Documents:		
46	\Schedules\2007 Sun City West Water Sch. A-F.xls\		
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A Schedules

Tubac Water

Company Rejoinder

Line No.					
1	Original Cost Rate Base			\$	1,457,349
2					
3	Adjusted Operating Income				(40,106)
4					
5	Current Rate of Return				-2.75%
6					
7	Required Operating Income			\$	122,417
8					
9	Required Rate of Return				8.40%
10					
11	Operating Income Deficiency			\$	162,524
12					
13	Gross Revenue Conversion Factor				1.6648
14					
15	Increase in Gross Revenue Requirement			\$	270,575
16					
17					
18	Customer Classification	Present Rates	Proposed Rates	Dollar Increase	Percent Increase
19					
20					
21	Residential	\$320,770			0.00%
22	Commercial	102,289			0.00%
23					
24	Total Water Revenues	\$423,059	\$693,634	\$ 270,575	63.96%
25					
26	Other Revenue	3,839	3,839	-	0.00%
27					
28	Total Water Revenues	\$426,898	\$697,473	\$270,575	63.38%
29					
30					
31					
32					
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40	Supporting Schedules:				
41	B-1				
42	C-1				
43	H-1				
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49					
50	\\Schedules\2007 Tubac Water Sch. A-F.xls\				

B Schedules

Tubac Water

		Company Rejoinder			
		[A]	[B]	[C]	[D]
Line No.		Adjusted End of Test Year	Adjust Working Capital	Total Rejoinder Pro Forma Adjustments	Rejoinder Adjusted End of Test Year
1	Gross Utility				
2	Plant in Service	\$ 3,423,384		\$ -	\$ 3,423,384
3					
4	Less:				
5					
6	Accumulated Depreciation	939,364		-	939,364
7					
8	Net Utility Plant				
9	in Service	\$ 2,484,020	\$ -	\$ -	\$ 2,484,020
10					
11	Less:				
12	Advances in Aid of				
13	Construction	1,042,125		-	1,042,125
14	Contributions in Aid of	-		-	-
15	Construction - Net	178		-	178
16	Imputed Regulatory Advances	-		-	-
17	Imputed Regulatory Contributions	58,023		-	58,023
18	Customer Meter Deposits	540		-	540
19	Deferred Income Taxes	(46,088)		-	(46,088)
20	Investment Tax Credits	-		-	-
21					
22					
23	Plus:				
24	Deferred Debits	3,381		-	3,381
25	Working capital	24,726	-	-	24,726
26	Utility Plant Acquisition Adjustment	-		-	-
27					
28	Total	\$ 1,457,349	\$ -	\$ -	\$ 1,457,349
29					
30					
31					
32					
33	¹ RUCO RB Adjustment #5				
34	is the same dollar amount.				
35					
36					
37					
38	Supporting Schedules:				
39	B-5				
40	E-1				
41	08 AZ MEGA\08 Tubac\Work Papers\Rate Base\				
42	08 AZ MEGA\08 Tubac\Work Papers\Rate Base\				
43	08 AZ MEGA\Common\Workpapers\Corp Rate B:				
44	08 AZ MEGA\Common\Workpapers\Corp Rate B:				
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50	\\Schedules\2007 Tubac Water Sch. A-F.xls\				

Company Rejoinder

Line		
<u>No.</u>		
1		
2	Working Cash Requirement	\$ 21,683
3	Material and Supplies Inventories	1,445 ¹
4	Prepayments	1,598
5		
6		
7	Total Working Capital Allowance	<u>\$ 24,726</u>
8		
9	Total Adjusted Test Year Working Capital Allowance	\$ 24,726
10		
11	Increase (Decrease in Working Capital Allowance	<u>\$ -</u>
12		
13	Increase (Decrease in Working Capital Allowance	<u>\$ -</u>
14		
15		
16		
17		
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43	Supporting Schedules:	Recap Schedules:
44	E-1	B-1
45	Workpapers & Supporting Documents:	
46	¹ Thirteen-month average	
47		
48		
49		
50	\Schedules\2007 Tubac Water Sch. A-F.xls\	

TUBAC WATER

Company Rejoinder						
Line No.	Test Year Adjusted Results	Revenue Lag Days	Expense Lag Days	Net Lag Days	Lead/Lag Factor	Cash Working Capital Required
1	OPERATING EXPENSES					
2	\$ 130,440	49.65788	12.0000	37.6579	0.1032	\$ 13,458
3	-	49.65788	86.8700	-	-	-
4	25,631	49.65788	32.4200	17.2379	0.0472	1,210
5	2,190	49.65788	28.4700	21.1879	0.0580	127
6	-	49.65788	30.0000	19.6579	0.0539	-
7	86,131	49.65788	(3.8800)	53.5379	0.1467	12,634
8	24,921	49.65788	(4.6445)	54.3024	0.1488	3,708
9	28,546	49.65788	45.0000	4.6579	0.0128	364
10	5,049	49.65788	45.0000	4.6579	0.0128	64
11	11,644	49.65788	7.4600	42.1979	0.1156	1,346
12	4,146	49.65788	(10.6818)	60.3397	0.1653	685
13	-	49.65788	-	49.6579	0.1360	-
14	81,073	49.65788	30.0000	19.6579	0.0539	4,366
15	TAXES					
16	11,078	49.65788	15.6511	34.0068	0.0932	1,032
17	26,350	49.65788	212.5000	(162.8421)	(0.4461)	(11,756)
18	50,296	49.65788	42.0402	7.6177	0.0209	1,050
19						
20	42,409	49.65788	106.5200	(56.8621)	(0.1558)	(6,607)
21						
22						
23						
24						
25						
26	WORKING CASH REQUIREMENT	<u>\$ 529,904</u>				<u>\$ 21,683</u>

¹All other Operating Expenses are assumed to be paid by the 15th of the month following the receipt of goods and services.

²At proposed rates.

C Schedules

Tubac Water

Arizona American Water Company - Tubac Water
 Test Year Ended December 31, 2007
 Income Statement Pro Forma Adjustments

Exhibit
 Schedule C-2
 Page 1
 Witness: Hubbard

Line No.	Company Rejoinder										
	(A) Rebuttal Test Year Adjusted Results	(B) ADJ SLH-1RJ Depreciation Expense	(C) ADJ SLH-2RJ Property Tax Expense	(D) ADJ SLH-3RJ Income Tax Expense	(E) ADJ SLH-4RJ Interest Synchronization	(F) Total Rejoinder Pro Forma Adjustments	(G) Rejoinder Test Year Adjusted Results	(H) Rejoinder Proposed Rate Increase	(I) Rejoinder Adjusted with Rate Increase		
1											
2	P02	Water Revenues									
3	P04	Other Revenues									
4											
5											
6		Operating Expenses									
7	P08	Labor									
8	P09	Purchased Water									
9	P10	Fuel & Power									
10	P11	Chemicals									
11	P12	Waste Disposal									
12	P13	Management Fees									
13	P14	Group Insurance									
14	P15	Pensions									
15	P16	Regulatory Expense									
16	P17	Insurance Other Than Group									
17	P18	Customer Accounting									
18	P19	Rentals									
19	P20	General Office Expense									
20	P21	Miscellaneous									
21	P25	Maintenance Expense									
22	P27-2	Depreciation & Amortization									
23	P29	General Taxes-Property									
24	P29	General Taxes-Other									
25	P30-3	Income Taxes									
26											
27		Total Operating Expenses									
28		Utility Operating Income									
29		Other Income & Deductions									
30	P39-4	Other Income & Deductions									
31	P56-6	Interest Expense									
32	P48-5	Other Expense									
33	P43	Gain/Loss Sale of Fixed Assets									
34		Total Other Income & Deductions									
35		Net Profit (Loss)									
36											
37											
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44											
45		Supporting Schedules:									
46		Workpapers & Supporting Documents:									
47		ISchedules\2007 Tubac Water Sch. A-F.xls									
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Supporting Schedules:

Workpapers & Supporting Documents:
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45 Workpapers & Supporting Documents:

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Arizona American Water Company - Tubac Water
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-2RJ

Exhibit
 Schedule C-2 Rejoinder
 Page 3
 Witness: Hubbard

Line No.		[A] Property Tax Expense For Conversion Factor	[B] Property Tax Expense
1	Adjust Property Taxes to Reflect Proposed Revenues:		
2			
3	Adjusted Revenues in year ended Dec. 2007	\$ 426,900	\$ 426,900
4	Adjusted Revenues in year ended Dec. 2007	426,900	426,900
5	Proposed Revenues	<u>\$ 426,900</u>	<u>\$ 697,475</u>
6	Average of three year's of revenue	<u>\$ 426,900</u>	<u>\$ 517,092</u>
7	Average of three year's of revenue, times 2	\$853,800	\$1,034,183
8	Add:		
9	Construction Work in Progress at 10%	47,960	47,960
10	Deduct:		
11	Net Book Value of Transportation Equipment	<u>\$ -</u>	<u>\$ -</u>
12			
13	Full Cash Value	\$ 901,760	\$ 1,082,143
14	Assessment Ratio	23%	23%
15	Assessed Value	<u>207,405</u>	<u>248,893</u>
16	Property Tax Rate	12.704496%	12.704496%
17			
18	Property Tax	26,350	31,621
19	Tax on Parcels	-	-
20			
21	Total Property Tax at Proposed Rates	<u>\$ 26,350</u>	<u>\$ 31,621</u>
22	Property Taxes in the test year-Rebuttal	<u>26,350</u>	<u>26,350</u>
23	Adjustment to Revenues and/or Expenses	<u>\$ -</u>	<u>\$ 5,271</u>
24			
25			
26			
27			
28	Increase in Property Tax Due to Increase in Revenue Requirement (Line 23 Col [B])		\$ 5,271
29			
30	Increase in Revenue Requirement (From Sch. A1)		\$ 270,575
31			
32	Increase in Property Tax Per Dollar Increase in Revenue (Line 32/Line 34)		1.9480%
33			
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43	Workpapers & Supporting Documents:		
44	\Schedules\2007 Tubac Water Sch. A-F.xls\		
45	\Common\Workpapers\Property Taxes\2007 pd in 07-08 AZ Tax Payment .xls		
46	\08 Tubac Water\Workpapers\Expenses\A of I - Tubac Water.xls		
47			
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Line No.		Test Year Adjusted Results	Adjusted with Rate Increase
1	<u>Calculation of Income Taxes at Proposed Rates</u>		
2			
3			
4	Operating Income Before Inc. Taxes	\$ (91,978)	\$ 172,713
5	Interest Expense	\$ 42,409	\$ 42,409
6	Arizona Taxable Income	<u>(134,387)</u>	<u>130,305</u>
7			
8	Less Arizona Income Tax	<u>\$ (9,364)</u>	<u>\$ 9,080</u>
9	Arizona Income Tax Rate = 6.968%		
10			
11	Federal Income Before Taxes	\$ (134,387)	\$ 130,305
12	Less Arizona Income Taxes	(9,364)	9,080
13	Federal Taxable Income	<u>\$ (125,023)</u>	<u>\$ 121,225</u>
14			
15	Federal Income Taxes: 34.000%	<u>\$ (42,508)</u>	<u>\$ 41,216</u>
16			
17			
18	Total Income Tax	<u>\$ (51,872)</u>	<u>\$ 50,296</u>
19			
20	Tax Rate	<u>38.60%</u>	<u>38.60%</u>
21			
22	Effective Income Tax Rates		
23	State	6.968%	6.968%
24	Federal	31.63%	31.63%
25			
26			
27	Adjusted Test Year Income Taxes-Rebuttal	<u>\$ (51,872)</u>	
28	Increase in Income Taxes	<u>-</u>	
29			
30	Adjustment to Revenues and/or Expense	<u>\$ -</u>	
31			
32	Test Year Income Taxes, Rejoinder		<u>\$ (51,872)</u>
33	Increase in Income Taxes		<u>102,168</u>
34			
35	Adjustment to Revenues and/or Expense		<u>102,168</u>
36			
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45	Workpapers & Supporting Documents:		
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Arizona American Water Company - Tubac Water
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-4RJ

Exhibit
 Schedule C-2 Rejoinder
 Page 5
 Witness: Hubbard

Line			
<u>No.</u>			
1	Interest Synchronization with Rate Base		
2			
3	Original Cost Rate Base (Sch. B-1, Ln. 24)		\$1,457,349
4	Weighted Cost of Debt from Schedule D-1		<u>2.91%</u>
5	Synchronized Interest Expense		42,409
6	Test Year Interest Expense-Rebuttal	42,409	
7			
8	Adjusted Test Year Interest Expense-Rebuttal	<u>42,409</u>	<u>42,409</u>
9			
10	Increase (decrease) in Interest Expense		<u>\$ -</u>
11			
12	Adjustment to Revenues and/or Expense		<u>-</u>
13			
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45	Workpapers & Supporting Documents:		
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Company Rejoinder

Line No.	Description	Percentage of Incremental Gross Revenues
1	Federal Income Taxes	31.63%
2		
3	State Income Taxes	6.97%
4		
5	Property Taxes Effective Rate = 1.9480% One Minus Combined	38.60%
6		61.40%
7	Bad Debt Expense Effective Rate = 0.23% One Minus Combined	1.20%
8		<u>0.14%</u>
9	Total Tax Percentage	39.93%
10		
11	Operating Income % = 100% - Tax Percentage	60.07%
12		
13		
14		
15		
16	1 = Gross Revenue Conversion Factor	
17	Operating Income %	1.6648
18		
19		
20		
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22		
23		
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26		
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28		
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43	Supporting Schedules:	Recap Schedules:
44		A-1
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A Schedules

Mohave

Wastewater

Company Rejoinder

Line
 No.

1	Original Cost Rate Base		\$	5,134,633
2				
3	Adjusted Operating Income			116,410
4				
5	Current Rate of Return			2.27%
6				
7	Required Operating Income		\$	431,309
8				
9	Required Rate of Return			8.40%
10				
11	Operating Income Deficiency		\$	314,899
12				
13	Gross Revenue Conversion Factor			1.6672
14				
15	Increase in Gross Revenue			
16	Requirement		\$	525,014
17				
18	Customer	Present	Proposed	Dollar
19	<u>Classification</u>	<u>Rates</u>	<u>Rates</u>	<u>Increase</u>
20				<u>Percent</u>
21	Residential	\$ 722,719		0.00%
22	Commercial	19,460		0.00%
23	OPA	7,745		0.00%
24	Effluent Sales	41,299		0.00%
25				
26	Total of Water Revenues	\$ 791,223	\$ 1,316,236	\$ 525,014
27				66.35%
28	Other Revenue	4,882	4,882	-
29				0.00%
30	Total Revenue	\$ 796,105	\$ 1,321,118	\$ 525,014
31				65.95%
32				
33				
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40	Supporting Schedules:			
41	B-1			
42	C-1			
43	H-1			
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B Schedules

Mohave

Wastewater

Line No.	Company Rejoinder				
	[A]	[B]	[C]	[D]	[E]
	Adjusted End of Test Year		Adjust Working Capital	Total Rejoinder Pro Forma Adjustments	Rejoinder Adjusted End of Test Year
1					
2					
3					
4					
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11					
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Company Rejoinder

Line		
<u>No.</u>		
1		
2	Working Cash Requirement	\$ (3,481)
3	Material and Supplies Inventories	341 ¹
4	Prepayments	3,661
5		
6		
7	Total Working Capital Allowance	<u>\$ 521</u>
8		
9	Total Adjusted Test Year Working Capital Allowance	\$ 4,427
10		
11	Increase (Decrease in Working Capital Allowance	<u>\$ (3,906)</u>
12		
13	Increase (Decrease in Working Capital Allowance	<u>\$ (3,906)</u>
14		
15		
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43	Supporting Schedules:	Recap Schedules:
44	E-1	B-1
45	Workpapers & Supporting Documents:	
46	¹ Thirteen-month average	
47		
48		
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50	\Schedules\2007 Mohave Wastewater Sch. A-F.xls\	

MOHAVE WASTEWATER

Company Rejoinder

Line No.	Test Year Adjusted Results	Revenue Lag Days	Expense Lag Days	Net Lag Days	Lead/Lag Factor	Cash Working Capital Required
1	OPERATING EXPENSES					
2	\$ 107,318	46.42606	12.0000	34.4261	0.0943	\$ 10,122
3	73,650	46.42606	31.6979	14.7282	0.0404	2,972
4	9,214	46.42606	33.3950	13.0311	0.0357	329
5	(13,733)	46.42606	30.0000	16.4261	0.0450	(618)
6	122,176	46.42606	(3.8800)	50.3061	0.1378	16,839
7	24,046	46.42606	(4.6445)	51.0706	0.1399	3,364
8	18,447	46.42606	45.0000	1.4261	0.0039	72
9	7,294	46.42606	45.0000	1.4261	0.0039	28
10	16,497	46.42606	7.4600	38.9661	0.1068	1,761
11	1,613	46.42606	(10.6818)	57.1079	0.1565	252
12	P27-: Depreciation & Amortization					
		46.42606	-	46.4261	0.1272	-
13	Other Operating Expenses ¹					
	44,945	46.42606	30.0000	16.4261	0.0450	2,023
14	TAXES					
15	P29 Taxes Other than Income					
	9,778	46.42606	15.6511	30.7750	0.0843	824
16	P29 Property Taxes					
	41,714	46.42606	212.5000	(166.0739)	(0.4550)	(18,980)
17	P30-: Income Tax ²					
	177,207	46.42606	42.0402	4.3859	0.0120	2,129
18						
19	P56-: Interest					
	149,418	46.42606	106.5200	(60.0939)	(0.1646)	(24,600)
20						
21						
22						
23						
24						
25						
26	WORKING CASH REQUIREMENT	\$ 789,583				(3,481)

¹All other Operating Expenses are assumed to be paid by the 15th of the month following the receipt of goods and services.

²At proposed rates.

C Schedules

Mohave

Wastewater

Line

No.

1 Adjust Depreciation Expense to Reflect Test Year Adjusted Plant:

2

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45 Workpapers & Supporting Documents:

46 \Schedules\2007 Mohave Wastewater Sch. A-F.xls\

47 \08 Mohave Sewer\Workpapers\Expense\A of I - Mohave Wastewater.xls

48 \08 Mohave Sewer\Workpapers\Rate Base\Imputed AIAC and CIAC.xls

49

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Line No.	[A] Property Tax Expense For Conversion Factor	[B] Property Tax Expense
1	<u>Adjust Property Taxes to Reflect Proposed Revenues:</u>	
2		
3	Adjusted Revenues in year ended Dec. 2007	
4	Adjusted Revenues in year ended Dec. 2007	
5	Proposed Revenues	
6	Average of three year's of revenue	
7	Average of three year's of revenue, times 2	
8	Add:	
9	Construction Work in Progress at 10%	
10	Deduct:	
11	Net Book Value of Transportation Equipment	
12		
13	Full Cash Value	
14	Assessment Ratio	
15	Assessed Value	
16	Property Tax Rate	
17		
18	Property Tax	
19	Tax on Parcels	
20		
21	Total Property Tax at Proposed Rates	
22	Property Taxes in the test year-Rebuttal	
23	Adjustment to Revenues and/or Expenses	
24		
25		
26		
27		
28	Increase in Property Tax Due to Increase in Revenue Requirement (Line 32 Col [B])	\$ 8,290
29		
30	Increase in Revenue Requirement (From Sch. A1)	\$ 525,014
31		
32	Increase in Property Tax Per Dollar Increase in Revenue (Line 32/Line 34)	1.5790%
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43	Workpapers & Supporting Documents:	
44	\Schedules\2007 Mohave Wastewater Sch. A-F.xls\	
45	\Common\Workpapers\Property Taxes\2007 pd in 07-08 AZ Tax Payment .xls	
46		
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Arizona American Water Company - Mohave Wastewater
 Test Year Ended December 31, 2007
 Income Statement Adjustment SLH-3RJ

Exhibit
 Schedule C-2 Rejoinder
 Page 4
 Witness: Hubbard

Line No.		[A] Test Year Adjusted Results	[B] Adjusted with Rate Increase
1	<u>Calculation of Income Taxes at Proposed Rates</u>		
2			
3			
4	Operating Income Before Inc. Taxes	\$ 95,660	\$ 608,516
5	Interest Expense	\$ 149,418	\$ 149,418
6	Arizona Taxable Income	<u>(53,758)</u>	<u>459,098</u>
7			
8	Less Arizona Income Tax	\$ (3,746)	\$ 31,990
9	Arizona Income Tax Rate = 6.968%		
10			
11	Federal Income Before Taxes	\$ (53,758)	\$ 459,098
12	Less Arizona Income Taxes	(3,746)	31,990
13	Federal Taxable Income	<u>(50,012)</u>	<u>\$ 427,108</u>
14			
15	Federal Income Taxes: 34.000%	\$ (17,004)	\$ 145,217
16			
17			
18	Total Income Tax	<u>\$ (20,750)</u>	<u>\$ 177,207</u>
19			
20	Tax Rate	<u>38.60%</u>	<u>38.60%</u>
21			
22	Effective Income Tax Rates		
23	State	6.968%	6.968%
24	Federal	31.63%	31.63%
25			
26			
27	Adjusted Test Year Income Taxes-Rebuttal	<u>\$ (20,794)</u>	
28	Increase in Income Taxes	<u>44</u>	
29			
30	Adjustment to Revenues and/or Expense	<u>\$ 44</u>	
31			
32	Test Year Income Taxes, Rejoinder		\$ (20,750)
33	Increase in Income Taxes		197,957
34			
35	Adjustment to Revenues and/or Expense		<u>197,957</u>
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45	Workpapers & Supporting Documents:		
46	\\Schedules\2007 Mohave Wastewater Sch. A-F.xls\		
47			
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Arizona American Water Company - Mohave Wastewater
Test Year Ended December 31, 2007
Income Statement Adjustment SLH-4RJ

Exhibit
Schedule C-2 Rejoinder
Page 5
Witness: Hubbard

Line No.		
1	Interest Synchronization with Rate Base	
2		
3	Original Cost Rate Base (Sch. B-1, Ln. 24)	\$5,134,633
4	Weighted Cost of Debt from Schedule D-1	<u>2.91%</u>
5	Synchronized Interest Expense	<u>149,418</u>
6	Test Year Interest Expense-Rebuttal	<u>149,531</u>
7	Increase (decrease) in Interest Expense	<u>\$ (114)</u>
8		
9	Adjustment to Revenues and/or Expense	<u>(114)</u>
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45	Workpapers & Supporting Documents:	
46	\Schedules\2007 Mohave Wastewater Sch. A-F.xls\	
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Company Rejoinder

Line No.	Description	Percentage of Incremental Gross Revenues
1	Federal Income Taxes	31.63%
2		
3	State Income Taxes	6.97%
4		
	Combined	38.60%
5	Property Taxes Effective Rate = 1.5790% One Minus Combined	61.40%
6		0.97%
7	Bad Debt Expense Effective Rate = 0.74% One Minus Combined	61.40%
8		<u>0.45%</u>
9	Total Tax Percentage	40.02%
10		
11	Operating Income % = 100% - Tax Percentage	59.98%
12		
13		
14		
15		
16	1 = Gross Revenue Conversion Factor	
17	Operating Income %	1.6672
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43	Supporting Schedules:	Recap Schedules:
44		A-1
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