BEFORE THE ARIZONA CORPORATION COMMISSION

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AZ Corporation Commission
Director Of Utilities

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IN THE MATTER OF THE APPLICATION OF PINEVIEW WATER COMPANY, INC. FOR AUTHORITY TO ISSUE PROMISSORY NOTE(S) AND OTHER EVIDENCE OF INDEBTEDNESS PAYABLE AT PERIODS OF MORE THAN TWELVE MONTHS AFTER THE DATE OF ISSUANCE.	DOCKET NO. W-01676A-04-0463
IN THE MATTER OF THE APPLICATION OF PINEVIEW WATER COMPANY, INC. FOR AN INCREASE IN ITS WATER RATES FOR CUSTOMERS WITHIN NAVAJO COUNTY, ARIZONA.	DOCKET NO. W-01676A-04-0500 DECISION NO. 67989 **OPINION AND ORDER**

DATES OF HEARING: February 24 and 25, and March 3, 2005

PLACE OF HEARING: Phoenix, Arizona

ADMINISTRATIVE LAW JUDGE: Teena Wolfe

APPEARANCES: Mr. Richard L. Sallquist, SALLQUIST & DRUMMOND, P.C., on behalf of Pineview Water Company, Inc.;

Mr. Dan E. Simpson, in propria persona; and

Mr. Tim Sabo and Ms. Diane Targovnik, Staff Attorneys, Legal Division, on behalf of the Utilities Division Staff of the Arizona Corporation Commission.

BY THE COMMISSION:

Pineview Water Company, Inc. ("Pineview" or "Company")[1] is a public service corporation providing water utility service to approximately 936 metered customers located in an approximately four square mile service area located southeast of the Town of Show Low in Navajo County, Arizona. On June 18, 2004, Pineview filed with the Arizona Corporation Commission ("Commission") the above-captioned application for financing authority. Also on June 18, 2004,

[1] The Company changed its name from Pineview Land and Water Company, Inc. to Pineview Water Company, Inc. on May 28, 1998.

Pineview filed an application for approval of an off-site facilities hook-up fee tariff, which was approved as amended in Decision No. 67265 (October 5, 2004). On July 9, 2004, Pineview filed the above-captioned rate application. The Commission consolidated the financing and rate applications, and held a full public hearing before a duly authorized Administrative Law Judge on February 24 and 25, and March 3, 2005.

Pursuant to Procedural Orders issued November 15, 2004, and December 10, 2004, intervention was granted to Thomas R. Cooper and Dan E. Simpson. Mr. Simpson provided public comment at the hearing. Mr. Ron McDonald, the General Manager of the Company since April 7, 2003, and Mr. Dan L. Neidlinger, who as consultant to the Company, assisted the Company in the preparation of both the financing and rate applications, testified on behalf of the Company. Mr. Alejandro Ramirez, Ms. Dorothy Hains, Mr. James Johnson, and Ms. Elena Zestrijan testified on behalf of the Commission's Utilities Division Staff ("Staff"). Although several customers filed written public comments prior to and following the hearing, no customers other than Mr. Simpson appeared to make public comment at the hearing.

DISCUSSION

A. FINANCING APPLICATION

In its application, Pineview requests authority to issue long-term notes and other evidences of indebtedness in the original amount not to exceed $730,978, from the Arizona Water Infrastructure Financing Authority ("WIFA") for the purpose of financing construction of an additional well at an estimated cost of $271,459, a two million gallon storage tank at an estimated cost of $304,150, and a 12-inch transmission line at an estimated cost of $155,369, for a total project cost estimate at $730,978 (Financing Application, Exh. A-2 at 1, Attachment B). The loan as requested by the Company would be a $730,978 twenty year, fully amortizing WIFA loan at 4.20 percent with monthly debt service of $4,507 (Direct Testimony of J. H. Johnson, Exh. S-12, Attached Memorandum at 2). The financing application further requests that to the extent the purposes of the proposed loan may be considered reasonably chargeable to operating expenses or to income, they be permitted by this Order (Exh. A-2 at 3).

Concurrently with the financing application considered herein, the Company filed, in a

separate docket, a tariff filing to implement an off-site facilities hook-up fee of $1,500 per 5/8 x 3/4-inch meter for the purpose of partially financing the facilities the Company is proposing in the financing application we consider herein. In Decision No. 67275, we authorized a reduced hook-up fee of $500 to recognize the 400,000 gallons of storage capacity recommended by Staff in lieu of the 2 million gallon storage tank as proposed by the Company. Decision No. 67275 found that the Company's proposal to add 2 million gallons of additional storage capacity was driven by the Company's plan to convert its existing system and customers to a gravity flow system, and that including the cost of the new storage required for gravity-flow for existing customers in the hook-up fee, which applies only to new customers, would be inappropriate. The Company projects 500 new customers in a planned development in its service territory. If the Company collects the hook-up fee authorized in Decision No. 67275 from each of its projected 500 new customers, it will collect $250,000 (500 x $500), or just over 50 percent of Staff's estimated cost of $439,537 for the new backbone facilities that would be required to serve the 500 new connections.

In this case, Staff is recommending financing approval in the amount of $577,578, subject to the establishment of rates to provide Staff's recommended operating income in the rate case (Exh. S-12 at 2). Staff's recommendation for financing differs from the $730,978 requested by the Company in that it includes funding for the projected cost of a one million gallon storage tank in lieu of a two million gallon storage tank, and excludes $54,000 for financing 1.5 acres of land for a wellsite upon which the Company has future plans to drill an additional well (Direct Testimony of Dorothy Hains, Exh. S-13 at 21-22).

The pro-forma capital structure for Pineview resulting from a $577,578 loan consists of 3.3 percent short-term debt, 68.2 percent long-term debt and 28.5 percent equity (Exh. S-12 at 3). Staff's witness on the financing application states that the Staff Engineering Report concludes that only $577,578 of the proposed expenditures are necessary for the continuation of service to present customers; that Pineview can support $577,578 in new long-term debt with implementation of Staff's recommended rates and a reduction in expenses consistent with Staff recommendations; and that use of loan proceeds for operating expenses or income is an inappropriate use of the funds (*Id.*). Staff recommends that Pineview not be allowed to utilize loan funds for operating expenses or income.

Pineview disagrees with Staff's analysis of plant needs for the Company. The Company argues that the ability to construct a two million gallon tank is a one-time opportunity, as the Company has acquired a well site at the highest point in its service area, which would allow gravity-feed to the water system, but that the site has a footprint large enough for only a single storage tank, and that if a one million gallon tank is constructed on that site, the tank cannot later be retrofitted to accommodate additional storage (Co Br. at 14). Staff stated that building a two million gallon tank without current and foreseeable need would mean that customers today would be paying for Pineview's future investment (Tr. at 358). Staff's engineering witness testified that its recommendation for a one million gallon storage tank will meet the Company's needs to serve its projected growth, including fireflow needs (Tr. at 346-347), and that a two million gallon tank is so large that with the Company's current production, it would take three days to fill, and would run the risk of not filling fast enough to prevent the pumps from burning out (Tr. at 348). Staff testified that the Company can still convert its system to a gravity flow system on its chosen site with a one-million gallon tank, and that if the future need arises, it can connect another storage tank or create a hybrid system of pressure and gravity storage, and that a future system encompassing dual tanks would be more reliable than a single larger tank in the event of an unplanned or scheduled tank outage (Tr. at 349).

We find Staff's engineering analysis to be sound regarding the Company's current capacity and plant construction needs. We also find, as we found in Decision No. 67275, that the Company's proposal to add a two million gallon storage tank is driven not by an actual need for two million gallons of storage, but by the Company's plan to convert its existing system and customers to a gravity flow system. Pineview argues on brief that financing the entire cost of a two million gallon tank with WIFA loan funds would result in lower costs to ratepayers than if the Company were to fund the difference between the cost of a one million gallon tank and a two million gallon tank with equity (Co. Br. at 14). This argument is based on an assumption that the capital costs of the additional one million gallons of capacity would be found prudent in a future rate proceeding. While the Company is free to make business investment decisions based on its assumption of future needs, our determination here is based on the Company's plant needs related to this proceeding, not a future

rate proceeding.

Staff's recommendations on the financing application are reasonable and will be adopted. Because a one million gallon storage tank will meet the Company's needs to serve its projected growth, including fireflow needs, our financing approval herein does not include the additional cost of one million gallons of excess storage capacity or the additional cost proposed for financing 1.5 acres of land for a wellsite on which the Company has future plans to drill additional wells.

B. RATE APPLICATION

Pineview's rate application was filed on June 9, 2004. Staff found the application sufficient on September 7, 2004, following Pineview's provision of supplemental information. The application is based on a test year ending December 31, 2003. The application requested a revenue increase of $126,453, or a 24.19 percent increase over a test year operating loss as filed of ($20,226). Staff recommended a revenue increase of $15,495, or a 2.96 percent increase over adjusted test year revenues of $35,418.

1. Rate Base

The application states an adjusted original cost rate base ("OCRB") of $730,084. No reconstruction cost new less depreciation ("RCND") schedules were filed. Staff recommends an adjusted OCRB of $662, 093.

Trucks and Backhoe

2001 GMC Trucks

The application requests recovery of lease expense associated with two 2001 GMC trucks purchased by Henry and Katherine Sutter on February 27, 2001. According to a document presented at hearing titled "Pineview Water Company Vehicle Lease to Purchase Agreement" dated April 13, 2001 and signed by Ernest E. Sutter in the capacity of Vice President, Pineview Water Company and Henry E. Sutter (not signed as President of Pineview Water Company, although he is the Company's President), Pineview agreed to pay Henry Sutter $1,200 each month for 60 months (Exh. A-11). According to the document, the monthly payment agreed upon by Henry Sutter and Ernest Sutter, his son, included $952.46 per month to go to make finance payments to Bank of the West, while $247.54 per month, for a total of $14,852.40 over the course of 60 months, considered the "Lease Fee," was to

go to Henry Sutter (*Id.*). Pineview's witness testified that the "Lease Fee" payments went to Henry Sutter for the purpose of "paying him back his down payment" (Tr. at 180). The same witness acknowledged, however, following the Company's presentation of the bills of sale for the trucks (Exhs. A-10 and A-12) that the down payment on the trucks was $5,000 for each truck, for a total of only $10,000 (Tr. at 222).

Staff recommends that all the lease expense for the two 2001 GMC trucks be disallowed and that the trucks be included in the Company's rate base at their original cost as shown on the bills of sale ($27,716.02 and $27,720.77, for a total of $55,436.79) less accumulated depreciation (Tr. at 408). Staff has proposed a reasonable ratemaking treatment for the vehicles, under the circumstances, and Staff's adjustments will be adopted.

As a public service corporation, the Company has a responsibility and a duty to utilize ratepayer revenues to provide water utility service to its customers, and for no other purpose. Behavior such as the mark-up of the loan to the Company over the actual purchase price of these two vehicles constitutes self-dealing behavior on the part of the Company and its owner[2] that is antithetical to ratemaking principles and is completely inexcusable. Likewise, the Company's action turning over its 1994 backhoe to its owner Henry Sutter, as described below, to trade in at a price that appears to be significantly below its book cost also constitutes inexcusable self-dealing behavior on the part of a public service corporation and its owner. This and any similar self-dealing behavior cannot and will not be tolerated. We will require Staff to carefully scrutinize the Company's books in the Company's next rate case. If the Company and its owners engage in similar activity in the future, appropriate punitive action will be taken. In addition, we will require the Company to submit pertinent financial information for calendar year 2006.

1979 Truck

Pineview's application requested lease expense for a 1979 truck, and in the alternative, asked that the truck be included in rate base. Staff recommended that both requests be denied, based on its conclusion that the truck is not used and useful (Exh. S-14 at 11). Staff points out that while

[2] Pineview's 2005 Annual Report lists Henry Sutter as a shareholder having more than a 20 percent beneficial interest in the Company.

Pineview's witness testified that the Company puts its logo on all of its equipment, the Company's logo is not on the 1979 truck; that the truck was not included with the other trucks in the Company's workpapers; and that Pineview could not produce the registration or insurance for the truck (Staff Br. at 5). Staff further argued that the lease would result in Pineview paying $7,200 for a 26-year old truck (*Id.*). Pineview has not demonstrated that the 1979 truck is used and useful. Therefore it should not be included in rate base, and no lease expense associated with the truck should be allowed.

Backhoe

The Company's application requested recovery of lease expense of $18,000 and equipment repair expense of $5,578 related to a 1998 Case Model 580 SL backhoe. While Staff and Pineview agree that a backhoe should be included in rate base, they disagree as to the original cost amount to be included. Staff recommends that the lease expense be disallowed, and that the Company's rate base reflect the original cost of an older 1994 backhoe that was included in rate base in the Company's prior 1996 rate case, because Pineview's books do not reflect the retirement of that backhoe, and because Pineview has not met its burden of proof to justify deviation from what is shown on its books (Staff Br. at 4). In the alternative, Staff states that in the absence of an accurate original cost number, a "market valuation" replacement cost for the new 1998 backhoe would be an acceptable approach (Staff Br. at 5). Pineview is not opposed to rate base treatment of the backhoe, and proposes capitalizing the backhoe at the amount shown on a 1998 invoice, with appropriate depreciation adjustments (Co. Br. at 6). Staff and Pineview agree that the backhoe approved in Pineview's last rate case must be removed from Pineview's books (Co. Br. at 7; Staff Br. at 4). Pineview states that $37,926, the value of the 1994 backhoe that appears as a plant addition in 1996, should be removed from its books along with the associated Accumulated Depreciation for 1996 through 2002 of $15,018 ($37,926 x 4.95 percent x 8 years = $15, 018) (Co. Br. at 7, citing Exh. S-20, Tr. at 246-252).

Evidence produced at the hearing regarding the backhoe included: 1) an invoice dated November 30, 1998 for $57,526.80 ($69,526.80 including tax, less $12,000 in rental payments applied) from Falcon Power to Pine View Land & Water for a Case 580SL 4WD Extendahoe SN JJG0267017 (Exh. A-18); 2) a document titled "Pineview Water Company Vehicle Lease to purchase

Agreement" dated May 2, 2000 and signed by Ernest E. Sutter in the capacity of Vice President, Pineview Water Company and Henry E. Sutter (not signed as President of Pineview Water Company), in which Pineview agreed to turn over a 1994 Case Backhoe to Henry Sutter as a $17,000 down payment for a 1998 Case Backhoe Model #580 SL, ID #JJG067017, and to pay Henry Sutter $1,000 each month for 43 months, after which Henry Sutter would provide a bill of sale conveying the equipment to Pineview (Exh. A-9); and 3) a page-printed from the website "usediron.point2.com" on March 2, 2005 depicting asking prices for four 1997 Case Model 580SL backhoes in Canadian and U.S. Dollars (Exh. S-27); and 4) conflicting testimony from Pineview's witness regarding the date the backhoe was placed in service (Tr. at 166 (indicating 2002) and Tr. at 266-268 and 566-67 (indicating 1998)). Pineview argues on brief, however, that the May 2, 2000 lease to purchase agreement demonstrates that the Company acquired the 1998 backhoe on or about May 2, 2000 (Co. Br. at 6).

It appears from the invoice and the testimony at hearing that Henry Sutter bought the backhoe in 1998 (Tr. at 88, 129, 163, 567) using the name Pine View Land & Water in order to obtain a "discount" (Exh. A-18; Tr. at 588); and that subsequently Henry Sutter decided to lease the backhoe to Pineview commencing May 2, 2000 (Exh. A-9). The May 2, 2000, lease-to-purchase agreement in the amount of $43,000 indicates that Pineview turned over the its existing backhoe (the 1994 backhoe placed in rate base in 1996) to Henry Sutter at a trade-in value of $17,000, and that Henry Sutter charged Pineview $60,000 for the 1998 Case backhoe (Exh. A-9).

Regarding the valuation of the new backhoe, we agree with Staff that the conflicting evidence makes it problematic. However, we do not believe that Staff's "market valuation" of the backhoe (Exh. S-27; Tr. at 543) provides a reasonable solution, in this particular case, to a determination of the original cost of the 1998 backhoe. Despite the existence of conflicting testimony, the preponderance of the evidence demonstrates that the correct in-service date for the 1998 backhoe is May 2, 2000, the date of the lease-to-purchase agreement signed by Ernest and Henry Sutter. Although the 1998 invoice depicts the purchaser of the backhoe to be "Pine View Land and Water," the Company's witness repeatedly testified that the purchaser was Henry Sutter (Tr. at 88, 129, 163, 567) and testified that the invoice was issued with the name of the Company instead of Henry Sutter's name so that Mr.

Sutter could acquire the backhoe at a lesser cost, due to a substantial governmental discount, than if he had bought the backhoe in his own name (Tr. at 588). In addition, if Pineview had in fact been the actual purchaser of the backhoe in 1998, it would be unlikely that Pineview would have requested lease expense recovery in its rate application.

As Staff points out, in order to establish the value of the 1998 backhoe, the trade-in value of the 1994 backhoe must be deducted from the purchase price (Tr. at 474). Because the lease-to-purchase agreement was not an arms' length transaction, and because there is no evidence independently establishing the trade-in value of the 1994 backhoe, it is reasonable to use the book value of the 1994 backhoe less the accumulated depreciation as of the date of the lease-to purchase agreement for the purpose of establishing its trade-in value. Following the depreciation formula provided in the Company's brief, the value of the 1994 backhoe at the time of Pineview's "trade-in" to Henry Sutter under the May 2, 2000 lease-to-purchase agreement for $60,000 would have been $29,477.97, and not the $17,000 shown on the agreement:

Item	Amount	Reference
Original Cost of 1994 Backhoe in 1996	$ 37,926.00	As established in Decision No. 59934
Service Life	20 years	Account 345 Depreciation Rate Schedule (Exh. S-20 at 29)
Annual Depreciation Rate	4.95 percent	Per Company's Brief at 7
Annual Depreciation Amount	$ 1,877.34	(4.95 percent x $37,926)
1996 depreciation	$ 938.67	(Half-year convention)
1997 depreciation	$ 1,877.34	
1998 depreciation	$ 1,877.34	
1999 depreciation	$ 1,877.34	
2000 depreciation	$ 1,877.34	
Total depreciation, 1996-2000	$ 8,448.03	
1994 backhoe Original Cost in 1996	$ 37,926.00	
Accumulated Depreciation, 1996-2000	$ 8,448.03	
Reasonable 1994 backhoe net book value at trade-in	$ 29,477.97	

Absent clear evidence verifying the original cost for the 1998 backhoe placed in service in May 2000, a reasonable original cost should be established in this proceeding, based on the evidence. Because the lease-to-purchase agreement price of $60,000 ($17,000 down payment and $43,000 in lease-purchase payments) is not the result of an arms-length transaction, we have utilized the

available evidence to establish a reasonable original cost of $20,929.88 for the 1998 backhoe at its May 2, 2000 acquisition date, as follows:

Item	Amount	Reference
November 30, 1998 Invoice Cost	$ 57,526.80	Per Exh. A-18, $ 69,526.80 including tax, less $ 12,000.00 in rental payments applied[3]
In-service date	May 2, 2000	Co. Brief at 6; Tr. at 270
Service Life, Account 345	20 years	Depreciation Rate Schedule (Exh. S-20 at 29)
Annual Depreciation Rate	4.95 percent	Per Company's Brief at 7
Annual Depreciation Amount	$ 2,847.58	
1998 depreciation	$ 1,423.79	Half-year convention
1999 depreciation	$ 2,847.58	
2000 depreciation	$ 2,847.58	
Total depreciation from 1998-2000	$ 7,118.95	
November 30, 1998 Invoice Cost	$ 57,526.80	
Less: reasonable depreciation, 1998-2000	$ 7,118.95	
Less: reasonable book value of trade-in	$ 29,477.97	See table above
Reasonable May 2, 2000 Original Cost	$ 20,929.88	

Because the 1994 backhoe was retired from service when it was traded in on May 2, 2000, the 1994 backhoe at its original cost of $37,926 should be removed from rate base, with a corresponding $3,754.68 adjustment to Accumulated Depreciation to account for the two years of depreciation expense following its trade-in in 2000. The reasonable original cost of $20,929.88 for the 1998 backhoe placed in service in May 2000, as determined above, should be added to rate base, with an associated adjustment to Accumulated Depreciation in the amount of $3,626.88. This adjustment to Accumulated Depreciation is determined as follows:

Item	Amount	Reference
Reasonable May 2, 2000 Original Cost	$ 20,929.88	See table above
In-service date	May 2, 2000	Co. Brief at 6; Tr. at 270
Service Life, Account 345	20 years	Depreciation Rate Schedule (Exh. S-20 at 29)
Annual Depreciation Rate	4.95 percent	Per Company's Brief at 7

[3] It must be assumed that the person or entity who paid the $12,000 in rental payments received the use of the backhoe in exchange in an equal amount. Pineview's ratepayers should therefore not be responsible for the $12,000.

Annual Depreciation Amount	$ 1,036.29	
2000 depreciation	$ 518.01	Half-year convention
2001 depreciation	$ 1,036.29	
2002 depreciation	$ 1,036.29	
2003 depreciation	$ 1,036.29	
Accumulated Depreciation from 2000-2003	$ 3,626.88	

Leasehold Improvements

The Company is requesting the capitalization of $1,725 in costs expended to improve the interior of its offices, which are leased from Officers of the Company, and argues that the Company's lease clearly establishes the Company's obligation to fund the improvements (Co. Br. at 8). Staff agrees that the expenses were the responsibility of Pineview under its lease (Staff Br. at 5). We agree with the Company and Staff. The $1,725 in costs will be capitalized.

Well Site

The Company has requested inclusion in rate base of $50,750 for a well site it owns. Staff recommends removal of the well site from rate base on the grounds that it is not used and useful due to the fact that wells have not yet been drilled on the site (Staff Br. at 5). The Company admits that the well site does not have all facilities installed at this time, but argues that it should be included in rate base nonetheless because there is a need for additional wells on the system at the well site, the need for new wells is recognized by Staff, and the well site parcel is essential to the engineering plans for the storage and gravity pressure system for the entire system (Co. Br. at 5). At the time of the hearing, over a year following the end of the test year, the wells planned for the well site were permitted, but not yet in existence (Tr. at 119-120). Because no water utility service is being provided from the well site, ratemaking principles prohibit its inclusion in rate base. Staff's recommended adjustment removing the well site from rate base will therefore be adopted.

Other Rate Base Issues

Reclassifications

Staff recommended reclassification of various items between plant accounts (Exh. S-14, Sched. ENZ-5, notes 3,4,6 and 8). In addition, Staff recommended reclassification of a touchreader from operating expense to Miscellaneous Equipment (Exh. S-14, Sched. ENZ-5, note 9). Pineview

did not object to these reclassifications and they will be adopted.

Accumulated Depreciation

Staff recalculated accumulated depreciation starting from the authorized levels in the 1996 rate case order (Exh. S-14, Scheds. ENZ-3 and ENZ-6), and re-adjusted accumulated depreciation during the course of the hearing (Exh. S-19, revised Sched. ENZ-3). Staff's recommendation will be adopted, with appropriate additional adjustments necessary to conform to the rate base adjustments for the backhoe described above, for an accumulated depreciation balance of $1,075,069.

Contributions in Aid of Construction ("CIAC")

Staff recommended adjusting CIAC upward by $622 to reflect used Pineview's actual level of CIAC of $15,334 as shown on Pineview's books, and made a corresponding $622 adjustment to CIAC accumulated amortization (Exh. S-14, Sched. ENZ-7 and ENZ-8). Pineview did not object and Staff's adjustments will be adopted.

Customer Deposits

Staff adjusted customer deposits to match Pineview's general ledger amount of $7,769 (Exh. S-14, Sched. ENZ-9). Pineview did not object. Staff's adjustment will be adopted.

Meter Advances

Staff originally adjusted Meter Advances downward (Exh. S-14, Sched. ENZ-3). However, at the hearing, Staff provided an exhibit the effect of Staff's withdrawal of this adjustment on its rate base recommendations (Exh. S-19). Staff's original adjustment will therefore not be adopted.

Adjusted Original Cost Rate Base/Fair Value Rate Base

The foregoing adjustments to the Company's proposed OCRB of $730,084 result in an OCRB for this proceeding of $663,243. No RCND schedules were filed. The Company's fair value rate base ("FVRB") is determined to be $663,243, the same as its OCRB.

2. Operating Income and Expenses

The application states test year operating revenue of $522,724, and was not contested. Staff recommends a total of 11 adjustments to the Company's test year expenses, as follows:

Salary and Wages Expense

The Company requests Salaries and Wages Expense of $231,295 (Exh. A-1, Sched. C-1).

Staff recommends an adjustment that removes salaries for Mr. Henry Sutter, $33,000 ($3,000 per month for 11 months); Mrs. Katherine Sutter, $33,000 ($3,000 per month for 11 months); Ms. Mandy Sutter, $12,720 ($240/week for 53 weeks); and Taren Sutter, $2,200 ($440/week for 5 weeks) for a total reduction in Salaries and Wages Expenses of $80,920 (Exh. S-14 at 9-10, Scheds. ENZ-12 and 13). Staff recommends allowance of Salaries and Wages Expense for the following staffed positions per job descriptions submitted by the Company: Billing Clerk, Staff Accountant, Senior Serviceman, Operations Superintendent, Site Project/Inspection Manager, and General Manager for a total amount of $178,000. Staff further recommends that Directors' fees of $150 each per monthly Board of Directors meetings be allowed for Henry, Katherine and Mandy Sutter, for a total of $5,400. Staff's total recommended Salaries and Wages Expense is $184,280.

The Company objects to Staff's recommendation that the salaries of Henry, Katherine, Mandy and Taren Sutter be disallowed. The Company asserts that because Staff conceded that the job functions in detailed job descriptions that the Company provided to Staff may be legitimate functions for Company employees, Staff's refusal to acknowledge the expense is arbitrary (Co. Br. at 9). We disagree. Staff notes that there is no minimally adequate workspace available in the Company's business office for the purported Sutter family "executives" to perform executive functions (Tr. at 442, 445-446), and that water companies of Pineview's size do not maintain as many employee positions as Pineview is requesting in this case (Tr. at 443). In addition, Staff testified that the oversight functions described in the detailed job descriptions are functions legitimately discussed and resolved at the monthly Board of Directors' meetings for which Staff is recommending compensation of Board members Henry, Kathrine and Mandy Sutter (Tr. at 445-446; Exh. S-14, Sched. ENZ-13). The Company presented no evidence to rebut this testimony.

We also agree with Staff that Pineview's Operations Manager's extensive management experience in running a public works unit with 60 employees qualifies him to supervise Pineview's six employees without the assistance of Sutter family members at the additional $80,920 requested salary expense (Tr. at 142-43). Staff's recommended adjustments to Salaries and Wages Expense are reasonable and we will adopt them.

Employee Pensions and Benefits

Staff recommends that based on the Company's benefits percentage as submitted by the Company and on Staff's adjustments to Salaries and Wages Expense, Pineview's Employee Pensions and Benefits Expense be adjusted downward 16 percent, or $7,557, from $37,171 to $29,614. On April 22, 2005, after closing briefs were filed, the Company filed an affidavit in which the Company's witness Ron McDonald requested that Staff's recommended Pension and Benefit disallowance of $7,557 not be adopted. The affidavit stated that he failed to testify that the Pensions and Benefits expense of $7,557 was associated with salaried and hourly employees other than Sutter family members. Staff filed a response to the affidavit on April 27, 2005. Staff objected to the filing as untimely. In addition, Staff addressed the substance of the affidavit, stating that the paperwork accompanying the affidavit is a company-produced document that is not an actual receipt proving that the monies are going to pay Employee Pensions and Benefits Expense. Staff states that even if the paperwork filed with the affidavit is correct, Staff's recommended disallowance of Employee Pensions and Benefits Expense is fair and justified, in that the disallowance constitutes 16 percent of the Company's claimed total Employee Pensions and Benefits Expense, to accord with Staff's recommended disallowance of 16 percent of total Salary and Wages Expense. We agree with Staff that its approach to Employee Pensions and Benefits Expense is consistent with its approach to Salary and Wages Expense, which we have adopted for the reasons stated above. The Company's post-briefing affidavit was not admitted into the hearing record, and in any event, does not provide a convincing rationale for deviation from Staff's recommended approach. Staff's recommended adjustment will be adopted.

Purchased Power Expense

Staff recommends a reduction to Purchased Power Expense of $3,441, based on records the Company provided to Staff showing Purchased Power Expense broken down by location for a total test year expense of $39,512. In rebuttal testimony, Pineview's witness stated that the Company has receipts for purchased power in 2003 totaling $42,953 and that Purchased Power Expense should therefore be increased by $3,441 (Rebuttal Testimony of Ron McDonald, Exh. A-6 at 8), but no evidence of such data or receipts were produced for the record. Pineview did not demonstrate that

test year Purchased Power Expense exceeded $39,512. Staff's adjustment is reasonable and will be adopted.

Repairs and Supplies Expense

The Company proposes $29,243 in test year Repairs and Supplies Expense. Staff's recommended $7,017 adjustment to this expense account includes the removal of a duplicate $350 billing for a septic clean up, reclassification of $1,089 to transportation expense for repairs related to the two 2001 GMC trucks, and removal of $5,578 pertaining to heavy equipment repairs that Staff believed were related to Mr. Sutter's heavy equipment rental operations, and not to equipment that Pineview owned (Staff Br. at 7; Exh. A-14 at 10, Sched. ENZ-16).

The Company argues that repair costs related to the 580 SL backhoe should be allowed if the backhoe is included as either lease expense or capital addition (Co. Br. at 10). We agree. Because the 580 SL backhoe has been allowed in rate base, the associated repair and maintenance costs for which invoices appear in the record shown on Exhibit S-22, admitted at the hearing, should be allowed, in the amount of $664.13. Staff's adjustments to Repairs and Supplies Expense will be adopted, except that Staff's downward adjustment disallowing expenses for backhoe repairs will be reduced from $5,578 to $4,914.

Office Supplies and Expense (Uniform Expenses)

The Company asserts that the Company's requested $720 per year uniform replacement cost associated with the new practice of employee-maintained uniforms in lieu of uniform rental should be allowed if the test year uniform rental expense of $1,152 is disallowed (Co. Br. at 10). Staff agrees (Staff Br. at 8). The downward adjustment to Office Supplies Expense recommended by Staff is therefore $432, and not $1,152, and we adopt it.

Contractual Services Expense

Staff recommended that this expense be increased by $3,157 (Exh. S-14, Sched. ENZ-17). The Company did not object and this adjustment will be adopted.

Rate Case Expense

The Company requested recovery of rate case expense in the amount of $48,000. Staff did not dispute the amount of rate case expense, but recommended that it be amortized over a 5-year

period as opposed to the Company's proposed three years (Staff Br. at 8; Tr. at 518, Exh. S-16, Sched. ENZ-21). However, Staff stated that if its recommendation that Pineview be ordered to file a rate case within 3 years is adopted, the amortization period for rate case expense should accordingly be shortened to 3 years (*Id.*). As we will adopt Staff's recommendation to require Pineview to file a rate case in 3 years, we will adopt the Company's and Staff's recommendation that rate case expense be amortized over 3 years.

Lease Expense (Equipment)

Staff recommended removal of lease expense for the two 2001 GMC trucks in the amount of $14,400; the heavy equipment lease for the backhoe in the amount of $18,000; and rent expense of $5,067 for unsubstantiated expenses, such as checks issued directly to Henry Sutter for the lease of a 1979 truck that is not used and useful, and installation of a toolbox (Exh. S-14, Sched. ENZ-18). As discussed above, including lease expense for the two 2001 GMC trucks and the 1998 backhoe is unnecessary as they are included in rate base. Also as discussed above, the 1979 truck is not used and useful, so no lease expense is appropriate. Staff's adjustments are reasonable and will be adopted.

Transportation Expense

As described above, Staff recommended that $1,089 be reclassified from repairs and maintenance to Transportation Expense. In addition, Staff recommended the following adjustments to Transportation Expense: removal of Henry Sutter's fuel expense in the amount of $480, for mileage unrelated to Company business; an unsubstantiated fuel expense of $79; and fuel expenses of $530 for the 1979 truck which is not used and useful (Exh. S-14 at 12, Sched. ENZ-20). Pineview objected to the removal of Henry Sutter's fuel expense based on the argument that Mr. Sutter incurred the fuel expense as an employee in performing his duties as President of the Company (Co. Br. at 10). The Company failed to show that the mileage expense was related to Company business. Staff's adjustments are reasonable and will be adopted.

Postage and Freight Expense

Staff recommended disallowance of $311 in Postage and Freight Expense that was incurred by Mercon Incorporated, a company owned by Ernie Sutter and Paula Sutter (Exh. S-14, Scheds.

ENZ-11 and ENZ 21). Mr. McDonald testified that the $311 in Mercon invoices were actually Pineview expenses, and that since his arrival at the Company all invoices with incorrect company references have been returned to the vendor for rebilling prior to payment (Tr. at 192-194). Staff's adjustment disallowing expenses invoiced to Mercon is proper and appropriate, and will be adopted.

Telephone Expense

The Company requested $9,013 in test year telephone expense. Staff recommended recognition of the following telephone expense: $1,478 for answering service; $2,417 for four cellular phones; $2,559 for two office landlines and one landline for facsimile; and $445 for long distance carrier charges (Exh. S-16; Tr. at 413-414, 482, 484). Staff argues that its recommended adjustment accurately reflects ongoing expenses and is necessary because Pineview achieved substantial savings by switching its cellular providers (Staff Br. at 7-8). The Company argues on brief that Staff's adjustment to Telephone Expense in the amount of $1,994 is a disallowance of telephone landlines expense, and that Staff did not demonstrate that the landlines are no longer used or that the adjustment is reasonable (Co. Br. at 10). However, Pineview's witness stated that the current telephone bills provided by the Company, on which Staff based its adjustments, accurately depict the Company's current telecommunications charges (Tr. at 150). Staff's adjustment does not disallow telephone landlines expense, and it accurately reflects a known and measurable, and reasonable, change in test year expenses. Staff's adjustment to Telephone Expense will be adopted.

Materials and Supplies Expense

Staff recommended an adjustment reclassifying the purchase of a touchreader to plant in service (Exh. S-14 at 12, Sched. ENZ 19). Pineview did not object. Staff's recommended adjustment is reasonable and will be adopted.

Bad Debt Expense

The Company requested recognition of a write-off of bad debt expense of $11,131, amortized over three years for a test year expense amount of $3,710. This bad debt expense dates back to the beginning of the Company, and prior to this rate case, the Company has never written off any bad debt expense (Tr. at 485). The Company asserts that Staff is proposing an $8,347 reduction in bad debt expense, which duplicates the Company's amortization adjustment (Co. Br. at 11). However, as

explained by Staff, the amount labeled in Exhibit S-14 on Schedule ENZ-21 as "Four year average, accounts receivable write-offs $8,347" was labeled in error. The $8,347 adjustment included several expense adjustments totaling approximately $1,022 in addition to the bad debt amortization, and actually included only a $928 upward adjustment to the Company's proposed $3,706 in bad debt expense (Exh. S-16, Tr. at 489, 499). This $928 difference reflects Staff's proposed four-year amortization instead of the Company's proposed three-year amortization. As Staff stated, Staff's proposed adjustment is very lenient, as the $11,131 could reasonably be spread over a period longer than four years (*See* Tr. at 485; Staff Br. at 8). The Company did not object to the $1,022 in expense adjustments which are detailed in Exhibit S-16. The proposed adjustments are reasonable and will be adopted. Staff's proposed adjustment to bad debt expense is also reasonable, and we will adopt it.

Total Test Year Operating Expenses

The foregoing adjustments result in test year Operating Expenses of $379,236. In addition, Staff proposed an adjustment to test year depreciation expense using the recommended depreciation rates as shown on page 29 of Exhibit S-13. This resulted in an increase in Depreciation Expense of $37,589, for a total of $82,273, which we adopt. An adjustment increasing property tax expense by $10,321 over Staff's recommended $27,797 is also required, for total property tax expense of $38,118.

Consolidation of Expense Accounts/Commingling

Staff noted that the Company is consolidating too many expense accounts into miscellaneous expense, and recommended that on a going-forward basis, the Company be ordered to keep all its expense information in accordance with the National Association of Regulatory Utility Commissioners' ("NARUC") Uniform System of Accounts ("USOA"), and to file an affidavit within 120 days of this Decision attesting that its accounting system has been updated to comply with the NARUC USOA. This recommendation is reasonable, and we will order Pineview to follow it. The Company's adoption of a more detailed expense accounting system should facilitate the separation of Company expenses from expenses associated with non-Company operations of the Company's owners, and should make clear to the Company's employees the necessity of a strict prohibition of payment of any non-Company expenses from water utility revenues. We expect the intermingling of Company business with non-Company business, in regard to expenses and plant, to be completely

eliminated before the Company's next rate case filing. We will adopt Staff's recommendation to order the Company to institute mandatory training for its equipment operators to keep logs on equipment usage, and will also direct the Company to institute mandatory employee training to address commingling issues. We will require the Company to submit for Staff approval a detailed implementation plan for the mandatory training and will require Staff to follow up on the Company's implementation of the plan. We will also direct Staff to closely examine the Company's books and records in the Company's next rate case, and to bring to the attention of the Commission any questionable expenses and plant additions. If the Company cannot clearly demonstrate that expenses and plant additions are for the sole benefit of the Company in its provision of water utility service to the public, they will be disallowed. In addition, if the intermingling which was clearly evident in this case is not eliminated, we will strongly consider levying penalties on the Company. We will also require the Company to submit before March 31, 2007 all information identified in A.A.C. R14-2-103 describing the Company's business activities in calendar year 2006, except Reconstruction Cost New (RCN) information and Schedules F, G and H. We will direct Staff to closely examine this information to evaluate the extent to which the Company's expenses and plant additions are for the sole benefit of the Company in its provision of water utility service to the public and the Company is complying with all other requirements of this Decision. As appropriate to the results of its review, Staff shall make a recommendation to the Commission regarding the need for Commission action before the Company's next rate filing. We do not predict the outcome of Staff's review here nor seek to prescribe the range of recommendations that Staff may suggest; however, if the intermingling which was clearly evident in this case persists, we will consider Staff's petition for an Order to Show Cause to be appropriate.

3. <u>Cost of Capital</u>

Pineview and Staff propose the following capital structure, cost of debt and return on equity:

Pineview's Proposed:

	Weight (%)	Cost	Weighted Cost
Long-term Debt	49.03%	5.43%	2.662%
Common Equity	50.97%	15.39%	7.843%
Weighted Avg. Cost of Capital			**10.505%**

Staff's Proposed:

	Weight (%)	Cost	Weighted Cost
Long-term Debt	49.0%	5.43%	2.7%
Common Equity	51.0%	8.9%	4.5%
Weighted Avg. Cost of Capital			**7.2%**

Staff recommends adoption of the Company's proposed capital structure, rounded to 49 percent debt and 51 percent equity, and the Company and Staff agree on the Company's cost of debt of 5.43 percent. The Company and Staff disagree, however, on the cost of equity to be established for Pineview in this proceeding. This is the basis of the Company's and Staff's differing recommendations on the Company's weighted average cost of capital.

Staff recommends a 7.2 percent weighted average cost of capital, which is based on Pineview's cost of debt of 5.43 percent and on Staff's cost of equity estimates that range from 8.5 percent to 9.3 percent. In coming to its weighted average cost of capital recommendation, Staff employed a cost of capital analysis consistent with its approach in recent cases (Tr. at 339), using a capital asset pricing model ("CAPM"), a constant-growth discounted cash flow ("DCF") model, and a multi-stage growth DCF model.

The Company's witness stated that he had no quarrel with the market-approach methodologies Staff used in coming to its cost of capital recommendations, but that an adjustment should be made to Staff's calculations to account for the fact that Pineview is a smaller company than the large investor-owned utilities that Staff used in its study (Tr. at 26). Pineview states that its rate request in this proceeding is based on debt coverage ratios and not upon rate base/rate of return ratemaking (Co. Br. at 5). Pineview states that it did not conduct a cost of equity study because it is not seeking equity funds, but that it instead conducted the type of analysis that WIFA would conduct in determining the amount of capital required to meet WIFA's debt coverage requirements, and has asked for an operating income based upon WIFA's mandated debt service coverages (Co. Br. at 12, 16). Staff's witness testified that using only future debt coverage to determine a utility's operating income does not constitute sound financial practice as it disregards the actual cost of equity (Tr. at 281-282). We agree that this is correct for Class C and larger utilities. He further explained that even if hypothetical debt were to be considered, that as the amount of debt increases, a company's capital structure

changes, and because debt costs less than equity, the increased amount of debt in the capital structure offsets any increase in financial risk that might increase the cost of equity, such that the overall cost of capital remains about the same (Tr. at 284-285 and 321-322).

The Company argues that it cannot obtain the WIFA loan for which it is seeking approval without the revenue levels it requests in its rate application (Co. Br. at 13). Staff points out, however, that its recommended cost of capital and rate of return provides a times interest earned ratio ('TIER') to cover the amount of debt for which Staff is recommending approval (Tr. at 283, 341), and that in any event the TIER does not take into account the effect of noncash expenses like depreciation, which leave additional cash available to Pineview to cover contingencies (Tr. at 341-342). We find Staff's approach to be a sound, reasonable and fair methodology for determining Pineview's cost of capital, and we determine the Company's weighted average cost of capital to be 7.20 percent.

Cost of Capital Summary

	Percentage	Cost	Weighted Cost
Long-Term Debt	49.0%	5.43%	2.7%
Common Equity	51.0%	8.9%	4.5%
Cost of Capital			**7.2%**

4. Rate of Return/Revenue Requirement/Authorized Increase

The Company did not submit RCND schedules, so the 7.20 percent weighted average cost of capital determined herein translates into a 7.20 percent fair value rate of return on FVRB of $663,243 as authorized hereinabove. Multiplying the 7.20 percent rate of return by the FVRB produces required operating income of $47,753. This is $25,742 more than the Company's test year adjusted operating income of $22,012. Multiplying the deficiency by the gross revenue conversion factor of 1.26459 results in a required increase in revenues of $32,553, for a revenue requirement of $555,277, a 6.23 percent net increase over adjusted test year revenues of $522,724.

5. Rate Design

The Company's present rate design consists of a single tier commodity rate. In its application, the Company proposed a three-tier rate design. Pineview states that its proposed first-tier minimum monthly rate varies by meter size to recognize the difference in customer classes, and sends the appropriate pricing signals to the customers (Co. Br. at 15). Staff also recommends a three-tier rate

design with breakover points that differ from the Company's proposal.

The Company requests that Staff's proposed first-tier range be adjusted so that customers do not receive a rate reduction as a result of a revenue increase (Co. Br. at 15). Staff's proposed rate design is consistent with recent Staff recommendations. It provides a reduced rate for the first 3,000 gallons, and promotes conservation at higher usage levels. In response to the Company's argument that its rate design results in a reduction to the median bill, Staff responds that the slight decrease is offset by the substantial increase given to high use customers (Staff Br. at 10). Staff argues that when three-tiered rates are first implemented, the rate impact will vary by consumption levels, and that this sometimes will result in rate reductions for some consumption levels, but that the most important point of the three-tiered rate design is that beyond the first tier, the rate structure will send an appropriate price signal to customers, resulting in conservation over the long term (*Id.*). We agree with Staff's that its proposed rate structure will send an appropriate price signal to customers, and will result in conservation over the long term. We will therefore adopt Staff's proposed rate design, adjusted to produce the approved level of revenues. We note that the rate design approved herein does not result in a reduction to the median 5/8-inch customer bill.

6. <u>Other Staff Recommendations</u>

Staff recommends that Pineview be ordered to use the individual depreciation rates as shown in Exhibit 6 attached to hearing Exhibit S-13. In addition, Staff recommends that the Company be ordered to include a provision in its tariff to allow for the flow-through of all appropriate state and local taxes as provided for in A.A.C. R14-2-409(D)(5).

Staff recommends that the Commission order Pineview to cease and desist from further commingling of Company expenses and capital equipment with non-Company business. Staff further recommends that the Commission order 1) mandatory training for equipment operators; 2) a requirement for Commission approval of all further transactions with affiliates or members of the Sutter family; 3) maintenance of written usage reports for the Company's Transportation and Power Operated Equipment (NARUC USOA Accounts 341 and 345, respectively), to include the date, time of use or mileage and the purpose of the equipment usage; and 4) the filing of a new rate case within three years of this Decision (Exh. S-14 at 16). Based on the evidence presented in this proceeding,

we find these Staff recommendations to be reasonable and necessary and will adopt them. We will also institute further requirements with the aim of preventing any further use of ratepayer revenue for improper purposes.

* * * * * * * * * *

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

FINDINGS OF FACT

1. Pineview is an Arizona public service corporation providing water utility service within Navajo County, Arizona pursuant to authority granted by the Commission in Decision No. 32007 (December 28, 1959).

2. Pineview serves an area consisting of approximately four square miles located southeast of the Town of Show Low in Navajo County, Arizona.

3. The Company changed its name from Pineview Land and Water Company, Inc. to Pineview Water Company, Inc. on May 28, 1998.

4. On June 18, 2004, Pineview filed the above-captioned financing application.

5. Also on June 18, 2004, Pineview filed an application for approval of an off-site facilities hook-up fee tariff, which was approved as amended in Decision No. 67275 (October 5, 2004).

6. On July 9, 2004, Pineview filed the above-captioned rate application.

7. On July 15, 2004, Pineview filed an Affidavit of Publication certifying that it caused notice of the financing application to be published in the *White Mountain Independent* on July 2, 2004.

8. On August 9, 2004, Staff filed a letter informing the Company that its rate application had not met the Commission's sufficiency requirements.

9. On August 20, 2004, Pineview filed an amendment to its rate application.

10. On September 7, 2004, Staff filed a letter indicating the Company's rate application was sufficient, and classifying the Company as a Class C utility.

11. By Procedural Order issued September 13, 2004, a hearing on the application was

scheduled for March 7, 2005. On October 1, 2004, the Company filed a request to reschedule the hearing date due to unavailability of counsel. By Procedural Order of October 5, 2004, the hearing date was rescheduled to commence on February 24, 2005, and procedural deadlines were reset accordingly.

12. Pineview caused a Notice of Hearing on its application to be mailed to all of its customers by First Class U.S. Mail on October 18, 2004.

13. By Procedural Orders issued November 15, 2004, and December 10, 2004, intervention was granted to Thomas R. Cooper and Dan E. Simpson. No other intervention requests were filed.

14. Public comment letters in opposition to the requested rate increase were filed in the docket on November 9, 2004, November 15, 2004, and November 24, 2004.

15. By Procedural Order issued January 12, 2005, the request of Staff and the Company to consolidate the above-captioned financing application with the rate application was granted.

16. On February 24, February 25, and March 3, 2005, a full public hearing was held as scheduled before a duly authorized Administrative Law Judge of the Commission at the Commission's offices in Phoenix, Arizona. The Company and Staff appeared through counsel and presented evidence. Intervenor Dan E. Simpson entered an appearance, but chose to make public comment in lieu of providing sworn testimony. No other members of the public appeared to provide public comment at the hearing. Following the hearing and the filing of simultaneous closing briefs on April 8, 2005, the consolidated matters were taken under advisement pending submission of a Recommended Opinion and Order to the Commission.

17. The number of contested issues, the length of the hearing, and the number of exhibits admitted to the record in this proceeding constitute an extraordinary event for a Class C utility. At the close of the hearing, the timeclock in this matter was therefore extended pursuant to A.A.C. R14-2-103(B)(11)(e) in order to allow time for the Company and Staff to file closing briefs in lieu of making closing statements. The Company and Staff filed simultaneous closing briefs on April 8, 2005.

18. On April 15, 2005, a public comment letter in support of the requested rate increase

was filed.

19. On April 22, 2005, Pineview docketed an Affidavit.

20. On April 27, 2005, Staff filed a Response to Pineview's Late-Filed Affidavit.

21. Pineview's present rates and charges produced adjusted test year operating revenues of $522,724 and adjusted operating expenses of $500,712 resulting in an operating income of $22,012 during the test year ended December 31, 2003.

22. Average and median usage during the test year were 5,277 and 3,250 gallons per month, respectively, for 5/8' inch meter customers, which comprise the majority of Pineview's customers.

23. The rates and charges for Pineview at present, as proposed in the rate application, and as recommended by Staff are as follows:

	Present Rates	Proposed Rates Company	Proposed Rates Staff
MONTHLY USAGE CHARGE:			
5/8'x ¾'Meter	$ 17.00	$ 21.25	$ 16.75
¾'Meter	24.14	30.25	26.00
1"Meter	42.27	53.00	45.00
1 ½'Meter	82.49	103.00	86.00
2'Meter	130.76	163.00	132.00
3'Meter	241.35	300.00	255.00
4'Meter	402.25	500.00	418.75
6'Meter	804.50	1,000.00	837.50
8'Meter	1,206.75	1,500.00	1,675.00
10'Meter	1,609.00	2,000.00	2,512.50
Gallons Included in Minimum	0	0	0
Commodity Rates per 1,000 Gallons			
5/8'x 3/4'Meter			
0 to 5,000 Gallons	3.26	3.78	N/A
0 to 3,000 Gallons	3.26	N/A	3.10
5,001 to 20,000 Gallons	3.26	4.10	N/A
3,001 to 20,000 Gallons	3.26	N/A	3.66
Over 20,000 Gallons	3.26	4.50	4.20
3/4'Meter			
0 to 10,000 Gallons	3.26	3.78	N/A
0 to 3,000 Gallons	3.26	N/A	3.10
10,001 to 40,000 Gallons	3.26	4.10	N/A

3,001 to 20,000 Gallons	3.26	N/A	3.66
Over 40,000 Gallons	3.26	4.50	N/A
Over 20,000 Gallons	3.26	N/A	4.20
<u>1"Meter</u>			
0 to 20,000 Gallons	3.26	3.78	N/A
0 to 30,000 Gallons	3.26	N/A	3.10
20,001 to 80,000 Gallons	3.26	4.10	N/A
30,001 to 75,000 Gallons	3.26	N/A	3.66
Over 80,000 Gallons	3.26	4.50	N/A
Over 75,000 Gallons	3.26	N/A	4.20
<u>1 1/2"Meter</u>			
0 to 20,000 Gallons	3.26	3.78	N/A
0 to 50,000 Gallons	3.26	N/A	3.10
20,001 to 80,000 Gallons	3.26	4.10	N/A
50,001 to 100,000 Gallons	3.26	N/A	3.66
Over 80,000 Gallons	3.26	4.50	N/A
Over 100,000 Gallons	3.26	N/A	4.20
<u>2"Meter</u>			
0 to 60,000 Gallons	3.26	3.78	N/A
0 to 120,000 Gallons	3.26	N/A	3.10
60,001 to 200,000 Gallons	3.26	4.10	N/A
120,001 to 200,000 Gallons	3.26	N/A	3.66
Over 200,000 Gallons	3.26	4.50	4.20
<u>3"Meter</u>			
0 to 100,000 Gallons	3.26	3.78	N/A
0 to 150,000 Gallons	3.26	N/A	3.10
100,001 to 400,000 Gallons	3.26	4.10	N/A
150,001 to 250,000 Gallons	3.26	N/A	3.66
Over 400,000 Gallons	3.26	4.50	N/A
Over 250,000 Gallons	3.26	N/A	4.20
<u>4"Meter</u>			
0 to 200,000 Gallons	3.26	3.78	N/A
0 to 150,000 Gallons	3.26	N/A	3.10
200,001 to 600,000 Gallons	3.26	4.10	N/A
150,001 to 250,000 Gallons	3.26	N/A	3.66
Over 600,000 Gallons	3.26	4.50	N/A
Over 250,000 Gallons	3.26	N/A	4.20
<u>6"Meter</u>			
0 to 700,000 Gallons	3.26	3.78	N/A
0 to 150,000 Gallons	3.26	N/A	3.10
700,001 to 2,000,000 Gallons	3.26	4.10	N/A
150,001 to 250,000 Gallons	3.26	N/A	3.66

Over 2,000,000 Gallons	3.26	4.50	N/A
Over 250,000 Gallons	3.26	N/A	4.20
8'Meter			
0 to 1,000,000 Gallons	3.26	3.78	N/A
0 to 150,000 Gallons	3.26	N/A	3.10
1,000,001 to 3,000,000 Gallons	3.26	4.10	N/A
150,001 to 250,000 Gallons	3.26	N/A	3.66
Over 3,000,000 Gallons	3.26	4.50	N/A
Over 250,000 Gallons	3.26	N/A	4.20
10'Meter			
0 to 2,000,000 Gallons	3.26	3.78	N/A
0 to 150,000 Gallons	3.26	N/A	3.10
2,000,001 to 5,000,000 Gallons	3.26	4.10	N/A
150,001 to 250,000 Gallons	3.26	N/A	3.66
Over 5,000,000 Gallons	3.26	4.50	N/A
Over 250,000 Gallons	3.26	N/A	4.20
Construction Water–All Usage per 1,000 Gallons	3.26	4.75	4.75

SERVICE LINE AND METER INSTALLATION CHARGES:
(Refundable pursuant to A.A.C. R14-2-405)

5/8'x ¾'Meter	$ 400.00	$ 475.00	$ 475.00
¾'Meter	440.00	550.00	550.00
1'Meter	500.00	650.00	650.00
1 ½'Meter	715.00	900.00	900.00
2'Meter (Turbine)	1,170.00	1,550.00	1,550.00
2'Meter (Compound)	1,700.00	2,300.00	2,300.00
3'Meter (Turbine)	1,585.00	2,200.00	2,200.00
3'Meter (Compound)	2,190.00	3,100.00	3,100.00
4'Meter (Turbine)	2,540.00	3,400.00	3,600.00
4'Meter (Compound)	3,215.00	4,400.00	4,400.00
6'Meter (Turbine)	4,615.00	6,200.00	6,200.00
6'Meter (Compound)	6,270.00	7,900.00	7,900.00
8'Meter (Turbine)	6,655.00	8,850.00	7,543.00
8'Meter (Compound)	7,040.00	9,350.00	7,980.00
10'Meter (Turbine)	8,495.00	11,300.00	9,629.00
10'Meter (Compound)	9,950.00	13,200.00	11,278.00
Service Charges:			
Establishment–Regular Hours	$20.00	$25.00	$20.00
Establishment–(After Hours)	35.00	50.00	35.00
Re-Establishment Fee (Within 12 Months)	*	*	*

Re-Connection of Service–Regular Hours	15.00	50.00	15.00
Re-Connection of Service–After Hours	NR (1)	75.00	30.00
Water Meter Test–If Correct	20.00	Cost (2)	20.00
Water Meter Relocation at Customer Request	NR (1)	Cost (2)	Cost (2)
Meter Re-read–if Correct	15.00	No Charge	No Charge
NSF Check Charge	15.00	25.00	15.00
Late Charge	1.5%	1.5%	1.5%
Deferred Payment (Per Month)	1.5%	1.5%	1.5%
Service Calls–Regular Hours	No Charge	No Charge	No Charge
Service Calls–After Hours	NR (1)	50.00	25.00
Deposits Requirements	**	**	**
Deposit Interest	**	**	**

* Months off system times the monthly minimum per Commission rule A.A.C. R14-2-403(D).

** Per Commission rule A.A.C. R14-2-403(B).

Notes:

(1) No Currently Approved Rate

(2) Cost Includes Materials, Labor and Overheads

24. Pineview's OCRB is determined to be $663,243. Pineview did not file RCND schedules. Pineview's FVRB is therefore determined to be $663,243.

25. Total adjusted test year operating expenses were $507,523.

26. With the adjustments adopted herein, Pineview's adjusted test year operating income was $22,012, for a 3.32 percent rate of return on FVRB of $663,243.

27. Pineview's proposed revenue requirement of $649,177 would result in an annual increase in operating revenues of $126,453 or 24.19 percent over test year revenues of $522,724.

28. Staff's proposed revenue requirement of $538,219 would result in an annual increase in operating revenues of $15,495 or 2.96 percent over test year revenues of $522,724.

29. The revenue requirement of $555,277 adopted herein will result in an annual increase in operating revenues of $32,553 or 6.23 percent over test year revenues of $522,724.

30. Although the majority of Staff's adjustments are adopted in this case, the revenue requirement we adopt is higher than that recommended by Staff, and consequently the rates are slightly higher than those recommended by Staff. Although this difference is attributable in part to an increase in $1,150 in rate base owing to our inclusion of the newer backhoe in plant, it is mainly due

to a net increase of $16,975 in expenses. We have allowed approximately $664 in test year repair and maintenance expenses on the newer backhoe. To comport with our requirement that the Company file a rate application in three years instead of five, the amortization of rate case expense over three years increased expenses by $6,400. In addition, a $9,951 correction in the calculation of property tax expense was made.

31. Pineview's weighted average cost of capital is determined to be 7.20 percent. The Company did not submit RCND schedules, so the 7.20 percent weighted average cost of capital translates into a 7.20 percent fair value rate of return on FVRB of $663,243 as authorized hereinabove. Multiplying the 7.20 percent rate of return by the FVRB produces required operating income of $47,753. This is $25,742 more than the Company's test year adjusted operating income of $22,012. Multiplying the deficiency by the gross revenue conversion factor of 1.26459 results in a required increase in revenues of $32,553, for a revenue requirement of $555,277, a 6.23 percent net increase over test year adjusted revenues of $522,724.

32. Pineview's proposed rate schedule in its rate application would have increased the median 5/8'meter customer's bill by 21.5 percent from $27.60 per month to $33.54 per month, and the average 5/8'meter bill by 20.7 percent from $34.20 per month to $41.29 per month.

33. Staff's proposed rate schedule would have reduced the median 5/8'meter customer's bill by 2.3 percent from $27.60 per month to $26.97 per month, and increased the average 5/8'meter bill by 0.5 percent from $34.20 per month to $34.38 per month.

34. The rate schedule adopted herein will increase the median 5/8'meter customer's bill by 2.0 percent from $27.60 per month to $28.15 per month, and the average 5/8'meter bill by 4.0 percent from $34.20 per month to $35.56 per month.

35. The rate design adopted herein is fair and reasonable.

36. Pineview's water system consists of four wells, three storage tanks having a total storage capacity of 540,000 gallons, three pressure tanks and a distribution system serving approximately 936 connections. According to Staff, the existing system has adequate capacity to serve an additional 280 customers.

37. Pineview's financing application requests authority to issue long-term notes and other

evidences of indebtedness in the original amount not to exceed $730,978 from WIFA at a term of twenty years at a rate of 4.20 percent for the purpose of financing construction of an additional well at an estimated cost of $271,459, a two million gallon storage tank at an estimated cost of $304,150, and a 12-inch transmission line at an estimated cost of $155,369. Pineview's application also requests authority to utilize loan funds for operating expenses or income.

38. Staff reviewed the projects proposed by the Company and recommends financing approval in the amount of $577,578. Staff's recommendation includes funding for the projected cost of a one million gallon storage tank in lieu of a two million gallon storage tank, and excludes $54,000 in financing for land for a future wellsite. Staff recommends denial of Pineview's request to utilize loan funds for operating expenses or income.

39. Staff recommends that the Commission order Pineview to file a new rate case within three years of this Decision.

40. Staff recommends that Pineview be ordered to use the individual depreciation rates as shown in Exhibit 6 attached to hearing Exhibit S-13.

41. Staff recommends that the Company be ordered to include a provision in its tariff to allow for the flow-through of all appropriate state and local taxes as provided for in A.A.C. R14-2-409(D)(5).

42. Staff recommends that the Commission order Pineview to cease and desist from further commingling of Company expenses and capital equipment with non-Company business. In addition, Staff recommends that the Company be ordered to:

(a) keep all its expense information in accordance with the National Association of Regulatory Utility Commissioners' ("NARUC") Uniform System of Accounts ("USOA");

(b) file an affidavit within 120 days of this Decision attesting that its accounting system has been updated to comply with the NARUC USOA;

(c) obtain Commission pre-approval of all future transactions with affiliates or members of the Sutter family;

(d) maintain written usage reports for the Company's Transportation and Power Operated Equipment (NARUC USOA Accounts 341 and 345, respectively), to include

the date, time of use or mileage and the purpose of the equipment usage; and to

(e) institute mandatory training for the Company's equipment operators on the maintenance of the above-described written usage reports.

43. Based on the evidence presented in this proceeding, Staff's recommendations set forth in Findings of Fact No. 38-42 are reasonable and should be adopted. In addition to the institution of mandatory training for the Company's equipment operators on the maintenance of equipment usage reports, we will also require the Company to institute mandatory training for all its employees in order to make clear to its employees the necessity of a strict prohibition of payment of any non-Pineview Water Company, Inc. expenses from water utility revenues. To ensure that the training program is implemented as soon as possible, we will require the Company to make a compliance filing within 30 days of this Decision, for Staff approval, detailing its plan to institute the mandatory employee training on the maintenance of the above-ordered written usage reports and on the necessity of a strict prohibition of payment of any non-Pineview Water Company, Inc. expenses from water utility revenues, and will require Staff to follow up on the Company's implementation of the approved plan and notify the Commission in the event the plan is not followed. Finally, with the goal of preventing any further improper use of ratepayer revenue, we will also require the Company to submit for Staff review, before March 31, 2007, all information identified in A.A.C. R14-2-103 describing the Company's business activities in calendar year 2006, except RCN information and Schedules F., G and H.

44. In its analysis of the Company's next rate filing, Staff should bring to the attention of the Commission any expenses and plant additions in the Company's books and records that cannot be clearly demonstrated to be for the sole benefit of the Company in its provision of water utility service to the public.

45. In its review of the Company's business information for calendar year 2006, Staff should evaluate the extent to which the Company's expenses and plant additions are for the sole benefit of the Company in its provision of water utility service to the public and the Company is complying with all other requirements of this Decision. As appropriate to the results of its review, Staff shall make recommendations to the Commission regarding the need for Commission action

before the Company's next rate filing.

46. According to Staff's Compliance Section, the Company has no outstanding compliance filing issues with the Commission.

47. At the time of the hearing Pineview was current with its property taxes.

48. Staff states that the Arizona Department of Environmental Quality ("ADEQ") has determined that the Company is currently delivering water that meets the water quality standards required by Title 18, Chapter 4 of the Arizona Administrative Code.

49. The Staff Report states that the most recent lab analysis by the Company indicated that the arsenic levels in the Company's supply are below the new federal arsenic maximum contaminant level ("MCL") that becomes effective January 23, 2006.

50. The Company is not located in any Arizona Department of Water Resources ("ADWR") Active Management Area ("AMA").

CONCLUSIONS OF LAW

1. Pineview is a public service corporation within the meaning of Article 15 of the Arizona Constitution and A.R.S. §§ 40-250, 40-251, and 40-302.

2. The Commission has jurisdiction over Pineview and the subject matter of this proceeding.

3. Notice of the applications was provided in the manner prescribed by law.

4. The rates and charges approved herein are just and reasonable.

5. Staff's recommendations as set forth in Findings of Fact No. 38-42 above are reasonable and should be adopted.

6. The additional requirements described in Findings of Fact No. 43 are reasonable based on the evidence in this proceeding.

7. The financing approved herein is for lawful purposes with Pineview's corporate powers, is compatible with the public interest, with sound financial practices and with the proper performance by Pineview as a public service corporation, and will not impair Pineview's ability to perform that service.

8. The financing approved herein is for the purposes stated in the application as

recommended by Staff, is reasonably necessary for those purposes, and such purposes are not wholly or in part reasonably chargeable to operating expenses or to income.

ORDER

IT IS THEREFORE ORDERED that Pineview Water Company, Inc. is hereby directed to file on or before July 29, 2005, a revised tariff schedule setting forth the following rates and charges:

MONTHLY USAGE CHARGE:	Rates
5/8'x ¾'Meter	$ 17.93
¾'Meter	27.00
1'Meter	49.00
1 ½'Meter	92.00
2'Meter	145.00
3'Meter	285.00
4'Meter	448.25
6'Meter	896.50
8'Meter	1,793.00
10'Meter	2,689.50

Commodity Rates per 1,000 Gallons

5/8'x 3/4'Meter	
0 to 3,000 Gallons	3.10
3,001 to 20,000 Gallons	3.66
Over 20,000 Gallons	4.20
3/4'Meter	
0 to 3,000 Gallons	3.10
3,001 to 20,000 Gallons	3.66
Over 20,000 Gallons	4.20
1'Meter	
0 to 30,000 Gallons	3.10
30,001 to 75,000 Gallons	3.66
Over 75,000 Gallons	4.20
1 1/2'Meter	
0 to 50,000 Gallons	3.10
50,001 to 100,000 Gallons	3.66
Over 100,000 Gallons	4.20
2'Meter	
0 to 120,000 Gallons	3.10
120,001 to 200,000 Gallons	3.66
Over 200,000 Gallons	4.20

3'Meter	
0 to 150,000 Gallons	3.10
150,001 to 250,000 Gallons	3.66
Over 250,000 Gallons	4.20
4'Meter	
0 to 150,000 Gallons	3.10
150,001 to 250,000 Gallons	3.66
Over 250,000 Gallons	4.20
6'Meter	
0 to 150,000 Gallons	3.10
150,001 to 250,000 Gallons	3.66
Over 250,000 Gallons	4.20
8'Meter	
0 to 150,000 Gallons	3.10
150,001 to 250,000 Gallons	3.66
Over 250,000 Gallons	4.20
10'Meter	
0 to 150,000 Gallons	3.10
150,001 to 250,000 Gallons	3.66
Over 250,000 Gallons	4.20
Construction Water–All Usage per 1,000 Gallons	4.75

SERVICE LINE AND METER INSTALLATION CHARGES
(Refundable pursuant to A.A.C. R14-2-405)

5/8'x ¾'Meter	$ 475.00
¾'Meter	550.00
1'Meter	650.00
1 ½'Meter	900.00
2'Meter (Turbine)	1,550.00
2'Meter (Compound)	2,300.00
3'Meter (Turbine)	2,200.00
3'Meter (Compound)	3,100.00
4'Meter (Turbine)	3,600.00
4'Meter (Compound)	4,400.00
6'Meter (Turbine)	6,200.00
6'Meter (Compound)	7,900.00
8'Meter (Turbine)	7,543.00
8'Meter (Compound)	7,980.00
10'Meter (Turbine)	9,629.00

10' Meter (Compound)	11,278.00

Service Charges:

Establishment–Regular Hours	$20.00
Establishment–(After Hours)	35.00
Re-Establishment Fee (Within 12 Months)	*
Re-Connection of Service–Regular Hours	15.00
Re-Connection of Service–After Hours	30.00
Water Meter Test–If Correct	20.00
Water Meter Relocation at Customer Request	Cost (1)
Meter Re-read–if Correct	No Charge
NSF Check Charge	15.00
Late Charge	1.5%
Deferred Payment Finance Charge	1.5%
Service Calls–Regular Hours	No Charge
Service Calls–After Hours	25.00
Deposits Requirements	**
Deposit Interest	**

MONTHLY SERVICE CHARGE FOR FIRE SPRINKLERS

4' or Smaller	***
6'	***
8'	***
10'	***
Larger than 10'	***

* Months off system times the monthly minimum per Commission rule A.A.C. R14-2-403(D).

** Per Commission rule A.A.C. R14-2-403(B).

*** 1% of Monthly Minimum for a comparable sized meter connection, but no less than $5.00 per month. The service charge for fire sprinklers is only applicable for service lines separate and district from the primary water service line.

Notes:

(1) Cost Includes Materials, Labor and Overheads

IT IS FURTHER ORDERED that the above rates and charges shall be effective for all service provided to customers on and after August 1, 2005.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall include a provision in its tariff to allow for the flow-through of all appropriate state and local taxes as provided for in A.A.C. R14-2-409(D)(5).

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall notify its customers of the rates and charges authorized herein and the effective date of same by means of an insert in its next regular monthly billing, which insert shall have been reviewed and approved by the Commission's Utilities Division Staff, and shall file a copy of the notice with the Commission's Docket Control Center within 60 days.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. is authorized to issue up to $577,578 in long term debt from the Arizona Water Infrastructure Financing Authority for a term not to exceed twenty years and at an interest rate not to exceed 4.20 percent for the purposes of funding those expenses identified in Findings of Fact No. 38 above.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. is hereby authorized to engage in any transaction and to execute any documents necessary to effectuate the authorization granted hereinabove.

IT IS FURTHER ORDERED that such authority shall be expressly contingent upon Pineview Water Company, Inc.'s use of the proceeds for the purposes set forth in Findings of Fact No. 38 above.

IT IS FURTHER ORDERED that approval of the financing set forth hereinabove does not constitute or imply approval or disapproval by the Commission of any particular expenditure of the proceeds derived thereby for purposes of establishing just and reasonable rates.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall use the individual depreciation rates as shown in Exhibit 6 attached to hearing Exhibit S-13.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall cease and desist from commingling its expenses and capital equipment with any non-Pineview Water Company, Inc. business.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall immediately begin keeping all its expense information in accordance with the National Association of Regulatory Utility Commissioners' Uniform System of Accounts.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall file an affidavit within 120 days of this Decision attesting that its accounting system has been updated to comply with the

National Association of Regulatory Utility Commissioners' Uniform System of Accounts.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall obtain Commission pre-approval of all future transactions with affiliates or members of the Sutter family.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall maintain written usage reports for its Transportation and Power Operated Equipment, to include the date, time of use, mileage and the purpose of the equipment usage.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall institute mandatory training for its equipment operators on the maintenance of the above-ordered written usage reports.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall institute mandatory training for all its employees in order to make clear to its employees the necessity of a strict prohibition of payment of any non-Pineview Water Company, Inc. expenses from water utility revenues.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall make a compliance filing within 30 days of this Decision, for Staff approval, detailing its plan to institute the mandatory employee training on the maintenance of the above-ordered written usage reports and on the necessity of a strict prohibition of payment of any non-Pineview Water Company, Inc. expenses from water utility revenues.

IT IS FURTHER ORDERED that Staff shall examine and follow up on the Company's approved mandatory training program and shall notify the Commission immediately in the event it learns that the program is not strictly followed.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall file a rate case within three years of this Decision.

IT IS FURTHER ORDERED that in its analysis of the next rate case application, Staff shall bring to the attention of the Commission any expenses and plant items in the Pineview Water Company, Inc.'s books and records that cannot be clearly demonstrated to be for the sole benefit of Pineview Water Company, Inc. in its provision of water utility service to the public.

IT IS FURTHER ORDERED that Pineview Water Company, Inc. shall submit for Staff review, before March 31, 2007, all information identified in A.A.C. R14-2-103 describing the

Company's business activities in calendar year 2006, except RCN information and Schedules F, G and H.

IT IS FURTHER ORDERED that in its review of the Company's 2006 business information, Staff shall evaluate the extent to which the Company's expenses and plant additions are for the sole benefit of the Company in its provision of water utility service to the public and the Company is complying with all other requirements of this Decision. As appropriate to the results of its review, Staff shall make a recommendation to the Commission regarding the need for Commission action before the Company's next filing.

IT IS FURTHER ORDERED that Staff shall investigate Pineview Water Company, Inc.'s use of the hook-up fees authorized in Decision No. 67275 and report its findings to the Commission within 60 days.

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

BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

CHAIRMAN

COMMISSIONER

COMMISSIONER

COMMISSIONER

COMMISSIONER

IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive Secretary of the Arizona Corporation Commission, have hereunto set my hand and caused the official seal of the Commission to be affixed at the Capitol, in the City of Phoenix, this 18th day of July, 2005.

BRIAN C. McNEIL
EXECUTIVE SECRETARY

DISSENT _____

DISSENT _____

SERVICE LIST FOR: PINEVIEW WATER COMPANY, INC.

DOCKET NOS.: W-01676A-04-0463 and W-01676A-04-0500

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