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MEMORANDUM
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TO: Docket Control Center

2009 JAN 28 P 4:40

FROM: Ernest G. Johnson
Director
Utilities Division

AZ CORP COMMISSION
DOCKET CONTROL

DATE: January 28, 2009

RE: PINE WATER COMPANY - REQUEST FOR MODIFICATION OF RATE CASE
DECISION NO. 67166 (DOCKET NO. W-03512A-03-0279)

In Decision No. 70559 ("the rate case Decision"), dated August 11, 2004, the Arizona Corporation Commission ("Commission") approved the application of Pine Water Company ("Pine") for a rate increase. The case was resolved by a settlement agreement among Pine, the Pine-Strawberry Water Improvement District ("the District"), Commission Staff and an intervenor. The Decision adopted the rates agreed upon in the settlement agreement but added a requirement that Pine file another rate case no later than June 1, 2008. On February 27, 2008, Pine requested the Commission extend the rate case deadline to June 1, 2009. Decision No. 70452, dated August 6, 2008, approved that request. On December 15, 2008, Pine filed a motion to modify the rate case Decision vacating any requirement that it file a rate case.

Background

Since the issuance of the rate case Decision in 2004, Pine has been the subject of several dockets regarding customer complaints and regarding the wishes of customers to have their properties deleted from Pine's certificated area. These dockets revolve around the availability of water and Pine's efforts to find water to serve new developments. An additional docket, Docket No. W-03512A-07-0362 ("the financing application"), requested approval of an encumbrance of Pine's assets as part of a Joint Well Development Agreement between Pine and the District whereby Pine would develop the K-2 well. Most of these dockets remain open and have not been resolved. On November 24, 2008, Pine filed a Notice of Withdrawal of the financing application.

A Status Report was filed by Pine on December 12, 2008, in the financing docket which indicated that the District had terminated the Joint Well Development Agreement, that Pine had filed arbitration claims against the District for breach of the agreement, and that the District had filed a condemnation complaint against Pine in Gila County Superior Court.

At the December 16, 2008 Open Meeting, the Commission denied Pine's request to withdraw the financing application. The Commission also stayed the proceeding until further order and required status reports every three months regarding the condemnation action, the pending arbitration and any other pertinent information.

Arizona Corporation Commission

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Pine's Financial Health

Staff reviewed Pine's 2007 Annual Report to the Commission. At December 31, 2007, Pine was operating at a net loss of \$172,454. Its capital structure was comprised of \$783,000 of payables to its parent, \$342,473 of contributions and negative equity of \$130,879. With the caveat that the annual report is not an audited financial statement, from these accounts alone it can be seen that Pine's financial health is less than ideal. Furthermore, due to limited water resources, Pine is currently operating under a Commission-ordered moratorium on hook-ups and is unable to look to customer growth to increase revenues. However, Pine has represented that its parent has not charged interest on the payables and will wait for repayment until the outcome of the arbitration and condemnation proceedings.

Recommendation

Staff recommends that the Commission deny Pine's request to vacate the requirement to file a rate case by June 1, 2009, and instead, order that the date for the rate case filing be extended to June 1, 2010, using a 2009 test year. Maintaining the currently required June 1, 2009 filing date could be burdensome to Pine. Although Staff is concerned about its financial health, Pine's management's plate is currently full. The arbitration and/or condemnation proceedings will be expensive and the cost of a rate case might be prohibitive under Pine's current financial circumstance. Also, a rate case filed in June 2009 could effect the outcome of the condemnation proceeding or a settlement of the condemnation by increasing or decreasing the value of Pine. In addition, if the K-2 well is ultimately installed, the impact on Pine's rate base would be large enough to necessitate a rate case possibly resulting in overlapping rate cases. Finally, if condemnation by the District is successful, the rate case could be moot because the District would set rates to District customers reflecting the District's costs, not Pine's.

The arbitration and condemnation proceedings are likely to be lengthy and if Pine's financial health does not improve, a rate case may be necessary before the resolution of the arbitration and condemnation proceedings. Therefore, Staff further recommends that a time extension beyond June 10, 2010, not be granted.

SERVICE LIST FOR: PINE WATER COMPANY
DOCKET NO. W-03512A-03-0279

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