

## Questions relating to Suncadia Water tariff Docket No. UW-081226 – 10/24/2008

In reviewing the materials relating to Suncadia Water Company's request to the WUTC in Docket No. UW-081226 and the detail supplied by the Suncadia consultant, residential owners at Suncadia have put forth a number of questions to the WUTC staff and Suncadia Water dating back to June 2008. Some of those questions that we believe would have a material impact on either the base rate or the consumption rate have not been responded to. Additionally, we have not seen nor received any information or supporting details to show that the WUTC Staff's review of the company's operations and financial records show that the new rates are justified. The WUTC staff concluded that the July filing lacked this justification and the current filing is not materially different from what we have been able to determine.

We have broken the questions down into the following general categories and subcategories. As detailed below, the questions fall generally into the following categories:

### Base Rate

- Affiliated interest transactions
- Allocation of costs between irrigation and domestic systems

### Consumption Rate

- Affiliated interest transactions
- Flat rate versus conservation rate

### General Concerns & Conclusions

### BASE RATE

The residential customers of Suncadia Water oppose the base rates as filed on the following points:

- The allowable return on investment is recovery of capital and debt that was not disclosed as part of the residential property purchase.
- The operating expenses have been disproportionately applied to the potable water system versus the irrigation water system. The irrigation water system is only used by the Developer, an affiliated interest.
- The commercial properties of the Developer have not paid for water for the past 2+ years while residential customers have paid a flat rate. This is not factored into the commercial rates and potentially impacts the base rate costs.

<b>BASE RATE DETAILS</b>	<b>BASE COSTS</b>	<b>BASE RATE</b>
Allowable return on invest.	\$ 72,805	\$ 13.90
Operating Expenses & Fixed Costs	\$ 131,815	\$ 25.16
<b>TOTAL</b>	<b>\$ 204,620</b>	<b>\$ 39.06</b>

<b>BASE RATE FIRE PROT. DETAILS</b>	<b>BASE COSTS</b>	<b>BASE RATE</b>
Allowable return on invest.	\$ 21,032	\$ 2.86
Operating Expenses & Fixed Costs	\$ 5,927	\$ .81
<b>TOTAL</b>	\$ 26,959	\$ 3.67

**Affiliated Interest Transactions**

Per the information filed and docket #081636 Suncadia, LLC (“Developer”) and Suncadia Water Company, LLC (“Suncadia Water”) are affiliated interests within the meaning of RCW 80.16.010. Thus, the burden of proof is on Suncadia Water to show that their current flat rate of \$35 for single family residences is insufficient to sustain the water system and that their proposed new rate is reasonable. The base rate is based on 436.6 equivalent residential units (ERUs). The information from the Suncadia Water consultant shows that there were 160 customers as of August 2008, yet all of the ERU calculations still use 125.

1. Suncadia Water seeks to recover capital and debt costs through its base residential water rate. We do not disagree with this being included in the commercial property rates since these are owned and operated by the Developer. This residential water system cost recovery was not disclosed at the time of purchase to the residential property owners. Property owners assumed that they paid for the costs of the water system in the same way that the cost of other utility infrastructures (electricity, gas, network, etc.) were included in the purchase price of their property. Copies of HUD Property Report and Washington Public Offering Statement from the sales agreement paperwork from Thomas Miller, Suncadia residential single-family lot owner have been provided. Note that the HUD report only contains the table of contents and the pages relating to utilities. Pages 18 and 19 cover the water system. On the WA Public Offering Statement, the water system is covered on pages 7 and 11. According to the information that we have been provided, capital and debt recovery costs account for \$16.76 (39%) of the base rate. Previously, the WUTC Staff has responded that they use "historical costs of assets when first placed in service for utility use. This cost is reflected on the company books and is being depreciated over its useful life on a straight-line basis. “Capital Recovery” fees are not regulated since the developer, Suncadia, LLC, recovers them and they are not part of the regulated tariff." We need a further explanation of this statement since capital recovery is part of the "allowable return on investment" fee structure, so we are confused if this is not part of the regulated tariff.

2. If the WUTC agrees that recovery of capital and debt costs can be included in the base rate, it is unclear why increasing the ready-to-serve (RTS) rate by \$10.79 (+108%) would only marginally reduce the base rate for active customers. There are approximately 4 times the number of RTS customers as opposed to the active customers (~608 vs. ~160). The logic of the filing and analysis do not clearly show how the increased RTS rate is being applied to reduce the impact on the base rate of the residential customers (most, if not all of the RTS customers are residential properties).

3. Suncadia Water has been charging residential property owners \$35 per month as soon as the property is occupied going back to the spring of 2006. Commercial properties have been using potable water from the same system throughout that time and have apparently not been charged anything for their water service during that time. From the information filed, the golf

courses have also been supplied irrigation water at no cost, as well. Since the golf courses and commercial properties are owned and operated by the Developer, it would seem fair that there be a "true up" of their water service payments prior to instituting a new rate structure. Suncadia should provide all documentation showing the fair cost of the irrigation and commercial system water usage for the past 2+ years so that the residential customers are not subsidizing the commercial properties. This should be equitably applied to the base and usage costs.

4. It is not clear that the system was transferred to Suncadia Water at the lower of cost or market. The Suncadia Water residential customers have not seen evidence from Suncadia Water or WUTC staff that all of the assets included in the rate base, as requested by Suncadia Water, have been appropriately valued and accounted for. In particular, it is important for Suncadia Development to make available to the WUTC its sources and valuation basis of the assets transferred, determine if the assets should be excluded from rate base because they constitute contributions in aid of construction ("CIAC") and determine the appropriate costs of capital associated with the assets transferred. More specifically, The CIAC percentage, accumulated depreciation percentage, and resulting % of net utility plant in service are not clearly supported and justified from the filing. See the table below showing the discrepancy between potable and irrigation water systems.

	Utility Plant in Service	Accumulated Depreciation	Accum. Deprec. Percentage	CIAC Plant In Service	CIAC Plant In Service Percentage
Potable	\$ 19,240,490	\$ 112,264	0.6%	\$11,619,115	60.4%
Irrigation	\$ 1,884,837	\$ 32,340	1.7%	\$ 1,257,414	66.7%

**Allocation of costs between irrigation and domestic systems**

It is not clear from the information provided in the filing that 93% of the total cost of the water system was required to install the potable water system. For example, it would seem fair that the irrigation system cover 50% of the common corridor installation areas and costs required to cross the river to the "Tumble Creek" area of the property. We lack information about how these costs were allocated from the filing and do not have the sophisticated staff required to evaluate these costs, but from our general knowledge of the property, it does not seem reasonable that the irrigation water system only incurred 7% of the total system capital costs. The allocation of these costs has had a significant impact on base rate and cost to residential customers as opposed to the golf courses which are the sole users of the irrigation water and are owned and operated by the Developer. We have been told that the WUTC Staff would review the cost of all assets listed and the depreciation life assigned. This review will also include all assets listed as CIAC (Contributions in Aid of Construction). This review has not yet been made available.

1. If Suncadia Water can recover capital costs and debt costs, the allocation of system costs between potable and irrigation systems needs to be more fully explained. See the table below for the relative weightings of Utility Plant in Service and Net Utility Plant in Service. There is no justification for these relative weightings in light of the fact that the irrigation system is operated only for use by the Developer.

	Utility Plant in Service	% of Utility Plant	Net Utility Plant In Service	% of Total Net Utility Plant In Service
Potable	\$ 19,240,490	91.1%	\$ 7,509,111	92.7%
Irrigation	\$ 1,884,837	8.9%	\$ 595,084	7.3%

2. According to the filing, the two maintenance staff are assigned to work on irrigation system 80% of the time during the 5.5 months of high water usage. This makes sense given that the irrigation system has 80% of the pump capacity and using "raw" water requires additional maintenance on filters and other system components. The current allocation of maintenance staff costs are that the remaining 6.5 months are paid for 100% by the potable "side." While the irrigation side of the system is not being used during those 6.5 months and the potable water system is, there does not seem to be sufficient work during the "winter" months when the entire system is covered with snow that would require 100% of 2 maintenance staff to accomplish. The net result of the current allocation is that the potable water system is paying for 71% of the maintenance staff costs. A more equitable allocation of maintenance staff costs would seem to be closer 60% potable and 40% irrigation during the "winter" months. This is a \$35,000 per year cost difference that impacts both the base rate and consumption rate.

#### **Proposed allocation of maintenance staff costs**

	Summer Maint. Staff Cost (5.5 mos.)	Actual % Summer Maint. Staff	Winter Maint. Staff Cost (6.5 mos.)	Actual % Winter Maint. Staff	Total Maint. Staff	% Total Maint. Staff
Potable	\$ 20,176	37%	\$ 64,055	100%	\$ 84,231	71%
Irrigation	\$ 34,024	63%	\$ 0	0%	\$ 34,024	29%
TOTAL	\$ 54,200	100%	\$ 64,055	100%	\$ 118,255	100%

#### **Equitable allocation of maintenance staff costs**

	Summer Maint. Staff Cost (5.5 mos.)	% Summer Maint. Staff	Winter Maint. Staff Cost (6.5 mos.)	% Winter Maint. Staff	Total Maint. Staff	% Total Maint. Staff
Potable	\$ 10,840	20%	\$ 38,432	60%	\$ 49,273	42%
Irrigation	\$ 43,360	80%	\$ 25,622	40%	\$ 68,982	58%
TOTAL	\$ 54,200	100%	\$ 64,055	100%	\$ 118,255	100%

3. Residential owners previously asked if costs were allocated based on short-run or long-run incremental costs. Given the nature of the system, we believe use of long-run costs is more appropriate. WUTC staff responded that they were unclear of this allocation and would get additional information to support this method of allocation. The residential owners have not received a response to this question from the WUTC staff nor Suncadia Water and we believe this could have a material impact on the rates.

4. If excess capacity is to be included in rate base, what if any mechanism will be used to provide for intergenerational equity, that is, requiring future connections to contribute a proportionate share of the capital cost of the system, through latecomer fees or otherwise? The residential owners have not received a response to this question from the WUTC staff nor Suncadia Water and this could have a material impact on the rates.

**CONSUMPTION RATE**

The residential customers of Suncadia Water oppose the consumption rates as filed on the following points:

- The operating expenses have been disproportionately applied to the potable water system versus the irrigation water system. The irrigation water system is only used by the Developer, an affiliated interest.
- Without having a tiered rate structure, conservation is not encouraged and the commercial properties of the Developer are being subsidized by the residential customers.

Suncadia Water has filed for a flat consumption rate until a reevaluation in 2010. This does not encourage conservation and is contrary to the expectations of the residential customers. As you can see from the table below 73% of the consumption rate is due to operating expenses.

<b>DETAILS</b>	<b>CONSUMPTION COSTS</b>	<b>PRICING RATE</b>
Cost of water (est. usage)	\$ 72,805	\$ .72
Operating Expenses	\$ 193,821	\$ 1.93
<b>TOTAL</b>	<b>\$ 266,626</b>	<b>\$ 2.65</b>

**Affiliated Interest Transactions**

1. Considering that The Lodge and parks irrigation are the highest volume users of potable water irrigation per the supplied information, it would seem that the residential owners are subsidizing the exorbitant water usage of Developer properties. There needs to be consideration given to applying tiered pricing based on usage that fairly spread these costs to the users of the system. It also is not clear why the calculations continue to be based on 125 single-family residences when calculating potable ERUs when their own information shows that number to be 160 in August 2008. That understates the ERUs by 9.1% and artificially raises the consumption rate.

<b>CONSUMPTION DETAILS</b>	<b>Est. 2008 Usage in 1,000 gals.</b>	<b>Est. Consumption Costs</b>	<b>Consumption %</b>
Residential	29,828	\$ 79,044	40%
Commercial	43,195	\$ 114,467	60%
<b>TOTAL</b>	<b>73,023</b>	<b>\$ 193,511</b>	<b>100%</b>

<b>BASE RATE DETAILS</b>	<b>Base Rate Costs</b>	<b>Base Rate %</b>
Residential	\$ 155,059	65%
Commercial	\$ 83,093	35%
<b>TOTAL</b>	<b>\$ 238,152</b>	<b>100%</b>

### **Flat rate versus consumption rate**

Suncadia Water has chosen to place more of the costs in the base rate to the benefit of the commercial properties and to the detriment of the residential owners. The Developer has enforced strict controls on landscaping and water features in residential construction, while following different guidelines for their commercial construction. While we would expect a reevaluation of the tiers used in the consumption rate when they have better data, there should be tiered rates to appropriately transfer the cost of the highest using customers to them. The Pricing Rate is reached by dividing the Consumption Costs by the estimated usage of 73,023,000 gallons for 2009. At the very least, we would expect to see a high usage surcharge of at least 3 times a more reasonable base rate for usage above 14,000 gallons per month. The tables above illustrate the discrepancy between the actual water usage by the commercial properties of the Developer versus what they pay. The net is that the residential owners pay for 54% of the cost of potable water and use 40% of the resource while the commercial properties pay for 46% of the cost and use 60% of the resource. This is one of the main reasons why the residential owners would prefer to see more of the charge against usage and have it tiered as opposed to increased base rate and a flat consumption. We have asked this question previously and have not received a response from the WUTC staff nor Suncadia Water. This seems to be a key issue that should be resolved prior to setting or recommending a rate.

### **GENERAL CONCERNS**

The close relationship Suncadia Water and the Developer are such that we are not confident that we can rely on fair and equitable delineation of the potable and irrigation system costs and treatments. Having the Developer provide accounting and management services does not provide the kind of protection that the customers of the water company should expect since the Developer also has commercial interests served by Suncadia Water. The Developer's questionable treatment of the transfers and costs make this a serious concern.

Suncadia Water was unable to account for over 83% of the potable water used in 2007. That is troubling information when rates are being set based on the information provided about costs and

allocation of other resources within this water system.

## CONCLUSIONS

Based on the information contained in the filing and related information, it is not clear that the current flat rate of \$35 per month is providing inadequate income from the single-family residences of Suncadia. We request that the WUTC not approve this rate change as filed until more information is provided that would support that such a change would not unduly benefit the Developer's commercial properties to the detriment of the residential owners. If you look at the residential rate illustration below with the capital cost recovery removed, you see why this is the case. Some of the residents of Suncadia have been reading their own meters and have had consistent usage of 6,000 gals in high usage summer months and less than 3,000 gallons in other months with an average of 4,000 gallons per month.

<b>MONTHLY SINGLE FAMILY RESIDENTIAL RATE</b>	<b>Current Flat Rate</b>	<b>Proposed Consumption Rate</b>	<b>Proposed Cost Comparison</b>
Base Rate	\$ 35.00	\$ 42.73	
Capital Recovery & Debt		(\$ 16.76)	
Consumption Rate (4 K gals)	N/A	\$ 10.60	
<b>TOTAL</b>	\$ 35.00	\$ 36.57	+4%

The difference between the adjusted proposed rate above and the current residential rates is \$3,014 ( $\$1.57 * 12 \text{ months} * 160 \text{ customers}$ ) per year, far different from the \$670,092 (554 percent) increase Suncadia Water has requested. If they remove the capital cost recovery from the RTS fees as they should be, those fees would actually go down from the proposed rate of \$20.79 by \$13.90 to \$6.10 reducing income by \$28,454 ( $\$3.90 * 12 * 608$ ). From the information above, it appears that the single-family residents of Suncadia are already paying more than their fair share for water.