Inscription Canyon Ranch Water Users Association
Rate Analysis Report

Introduction

Facilitation was contacted by Mark Armstrong, Vice President of the Board of Directors of the Inscription Canyon Ranch Water Users Association, ("ICRWUA")[1] to make adjustments and projections to 2019 financial data to create three scenarios of rate payer groups and the resultant estimated rates for the customers. The three customer base scenarios to be presented are:

- Scenario 1 – ICRWUA will remain intact with its current customer base, including the golf course.

- Scenario 2 – ICRWUA will retain its current customer base, but the golf course will be excluded.

- Scenario 3 – The portion known as Inscription Canyon Ranch ("ICR") on the west side of Williamson Valley Road ("WVR") will separate from the Talking Rock Ranch ("TRR") portion of ICRWUA on the east side of WVR, including the golf course.

System Comparison

In many ways the two systems, aside from the TRR golf course, are very similar. Based on the Staff report docketed April 7, 2020, in Docket W-02824A-20-0013, the ICR system sold 31,806,320 gallons to an average 381 customers during 2019. After removing the gallons associated with the golf course, the TRR system sold 26,322,703 gallons to an average 388 customers.

Based on those amounts, the ICR system had an average monthly usage of 6,957 gallons and TRR was 5,654. This slight difference makes sense as there appears to be a group of smaller residential parcels on the TRR side. Company-wide during 2019 (excluding the golf course), 58,129,023 gallons were sold to 769 customers for an average monthly usage of 6,299 gallons.

The main difference between the two systems seems to be property and well ownership. The ICR system does not own any of the wells that serve it on the west side of WVR. Instead, it purchases water per an agreement at $0.25 per thousand gallons[2]. On the other hand, several parcels of land are owned that utility infrastructure sits upon, including the 210,000 gallon tank off Magner Drive and the 350,000 tank by Whispering Canyon.

[1] ICRWUA has an open case with the Arizona Corporation Commission to transfer the assets and the CC&N to Inscription Canyon Water Company.
[2] This amount is increasing to $0.32 per 1,000 gallons in August 2020, and was used for this report.

In addition, ICR owns two other parcels at 14000 and 14030 Grey Bears Trail that house a building and what appears to be a well site. The ICR system pays for power to both of those locations in addition to another referred to as “ICR well”.

The three TRR wells all have the same Cadastral number on ADWR’s website, all appear to be at approximately 15775 WVR, and are assumed to be on parcels 300-28-016K and/or 300-28-121L. The remainder of TRR’s system assets are located on land owned by Talking Rock Ranch Association For Common Preservation. In addition to the above well site parcels, the TRR system pays for power at the unowned locations for the 300,000 gallon tank near 13000 N Cooper Morgan, the 350,000 gallon tank and pressure tank near 15527 Molly Way, and booster equipment at 14535 Double Adobe.

<u>Property Taxes</u>

Although it seems odd to many, each utility in Arizona pays property taxes. If they do not own land and pay a very nominal amount of tax for it, they still are required to pay a much larger amount of personal property tax that is based on the revenue of the utility. Based on the books of ICRWUA, the TRR system is not being charged with property taxes but the IRC system is. This is not correct.

Based upon the information from the Yavapai County website, both the ICR and TRR existing service areas are within tax area code (“TAC”) 0197. Currently ICRWUA is paying two property tax bills: parcels 901-10-244 02 and 901-10-197 09, which are both personal property tax parcels. The first parcel is in TAC 0244 and the other is in 0197. Both service areas are in 0197 and the only land parcels ICRWUA has in TAC 0244 are the two mentioned at 15575 WVR where the TRR system wells are.

Exhibit 1 illustrates the service area of TRR as it appears within TAC 0197. You can see that the well field off WVR near Copper Basin Wash is in TAC 0244. Exhibit 2 shows the entirely of the ICR system, which is also in TAC 0197. The 2019 tax bills reflected $5,150.82 due in TAC 0244, and $11,037.22 for 0197.

Exhibits 3 and 4 are the above mentioned 2019 property tax bills for ICRWUA for TAC 0244 and 0197 respectively. The entities that receive the property tax funds are listed so the Board can evaluate what is being paid to TAC 0244 instead of 0197, and the highlighted items are unique to each tax code. Because the property taxes are incorrect, TAC 0197 has been underfunded as some payments have been directed to TAC 0244 on the most recent bills. Since all of ICRWUA’s revenue is generated in TAC 0197 that is the code where the property tax bills should be paid.

Exhibit 5 shows the property tax expense calculation used for this report, which is the same methodology ACC Staff and ADOR use to calculate property taxes. The first two columns calculate property taxes for both the ICR and TRR systems as they should be moving forward. Because the TRR system has more than 64% higher revenue than ICR, its share of the personal property tax is higher.

Scenario 1

Exhibit 6 presents Scenario 1, which is the current customer base including both ICR and TRR customers and the golf course. The property tax adjustments for all scenarios were explained above and are on Exhibit 5 for reference. The other expense adjustments were to increase the ICR purchased water expense for the change in rate from $0.25 to $0.32 per 1,000 gallons. This change resulted in an estimated increase of $2,228 per year based upon the 2019 ICR system usage. The other adjustment was to reclassify a purchased power refund check from TRR to ICR for $1,510.

Once the expense adjustments are made, total projected expenses going forward should be about $576,227. Considering total 2019 revenue was $573,649, it is clear an increase would be necessary to have a positive operating income. As of late, the ACC has been setting the operating margin around 10.00%[3]. Under this scenario, an increase of $64,000 will result in revenue of $640,649 per year, and operating income of $64,422, or a 10.06% operating margin.

This increase amount of $64,000 is approximately 11.16% of 2019 revenue, and has been spread evenly across all customer charges. See Table 1 below for the impact to the average monthly consumption of 6,299 gallons:

	Current Bill	11.16% Increase	New Bill
Monthly Minimum	$ 20.00	$ 2.23	$ 22.23
Up to 4,000 gallons	11.20	1.25	12.45
4,000-10,000 gallons	9.20	1.03	10.23
Total	$ 40.40	$ 4.51	$ 44.91

Table 1

The average user would see their bill increase by $4.51 per month to $44.91 under this scenario.

The golf course would also experience an increase of 11.16%. In 2019 it paid $126,797 for its water at a rate of $1.40 per thousand gallons. The rate would increase by $0.16 to $1.56 per thousand gallons and would result in an increase of about $14,146 per year, or $1,179 per month.

[3] During the April 14, 2020 Open Meeting, Commissioner Justin Olsen stated that an operating margin should not be granted to utilities whose owners do not have an investment. Due to the amount of AIAC and CIAC used to build the systems, ICRWUA will not have positive rate base for many years.

Scenario 2

Exhibit 7 presents Scenario 2, which is the current customer base of the utility as in Scenario 1, but the golf course revenue and expenses are excluded. Again, property taxes were adjusted as explained above and detailed on Attachment 5. The purchased water expense adjustment for the ICR system and the reclassification of $1510 from TRR to ICR are also included here.

New adjustments for Scenario 2 are to remove the $126,797 of 2019 revenue for lake water sales to the golf course. The other golf course related item is the TRR's systems purchased power expense of $86,325, which includes the cost to pump water for the golf course. About 22.52% of the total TRR system gallons were non-golf course, so that percentage was applied to the purchased power expense of $86,325, which times 22.52% is $19,439.

Once the expense adjustments are made, total projected expenses going forward should be about $506,279. The loss of golf course revenue will have to be made up for, and under this scenario, an increase of $116,000 will result in revenue of $562,853 per year, and an operating income of $56,574, which is a 10.05% operating margin.

This increase amount of $116,000 is approximately 25.96% of 2019 revenue, and has been spread evenly across all customer charges. See Table 2 below for the impact to the average monthly consumption of 6,299 gallons:

	Current Bill	25.96% Increase	New Bill
Monthly Minimum	$ 20.00	$ 5.19	$ 25.19
Up to 4,000 gallons	11.20	2.91	14.11
4,000-10,000 gallons	9.20	2.39	11.59
Total	$ 40.40	$ 10.49	$ 50.89

Table 2

The average user would see their bill increase by $10.49 per month under this scenario, or 25.96%.

Scenario 3

Exhibit 8 presents Scenario 3, which only includes the customers on the ICR system. None of the golf course or TRR system revenues and expenses are included in this scenario. The property tax adjustment reduces property tax expense to the revenue based calculation on Exhibit 5. Purchased water expense again is increased for the change in rate and purchased power is reduced by $1,510 for an APS refund.

Once the expense adjustments are made, total projected expenses going forward should be about $245,777. Under this scenario, a revenue increase of $56,500 will result in $273,554 per year, and an operating income of $27,777, which is a 10.15% operating margin.

This increase amount of $56,500 is approximately 26.03% of 2019 revenue, and has been spread evenly across all customer charges. See Table 3 below for the impact to the average monthly consumption of 6,957 gallons:

	Current Bill	26.03% Increase	New Bill
Monthly Minimum	$ 20.00	$ 5.21	$ 25.21
Up to 4,000 gallons	11.20	2.92	14.12
4,000-10,000 gallons	11.83	3.08	14.91
Total	$ 43.03	$ 11.21	$ 54.24

Table 3

The average user would see their bill increase by $11.21 per month to $54.24 under this scenario.

Summary

Based on the information presented in this report, ICWUA had a total operating margin of 2.29% during 2019. The ICR system had a -11.84% operating margin and the TRR system's was 10.89%. It does appear that some kind of rate increase is warranted based upon those numbers.

Scenario 1, which retains the current customer base with both ICR and TRR systems as well as the golf course, results in the lowest amount of increase. The revenue must increase $64,000 per year to reach a 10% operating margin. The non-golf customers will increase $4.51 per month, or 11.16% for the average user of 6,299 gallons. The golf course will also see an 11.16% increase to its rate by $0.16 to $1.56 per thousand gallons, or a $1,142 increase per month.

Scenario 2 retains the current customer base with both ICR and TRR systems and excludes the golf course. In this case, the annual revenue must decrease by ($10,797) to $562,853, but with the loss of the golf course lake sales, the $116,000 increase to the other customers is necessary to make up for that loss. The customers will see an increase of 25.96%, or $10.49 per month for the average user of 6,299 gallons.

Scenario 3 includes only the ICR system. Under this scenario, the annual revenue must increase by $56,500 to $273,554. The customers would likely see an increase of 26.03%, or $11.20 per month for the average user of 6,957 gallons.

Scenario 1 is about 15% less increase in rates than Scenario 2 and Scenario 3 that do not include the golf course. Due to the golf course having its own distribution system, it is a very low cost customer as water can just be delivered to the lake. The only real expense related to the golf course appears to be purchased power, which is substantial (an estimated $66,886), but still less than the $126,797 in revenue provided by the golf course. Without it, both systems either together or apart, will require approximately a 26% increase.

I hope you have found this report informative and it has met your needs. If you have any questions, please do not hesitate to contact me at (602) 275-1710 or sonncpa@cox.net.

Sincerely,

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