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# MEMORANDUM

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Date: November 27, 2018

To: The Honorable Sharon Bronson, Member  
Pima County Board of Supervisors

From: C.H. Huckelberry  
County Administrator

Re: **Update on the Ajo Improvement Company's Arizona Corporation Commission Hearings on proposed rate increases**

As you know, the Ajo Improvement Company (AIC), a wholly-owned subsidiary of Freeport-McMoran (FM) and largely the sole provider of utilities for the former mining community of Ajo, has filed for rate increases for their water, electric and wastewater utilities. The exorbitant utility rate increases being sought by AIC will have a drastic impact on this low-income community, with many residents being retirees on fixed incomes with very limited disposable income. Pima County filed as an intervenor in this rate case as the County will also be impacted by these rate increases through the courthouse, Sheriff's substation and transportation facilities maintained in Ajo.

With past occasional subsidies from FM, AIC operates through charges for utility services to customers and direct payments from FM for services. In 2004, Phelps Dodge (PD), FM and AIC began a major capital repair and replacement effort for their aging utility infrastructure, with costs over \$47.8 million for AIC's repairs and replacement of streets, electric, water and wastewater systems. This was done without seeking ACC approval for rate increases to fund these major capital improvements. In fact, AIC has not sought any utility rate increases for the last 14 years for water and wastewater and 18 years for electric.

In December 2017, AIC filed for rate increases in its electric, water and wastewater utility divisions to the Arizona Corporation Commission (ACC) to achieve rates sufficient to cover operating costs plus an operating margin-based return. The filing included proposed utility rate hikes in the range of 120 to 360 percent. AIC initially proposed a 20 percent margin over operating costs with the rates phased in over 5 years for all three utility divisions. AIC's proposed operating costs include recovery of the PD/FM capital investment through a depreciation component.

Commission staff reviewed AIC's proposal and financial information, and instead recommended that AIC's new rates be set on a 12 percent operating margin, phased in over 5 years for water and electric and seven years for wastewater. Even with Commission staff's recommendation, rate increases will still be within 100 to 350 percent for customers.

The Honorable Chairman and Members, Pima County Board of Supervisors

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Many public comments in opposition have been filed with the ACC, including Pima County's objection. A couple of public hearings have been held, with the most recent being held on October 23, 2018 in Ajo, with approximately 60 people in attendance, including Commissioner Tobin with the ACC. Since then, Commissioner Burns, Tobin and Olson have filed subsequent requests to Commission staff for further information and calculations at different percent margins and phase in years (Attachment A). Ultimately, the rate increases remain similar.

On November 15, the ACC held an evidentiary hearing before an administrative law judge for AIC and interveners, including Pima County and a resident from Ajo. As an intervener, the County did not provide testimony but examined an AIC witness regarding the accounting bases for the infrastructure improvements. In particular, questions were directed at how AIC expensed part of the costs and whether capital expenditures were made to address poor maintenance and capacity improvements.

The next step is for the parties to file briefs by December 21, 2018, with responses due by January 11, 2019. Based on the briefs and testimony from the evidentiary hearing, the administrative law judge will issue an opinion and order, which will go to the ACC for consideration at a public hearing. We anticipate a decision on the rate increase sometime in February 2019.

If the ACC grants rate increases as proposed, the County will explore whether a judicial challenge is warranted.

Attachment

CHH/mp

c: The Honorable Chairman and Board of Supervisors  
Charles Wesselhoft, Deputy County Attorney  
Diana Durazo, Special Projects Manager for County Administrator's Office

Exhibit A

1. Commissioner Burns - 10% Operating Margin over 7 years

**Residential Bill**

<b>Impacts</b>	<b>Current</b>	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Year 4</b>	<b>Year 5</b>	<b>Year 6</b>	<b>Year 7</b>
Water Medium Usage	\$18.40	\$22.93	\$30.75	\$37.38	\$44.38	\$50.17	\$54.95	\$61.90
Wastewater	\$16.10	\$24.62	\$33.09	\$41.57	\$50.04	\$58.57	\$66.98	\$75.45
Electric Medium Usage	\$45.41	\$52.35	\$59.29	\$66.01	\$72.73	\$79.45	\$85.73	\$92.00

Exhibit B

2. Commissioner Burns - 10% Operating Margin over 10 years

**Residential Bill**

<b>Impacts</b>	<b>Current</b>	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Year 4</b>	<b>Year 5</b>	<b>Year 6</b>	<b>Year 7</b>	<b>Year 8</b>	<b>Year 9</b>	<b>Year 10</b>
Water Medium Usage	\$18.40	\$21.65	\$27.12	\$31.97	\$35.92	\$40.77	\$44.37	\$46.95	\$51.90	\$55.75	\$60.43
Wastewater	\$16.10	\$22.08	\$28.01	\$33.94	\$39.87	\$45.80	\$51.73	\$57.66	\$63.59	\$69.52	\$75.45
Electric Medium Usage	\$45.41	\$50.47	\$55.53	\$60.37	\$65.20	\$70.04	\$74.43	\$78.82	\$83.22	\$87.61	\$92.00

Exhibit C

3. Commissioner Olson - 12% Operating Margin over 5 years

**Residential Bill**

<b>Impacts</b>	<b>Current</b>	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Year 4</b>	<b>Year 5</b>
Water Medium Usage	\$18.40	\$24.79	\$33.13	\$41.47	\$50.06	\$63.13
Wastewater	\$16.10	\$28.53	\$40.86	\$53.21	\$65.56	\$77.91
Electric Medium Usage	\$45.41	\$55.43	\$65.45	\$75.25	\$85.05	\$94.85

Exhibit D

4. Commissioner Olson - 12% Operating Margin over 7 years

**Residential Bill**

<b>Impacts</b>	<b>Current</b>	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Year 4</b>	<b>Year 5</b>	<b>Year 6</b>	<b>Year 7</b>
Water Medium Usage	\$18.40	\$24.24	\$29.99	\$36.61	\$43.64	\$51.26	\$56.45	\$63.13

Wastewater	\$16.10	\$24.93	\$33.76	\$42.60	\$51.43	\$60.26	\$69.09	\$77.92
Electric Medium Usage	\$45.41	\$52.76	\$60.11	\$67.23	\$74.36	\$81.49	\$88.17	\$94.85

Exhibit E 4. Commissioner Olson - 12% Operating Margin over 10 years

**Residential Bill**

Impacts	Current	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
Water Medium Usage	\$18.40	\$21.17	\$27.94	\$32.80	\$37.68	\$42.31	\$45.45	\$49.93	\$54.09	\$58.60	\$63.13
Wastewater	\$16.10	\$22.33	\$28.50	\$34.68	\$40.85	\$47.03	\$53.20	\$59.38	\$65.56	\$71.73	\$77.91
Electric Medium Usage	\$45.41	\$50.75	\$56.10	\$61.22	\$66.34	\$71.47	\$76.14	\$80.82	\$85.50	\$90.17	\$94.84