

OPEN MEETING ITEM



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ARIZONA CORPORATION COMMISSION

2004 JAN 27 P 1:51

DATE: January 27, 2004
DOCKET NO: W-02065A-03-0490

AZ CORP COMMISSION
DOCUMENT CONTROL

TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Amanda Pope. The recommendation has been filed in the form of an Opinion and Order on:

WILHOIT WATER COMPANY
(TRANSFER OF ASSETS/CC&N CANCELLATION)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and thirteen (13) copies of the exceptions with the Commission's Docket Control at the address listed below by 4:00 p.m. on or before:

FEBRUARY 5, 2004

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Working Session and Open Meeting to be held on:

FEBRUARY 10 AND 11, 2004

For more information, you may contact Docket Control at (602)542-3477 or the Hearing Division at (602)542-4250. For information about the Open Meeting, contact the Executive Secretary's Office at (602) 542-3931.

Arizona Corporation Commission

DOCKETED

JAN 27 2004

DOCKETED BY

BRIAN C. McNEIL
EXECUTIVE SECRETARY

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 COMMISSIONERS

3 MARC SPITZER, Chairman
4 WILLIAM A. MUNDELL
5 JEFF HATCH-MILLER
6 MIKE GLEASON
7 KRISTIN K. MAYES

8 IN THE MATTER OF THE APPLICATION OF
9 WILHOIT WATER COMPANY FOR APPROVAL
10 OF THE TRANSFER OF A PORTION OF ITS
11 ASSETS AND CANCELLATION OF A PORTION
12 OF ITS CERTIFICATE OF CONVENIENCE AND
13 NECESSITY.

DOCKET NO. W-02065A-03-0490

DECISION NO. _____

14 OPINION AND ORDER

15 DATE OF HEARING:

December 1, 2003

16 PLACE OF HEARING:

Phoenix, Arizona

17 ADMINISTRATIVE LAW JUDGE:

Amanda Pope

18 APPEARANCES:

Mr. Douglas G. Martin, Martin & Bell, LLC, on
behalf of Wilhoit Water Company;

Ms. Carolyn Kusian Oberholtzer, Jorden,
Bischoff, McGuire & Rose, P.L.C., on behalf of
the City of Avondale; and

Mr. David Ronald, Staff Attorney, Legal
Division, on behalf of the Utilities Division of
the Arizona Corporation Commission.

19 **BY THE COMMISSION:**

20 On July 16, 2003, Wilhoit Water Company ("Wilhoit" or "Company") filed an application
21 with the Commission for approval of the sale of that portion of its water company assets that are
22 utilized to service the Glenarm Farms water system to the City of Avondale ("Avondale") and
23 cancellation of that portion of its Certificate of Convenience and Necessity ("CC&N" or
24 "Certificate") authorizing the provision of water services to the Glenarm Farms system
25 ("Application").
26

27 By Procedural Order dated August 25, 2003, the Application was deemed administratively
28 complete pursuant to Arizona Administrative Code ("A.A.C.") R14-2-411(C) and Arizona Revised

1 Statutes ("A.R.S.") § 41-1074(C), and the matter was set for hearing on October 22, 2003.

2 Wilhoit published notice of the sale and cancellation in *Arizona Capital Times* on September
3 5, 2003 and filed an affidavit of publication on September 17, 2003. No requests for intervention
4 were filed.

5 Commission Utilities Division Staff ("Staff") filed a Staff Report on October 7, 2003
6 recommending conditional approval of the Application.

7 On October 22, 2003, a full public hearing was convened before a duly authorized
8 Administrative Law Judge of the Commission. Counsel for the Company, Staff, and the City of
9 Avondale appeared. No members of the public appeared at the hearing. The hearing adjourned, and
10 it was ordered that the hearing be continued to a later date so that the Company could provide a
11 witness capable of testifying to the underlying issues related to its Application, including but not
12 limited to an outstanding tax matter, as well as address the argument raised by the City of Avondale
13 relating to the manner in which the outstanding tax is extinguished by operation of law.

14 On October 23, 2003, a procedural order was issued setting the hearing for December 1, 2003,
15 specifying the information, both documentary and testimonial, to be provided by Wilhoit at that
16 hearing and suspending the time clock for processing the Application during the pendency of the
17 continuance.

18 On December 1, 2003, the hearing convened and the Company, Staff, and the City of
19 Avondale appeared with counsel.

20 By its Application, Wilhoit seeks approval to sell that portion of its water company assets
21 utilized to service its Glenarm Farms water system. The Glenarm Farms system, one of four water
22 systems operated by Wilhoit,¹ serves approximately 143 connections in the Avondale area.

23 The assets that are the subject of the sale at issue are encumbered by tax liens totaling
24 approximately \$215,000, inclusive of interest. These liens are held by the State of Arizona as
25 Certificates of Purchase. Wilhoit and the City of Avondale argue, however, that these tax liens are
26 extinguished by operation of law.

27
28 ¹ Wilhoit Water Company also operates the Yavapai Estates, Blue Hills, and Thunderbird Meadows water systems.

1 By way of avowal, the City of Avondale presented its points and authorities in support of its
 2 argument that the delinquent tax at issue is extinguished based upon the "merger doctrine,"² and in
 3 support of its alternative argument that even if the taxes are not extinguished as a consequence of this
 4 legal principal, A.R.S. § 42-18208 would result in the reduction of the actual amount owed. Counsel
 5 for the Company deferred to the City of Avondale for the argument relating to the manner in which
 6 the taxes owed by Wilhoit are allegedly extinguished based upon the sale to the City of Avondale in
 7 its capacity as a subdivision of the state.

8 The Company presented an employee, Ms. Lori Redlin, as its sole witness whose duties
 9 encompass handling customer complaints, billing and some degree of bookkeeping. Ms. Redlin was
 10 unfamiliar with the Company's Application, the Staff Report, the delinquent taxes at issue, as well as
 11 the Company's current status with regard to the payment of taxes.

12 The City of Avondale also presented two witnesses, Mr. Charles McClendon, Assistant City
 13 Manager for the City of Avondale, and Mr. Rob Emmett, Utilities Director for the City of Avondale,
 14 in support of the Application, both of whom testified to the transaction at issue, the manner in which
 15 Avondale is currently providing service to the Glenarm Farm customers,³ and the plans to be
 16 undertaken by Avondale to continue to provide service.

17 Staff offered Mr. Jim Fisher as its witness, who testified to the substance of the Staff's
 18 recommendations as authored by Mr. Fisher and contained in the Staff Report.

19 At the conclusion of the hearing, the parties were ordered to file post-hearing briefs by
 20 December 8, 2003 on the issue of the manner and extent to which the merger doctrine is superceded
 21 by the provisions in A.R.S. § 9-404, which essentially states that liens on property purchased by a
 22 city are not extinguished or merged in the title of the property. Staff was additionally ordered to file
 23 in this docket a pleading responsive to the Company's July 17, 2003 filing of a curtailment tariff in
 24 Decision No. 66404.

25 _____
 26 ² The merger doctrine is a legal concept which provides that a previously existing lien becomes merged in legal title when
 27 the property affected is acquired by the state or one of its political subdivisions. *See, State v. ex. rel. Peterson v.*
 28 *Maricopa County*, 38 Ariz. 347, 300 P. 175 (1931); *City of Eloy v. Pinal County*, 158 Ariz. 198, 761 P.2d 1102 (App.
 1988).

³ At the hearing, Mr. Emmett testified that the City began billing Glenarm Farms customers by approximately the end of
 September 2003.

1 On December 8, 2003, the City of Avondale submitted a Memorandum in support of its
2 argument for extinguishment pursuant to the merger doctrine, and Staff submitted a Closing Brief in
3 support of the argument that the merger doctrine is superseded by A.R.S. § 9-404.

4 On December 9, 2003, Staff submitted an Errata to its Closing Brief, providing a copy of the
5 Arizona State Senate Fact Sheet for Senate Bill 1031, which was referenced in but not attached to its
6 Brief.

7 On December 10, 2003, Staff submitted its Position Regarding Curtailment Tariff, whereby
8 Staff indicated that the curtailment tariff on file for Wilhoit meets Staff's requirements thereby
9 satisfying the condition set forth in the Staff Report.

10 Upon receipt of the post-hearing briefs and Staff's filing, the matter was taken under
11 advisement pending submission of a Recommended Opinion and Order to the Commission.

12 DISCUSSION

13 All parties to this transaction support Wilhoit's Application as being in the public interest, and
14 all parties concur that the City of Avondale is a fit and proper entity to provide service to the
15 customers located in the Glenarm Farms system. Staff's approval, however, is conditioned upon
16 Wilhoit's ability to satisfy several conditions as set forth in its Staff Report, including but not limited
17 to, the requirement that Wilhoit file with the Director of the Utilities Division evidence that the State
18 of Arizona will be paid \$294,527.46 to satisfy the certificates of purchase related to outstanding
19 personal property taxes of the Company before close of escrow, or within 30 days of any decision in
20 this matter, whichever comes first.

21 The parties by their testimony and the terms of the Agreement acknowledge that the State of
22 Arizona holds certificates of purchase for outstanding personal property taxes unpaid by Wilhoit. It
23 is unclear, however, whether this unpaid tax amount relates to any of Wilhoit's other three water
24 systems. In its Staff Report, Staff states that in Wilhoit's last Arizona Corporation Commission
25 Annual Report, it reported paying no income or property tax. At the hearing, Counsel for Wilhoit
26 and the City of Avondale, as well as Avondale's witnesses, indicated that to best of their knowledge,
27 the tax at issue relates only to the Glenarm Farms system. No one was able to confirm, however, that
28 tax on the other three systems is being timely remitted.

1 This uncertainty surrounding Wilhoit's tax obligations is all the more troubling in light of the
2 fact that the established rates for all of its water systems include provisions for property tax expense.
3 In Decision No. 58102 (December 9, 1992), the Commission increased the rates for all four of
4 Wilhoit's water systems but not before noting an amount of outstanding property tax as reported by
5 Wilhoit in its 1991 annual report. The Commission reasoned that because Wilhoit's rates included
6 provisions for property tax, it would be inherently unfair to assess the ratepayers a second time for
7 such expenses. We believe that we are essentially faced with the same issue in this matter and that
8 Wilhoit's ongoing failure to remit tax which is collected in its rates must be addressed.

9 Furthermore, the Agreement indicates that the unpaid taxes equal \$294,527.46, yet at the
10 hearing, evidence was introduced to show that the amount of unpaid taxes, according to the Maricopa
11 County Treasurer's Office, is \$212,926.49 if paid by December 31, 2003 and \$214,065.54 if paid by
12 January 31, 2004.⁴ The parties to the transaction were, however, unable to explain with certainty
13 why the \$294,527.46 figure was utilized in the agreement and indicated that they had nothing to
14 substantiate use of that figure. Consequently, we conclude that the most accurate information with
15 regard to the outstanding liens is derived from the Maricopa County Treasurer's Office, and we will
16 utilize those numbers as reflecting the amount due and owing.⁵

17 As for the issue of who is responsible for payment of any outstanding liens, Wilhoit and
18 Avondale essentially argue that neither Wilhoit nor Avondale is responsible for the tax lien because
19 the unpaid taxes are extinguished by operation of law. At the hearing, Wilhoit deferred and assented
20 to the City of Avondale's argument that the merger doctrine serves to extinguish unpaid taxes on
21 property acquired by the State or any of its political subdivisions. Specifically, Avondale cites *State*
22 *v. ex. rel. Peterson v. Maricopa County*⁶ for the proposition that a previously existing lien becomes
23 merged in the legal title when the property affected is acquired by the state. This holding was then
24 validated and extended to political subdivisions of the state in *City of Eloy v. Pinal County*.⁷

25 The parties were instructed to brief the issue of whether A.R.S. § 9-404 supersedes the case

26 ⁴ See Exhibit C-1.

27 ⁵ The redemption statement from the Maricopa County Treasurer's Office indicates that the total outstanding amount,
inclusive of interest, is \$214,893.22 if paid by February 29, 2004.

28 ⁶ 38 Ariz. 347, 300 P. 175 (1931).

⁷ 158 Ariz. 198, 761 P.2d 1102 (App. 1988).

1 law cited in support of the merger doctrine. Enacted in 1999, A.R.S. § 9-404 states in relevant part,
 2 “[t]he lien for unpaid delinquent taxes, penalties and interest on property acquired by a city or town is
 3 not abated, extinguished, discharged or merged in the title to property.”⁸

4 In its post-hearing Memorandum, Avondale asserts that because neither the Arizona
 5 Constitutional provision giving rise to the doctrine nor the public policy reasons supporting the
 6 doctrine have been altered, A.R.S. § 9-404 may be held to violate Article 9, Section 2 of the Arizona
 7 Constitution.⁹ Staff’s Closing Brief concludes that the legislative history indicates the Legislature’s
 8 specific intent to address both the merger doctrine and the holding in *Eloy*¹⁰ and therefore supports
 9 the conclusion that A.R.S. § 9-404 takes precedence over the application of the merger doctrine in
 10 this matter.

11 In the alternative, Avondale argues that should the merger doctrine not apply, A.R.S. § 42-
 12 18208 operates to extinguish all except one of the certificates of purchase at issue based upon the fact
 13 that with one exception, the certificates were purchased before August 31, 2002 and no action was
 14 taken to redeem before the expiration of ten years from the date of purchase. A.R.S. § 42-18208
 15 states in relevant part, “[i]f a tax lien that was purchased on or before August 31, 2002 is not
 16 redeemed and the purchaser . . . fail[s] to commence an action to foreclose the right of redemption on
 17 or before ten years from the date that the lien was purchased, the certificate of purchase or registered
 18 certificate expires and the lien is void.”¹¹ It is unclear, however, how this statute operates in light of
 19 the fact that the certificates of purchase at issue were assigned to, rather than purchased by, the State.

20 Even if A.R.S. § 42-18208 operates to reduce the amount of the outstanding liens and despite
 21 comments made by Wilhoit and Avondale during the hearing with regard to the manner in which the
 22 tax at issue “runs with the property,” the evidence in the record is unclear which party is legally
 23 responsible for any unpaid tax liens that are not extinguished or mitigated by operation of law.
 24 Avondale failed to assert that there is a provision in the Agreement that relieves it of any tax liability
 25 associated with this transaction, yet in Paragraph 20.2, the Agreement states that “Seller hereby

26 ⁸ ARIZ. REV. STAT. ANN. § 9-404 (B) (1999).

27 ⁹ A.Z. CONST. ART. IX, § 2 states in relevant part, “[t]here shall be exempt from taxation all federal, state, county and
 municipal property.”

28 ¹⁰ 158 Ariz. 198, 761 P.2d 1102 (App. 1988).

¹¹ ARIZ. REV. STAT. ANN. § 42-18208(A) (1999).

1 represents that on or before the Closing Date it will have paid the real and personal property taxes for
2 all prior years imposed against the Property.” Although this provision makes no reference back to
3 Paragraph 12.2, which sets forth the outstanding personal property tax amount with specificity, this
4 provision could serve to render Wilhoit liable for the outstanding tax at issue.

5 **ANALYSIS**

6 Even if the underlying Agreement to this transaction were silent on the issue of responsibility
7 for any unpaid tax related to the property, we do not believe it is necessary to rule upon the
8 applicability of the merger doctrine with respect to the proposed transaction or to determine whether
9 A.R.S. § 9-404 supersedes that doctrine. Rather, we find that pursuant to A.R.S. § 40-285,¹² the
10 Commission has the authority to condition approval of the proposed sale on the requirement that
11 Wilhoit pay all outstanding tax liabilities. As a matter of public policy, parties should not be entitled
12 to avoid legitimate tax liabilities by structuring a purchase agreement in such a manner that could
13 potentially avoid payment of such taxes. Moreover, if Wilhoit is able to avoid its tax liability through
14 the sale of assets to Avondale, its owners will in effect gain a windfall profit due to the fact that the
15 Company has been collecting, through its authorized rates, revenues that include an allowance for
16 payment of taxes associated with its property and income. We decline to countenance a scheme that
17 will permit Wilhoit to escape its tax liability and we will, therefore, require that Wilhoit satisfy all
18 pending tax liabilities through the date of sale to Avondale. In accordance with A.R.S. § 40-285(A),
19 failure to satisfy this condition will render approval of the sale void.

20 * * * * *

21 Having considered the entire record herein and being fully advised in the premises, the
22 Arizona Corporation Commission (“Commission”) finds, concludes, and orders that:

23 **FINDINGS OF FACT**

24 1. Wilhoit is an Arizona corporation certificated, pursuant to Decision No. 39691
25 (October 24, 1968), to provide water service to the following separate unconnected systems:

- 26 a. Yavapai Estates – located in Chino Valley, Yavapai County;

27 ¹² A.R.S. § 40-285 requires public service corporations to secure the Commission’s approval prior to selling, leasing,
28 assigning or otherwise disposing of or encumbering any part of its plant or system necessary or useful in the performance
of its duties to the public.

- 1 b. Blue Hills – located in the town of Dewy, Yavapai County;
- 2 c. Thunderbird Meadows – located in Wilhoit, Yavapai County; and
- 3 d. Glenarm Farms – located in Avondale, Maricopa County.¹³

4 2. The Company currently serves approximately 410 customers, with approximately 143
5 connections being served by the Glenarm Farms system.

6 3. On July 1, 2003, under threat of condemnation by Avondale, Wilhoit and Avondale
7 entered into a Purchase and Sale Agreement between the City of Avondale and Wilhoit Water
8 Company (“Agreement”). Under the Agreement, Avondale will obtain all of the water transmission,
9 distribution, and service facilities dedicated to the Glenarm Farms system as well as any easements
10 useful or necessary to the operation of the system and serve all of the existing Wilhoit customers
11 currently being served by the Glenarm Farms system.

12 4. Under the Agreement, Avondale will pay Wilhoit the sum of \$350,000, \$24,900 of
13 which has been deposited as earnest money and \$325,100 of which will be paid on or before the close
14 of the transaction.

15 5. On July 16, 2003, Wilhoit filed the Application requesting approval for the sale of that
16 portion of its water company assets that are utilized to service the Glenarm Farms water system to
17 Avondale and for the cancellation of that portion of its CC&N authorizing the provision of water
18 services to the Glenarm Farms water system, the legal description of which is attached hereto as
19 Exhibit “A” and incorporated by reference herein.

20 6. By Procedural Order issued on August 25, 2003, the Application was deemed
21 administratively complete pursuant to A.A.C. R14-2-411(C) and A.R.S. § 41-1074 (C), and a hearing
22 was set for October 22, 2003.

23 7. On October 7, 2003, Staff filed its report recommending conditional approval of the
24 sale and cancellation of the Company’s CC&N for the Glenarm Farms area.

25 8. The State of Arizona (“State”) holds certificates of purchase totaling \$214,065.54 if
26 paid by January 31, 2004, which according to Wilhoit and Avondale, evidence the delinquent

27 _____

28 ¹³ In Decision No. 63153 (November 16, 2000), the Commission deleted approximately 163 acres of Wilhoit’s Glenarm Farms CC&N to facilitate a new development receiving service from the City of Peoria.

1 personal property taxes originally assessed on Wilhoit's Glenarm Farms personal property that is the
2 subject of this asset transfer.

3 9. Glenarm Farms collects property tax expenses from its customers in its current rates
4 and charges.

5 10. Neither Wilhoit nor Avondale cite to specific terms of the Agreement as setting forth
6 the party responsible for payment of the delinquent personal property taxes.

7 11. Wilhoit has outstanding customer deposits, which shall, pursuant to the Agreement, be
8 refunded prior to the close of escrow.

9 12. According to the Application, Wilhoit has outstanding main extension agreements,
10 which shall, pursuant to the Agreement, be refunded at the close of escrow.¹⁴

11 13. Staff states that the Glenarm Farms water system is regulated by the Maricopa County
12 Environmental Services Department Compliance ("MCESD"), which reported on August 26, 2003
13 that the Glenarm Farms water system is currently delivering water that meets the water quality
14 standards required by the A.A.C., Title 18, Chapter 4. MCESD also reported that the system has
15 monitoring deficiencies, but no compliance or enforcement action is pending.

16 14. Staff recommends approval of Wilhoit's Application conditioned upon the following:

17 a. that Wilhoit file with the Director of the Utilities Division evidence that the
18 State of Arizona will be paid \$294,527.46 to satisfy the certificates of
19 purchase related to outstanding personal property taxes of the Company
20 before close of escrow, or within 30 days of any decision in this matter,
21 whichever comes first;

22 b. that Wilhoit file a Backflow Prevention Tariff for each of its other
23 operating systems within 60 days of any decision in this matter; and

24 c. that Wilhoit file a Curtailment Tariff for each of its other operating systems
25 within 60 days of any decision in this matter.

26

27 ¹⁴ Wilhoit's Application indicates that there are main extension agreements to be refunded and that such refunds would be
28 made at the close of the transaction. At the hearing, Staff testified that there are no main extension agreements to be
refunded.

ORDER

1
2 IT IS THEREFORE ORDERED that Wilhoit Water Company's Application to Sell that
3 portion of its Assets utilized to service the Glenarm Farms water system to the City of Avondale is
4 approved, conditioned upon its compliance with the requirements as set forth herein.

5 IT IS FURTHER ORDERED that Wilhoit Water Company shall file with the Commission
6 evidence that the outstanding tax liens, which are calculated to equal \$214,065.54 as of January 31,
7 2004, and any subsequent accrual of interest have been satisfied before the close of escrow, or within
8 30 days of this Decision, whichever comes first.

9 IT IS FURTHER ORDERED that Wilhoit Water Company shall refund any outstanding
10 customer deposits.

11 IT IS FURTHER ORDERED that Wilhoit Water Company shall refund any outstanding main
12 extension agreements.

13 IT IS FURTHER ORDERED that Wilhoit Water Company shall file a Backflow Prevention
14 Tariff for each of its other operating systems within 60 days of this Decision.

15 IT IS FURTHER ORDERED that Staff's recommendations, as amended and set forth in
16 Findings of Fact Nos. 14 and 16, are hereby adopted.

17 IT IS FURTHER ORDERED that upon Wilhoit Water Company providing evidence that the
18 sale of assets has been consummated and conditioned upon its compliance with the ordering
19 paragraphs herein, that portion of Wilhoit Water Company's Certificate of Convenience and
20 Necessity authorizing the provision of water services to the Glenarm Farms system shall be canceled
21 without further Order of the Commission.

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IT IS FURTHER ORDERED that if Wilhoit Water Company, Inc. fails to comply with the conditions set forth herein, this Decision shall become null and void without further Order of the Commission.

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 ____ day of _____, 2004.

BRIAN C. McNEIL
EXECUTIVE SECRETARY

DISSENT _____
DISSENT _____

AP:mlj

1 SERVICE LIST FOR: WILHOIT WATER COMPANY

2 DOCKET NO.: W-02056A-03-0490

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EXHIBIT "A"

The SW ¼ of Sec. 29, T2N, R1E, G&SRB&M, Maricopa County, Arizona;
EXCEPT the North 30' of the West 60' of the East 160' thereof.