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ARIZONA CORP. COMM.
TUCSON, AZ.

September 17, 2004

Colleen Ryan, Supervisor
Docket Control
Arizona Corporation Commission
1200 W. Washington
Phoenix, AZ 85007

Re: In the Matter of the Application of Las Quintas Serenas Water Company for a Rate Increase
Docket No. W-01583A-04-0178

Dear Ms. Ryan:

Enclosed for filing in the above-captioned proceeding are the original and fifteen (15) copies of the Rebuttal Testimony of Kathleen (Kaycee) Conger, Dale Calvert and Steve Gay on behalf of Las Quintas Serenas Water Company.

Also enclosed are two additional copies to be conformed and returned to our office in the enclosed self-addressed stamped envelope.

Please contact our office if you have any questions, and thank you for your assistance.

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Sincerely,

Lawrence V. Robertson, Jr.

Lawrence V. Robertson, Jr.

Arizona Corporation Commission
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cc: All parties of Record

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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

MARC SPITZER, Chairman
WILLIAM A. MUNDELL
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ARIZONA CORP. COMM.
TUCSON, AZ.

IN THE MATTER OF THE APPLICATION OF LAS QUINTAS SERENAS WATER CO. FOR A RATE INCREASE	DOCKET NO. W-01583A-04-0178 **REBUTTAL TESTIMONY OF KATHLEEN (KAYCEE) CONGER**

MUNGER CHADWICK, P.L.C.
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INTRODUCTION

Q. Please state your name and business address.

A. My name is Kathleen or Kaycee Conger. My business address is 75 Calle de las Tiendas, Suite 115B, Green Valley Arizona 85614. My business mailing address is P.O. Box 68, Sahuarita Arizona 85629.

Q. By whom are you employed and in what capacity?

A. I am employed by Las Quintas Serenas Water Company (LQS) as their Office Manager.

Q. Please describe your work experience.

A. I completed my education in 1979 in Seattle Washington. I have been employed within the office framework in several different venues since that time. My responsibilities have included all of the basic office duties, human resources, statistics, and accounting functions (i.e. accounts payable, accounts receivable, payroll, billing, budgets, etc.). On April 1, 2000 I was hired by Las Quintas Serenas Water Company to perform all of the office functions for the company.

PURPOSE OF TESTIMONY

Q. What is the purpose of your testimony in this proceeding?

A. To provide certain testimony, which is intended to rebut some of the testimony and conclusions set forth in the Commission Staff's August 20th testimony and exhibits pertaining to the Staff's recommended Rate Design for Las Quintas Serenas Water Company.

RATE DESIGN

Q. Does the Company agree with the Staff's recommended Rate Design as set forth in Schedule ENZ 20, pages 1-3?

A. No.

Q. Why Not?

A. Assuming that the Staff's calculations are based on the Bill Count for the Test Year, which was provided with the Company's Rate Case Application, there is no provision in the Staff Rate design proposal to capture or retain reductions or loss of revenues which would otherwise occur by reason of customer reaction to the new rate design.

Q. What would be the nature of such customer reaction?

A. Based on the Bill Count, there were thirty (30) residential and forty (40) commercial accounts which, at the time, received service through a larger meter than the ⅝" – ¾" standard meter. According to the Staff's proposal, these accounts would be billed the brunt of the Company's revenue requirement, because their rates would be raised while the majority or rest of the Company's customers rates would be lowered.

This could essentially cause the thirty (30) affected residential accounts to change out their larger meters for the smaller standard size. The result would be decreased revenue from these customers, with no opportunity for the Company to recover the lost revenues from other customers under the Staff proposal.

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Q. Does the Company believe these meter change outs will occur?

A. Yes.

Q. How many customers does the Company think will make these changes to their water services should the Staff's Rate Design be implemented?

A. After reviewing the detail of the Bill Count and based on the knowledge of our customers, we conservatively estimate at least 50% of the residential accounts will reduce the size of their meter.

Q. Have you calculated what the monthly savings would be for the customers who changed out to the smaller ⅝" – ¾" standard meter?

A. Yes.

To illustrate the savings to the customer, the following tables compare the Staff's recommended Rate Design as it would be applied to the average gallon/month water usage for the Company's Test Year using a ⅝" – ¾" standard meter versus a 1" meter, 1-1/2" meter, and 2" meter.

1" - 17,000 Average Gallons/Month Billing

Meter	Commodity Rates		Usage	Water Cost	Monthly Usage	Total
⅝"-¾"	0.95	0-4,000 Gallons	4,000	3.80		
	1.15	4,001-23,000 Gallons	13,000	14.95	9.05	27.80
1"	1.15	0-40,000 Gallons	17,000	19.55	22.50	42.05

The difference would be a savings of $14.25 per month should the customer choose to change their meter.

1 ½" - 54,000 Average Gallons/Month Billing

Meter	Commodity Rates		Usage	Water Cost	Monthly Usage	Total
⅝"-¾"	0.95	0-4,000 Gallons	4,000	3.80		
	1.15	4,001-23,000 Gallons	19,000	21.85		
	1.35	23,001 + Gallons	31,000	41.85	9.05	76.55
1 ½"	1.15	0-100,000 Gallons	54,000	62.10	53.00	115.10

The difference would be a savings of $38.55 per month should the customer choose to change their meter.

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2" - 11,000 Average Gallons/Month Billing

Meter	Commodity Rates		Usage	Water Cost	Monthly Usage	Total
⅝"-¾"	0.95	0-4,000 Gallons	4,000	3.80		
	1.15	4,001-23,000 Gallons	7,000	8.05	9.05	20.90
2"	1.15	0-150,000 Gallons	11,000	12.65	66.00	78.65

The difference would be a savings of $57.75 per month should the customer choose to change their meter.

If fifteen (15) of the thirty (30) larger meter residential customers changed out, the monthly revenue loss to the Company would be $296.25, and annually the loss would be $3,555. Add $296 annually to that loss amount for each change out over those fifteen (15) customers.

As a result of changing out their meters, the fifteen (15) customers accounts would no longer be generating the revenues that the Staff has assumed would be available to offset the reduced rates, which Staff has proposed for the majority of customer accounts.

Thus, under the Staff's recommended Rate Design, there would be no way to make-up this loss or generate a positive cash flow.

Q. Has the Company considered the incentives to encourage conservation of water?

A. Yes.

In our preparation of the Company's Rate Case Application, we concluded that we would best serve our customer base and the goal of conservation by proposing a two-tier rate design primarily focused on water usage. That is, billing the customer for the amount of water they actually use per month.

Q. Do you still believe that is the appropriate Rate Design for this water company's system?

A. Yes, we do; and, for the reasons indicated, we believe that the Staff's Rate Design proposal is not.

Q. Does this conclude your rebuttal testimony?

A. Yes.

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Original and fifteen (15) copies of the foregoing were filed this 17th day of September, 2004 with:

Arizona Corporation Commission
Docket Control
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Tucson, Arizona 85701

Copies of the foregoing mailed/emailed this 17th day of September, 2004 to:

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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

MARC SPITZER, Chairman
WILLIAM A. MUNDELL
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ARIZONA CORP. COMM.
TUCSON, AZ.

IN THE MATTER OF THE APPLICATION OF LAS QUINTAS SERENAS WATER CO. FOR A RATE INCREASE

DOCKET NO. W-01583A-04-0178

REBUTTTAL TESTIMONY OF DALE R. CALVERT

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INTRODUCTIONS AND QUALIFICATIONS

Q. Please state your name and address?

A. My name is Dale R. Calvert. My business address is 2970 N. Swan Road #220, Tucson, Arizona 85712.

Q. What is your profession and background?

A. I am a Certified Public Accountant and am self-employed, providing accounting services to utility companies as well as general accounting services. I have a B.S. in Accounting from the University of Arizona (1970).

Q. Could you briefly summarize your prior work and regulatory experience?

A. Yes, I have been in private practice since 1979 where I have provided accounting and tax services to several water utilities including Rincon Ranch Estates Water Co., Inc., K & V Enterprises, Inc., Nicksville Water and Las Quintas Serenas Water Company. I have prepared several rate cases for Rincon Ranch Estates Water Co. and I am an Officer and Director of that

Company. Prior to entering private practice I was employed by Norman and Evans, Ltd., CPA's where I annually worked on the audit of the Salt River Indian Community. As a part of that work I did the audit tests on their water utility. After that I was employed by Riordan, Crouse and Collins, CPA's in Tucson where I annually did the audit of the Flowing Wells Irrigation District.

Q. On whose behalf are you testifying in this procedure?

A. I am testifying in this procedure on behalf of Las Quintas Serenas Water Company ("LQS" or "the Company"). Las Quintas Serenas Water is seeking increases in its rates and charges for utility service for their franchise area located in Pima County north of the unincorporated community of Green Valley and south and west of the Town of Sahuarita.

Q. What is the purpose of your rebuttal testimony?

A. To provide testimony regarding adjustments and issues raised by the staff in its direct testimony and report.

PLANT IN SERVICE AND ACCUMULATED DEPRECIATION

Q. The Staff has recommended a $942 adjustment in the plant in service at the end of the test period and $2,935 increase in the accumulated depreciation that was calculated by the Company. Do you have any comment on these adjustments.

A. The Company accepts the adjustments proposed by the staff and wishes to thank the staff for their diligent efforts in reviewing over $1,000,000 of plant additions over an eighteen year period of time.

METER ADVANCES

Q. The Staff has reduced the rate base by the $31,649 of meter advances. Do you agree with this adjustment.

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A. Yes

DEFERRED INCOME TAX CREDITS

Q. The Staff has reduced the rate base by $1,191 for deferred income tax credits. Do you agree with this adjustment.

A. Yes

OPERATING EXPENSES

Q. The Staff has proposed an adjustment of the claimed Salaries and Wages of $2,065. Is the Company in agreement with that adjustment?

A. No the Company does not agree with that adjustment. Staff cites the Company Board of Directors minutes for the approved rates, but fails to reflect that the Board of Directors have also approved a policy of time and a half for after hours call out work and approved raises during the year for the employees. In addition, in regard to Kaycee Conger, staff used her base rate of pay without her hourly allowance for fringe benefits. However, Staff confirms the accuracy of the Company records by showing that their analysis determines only a 1.85% differential from the Company records even though they did not include all the factors used in calculating the employee's compensation. Accordingly, the full $111,468 of compensation should be allowed.

Q. The Staff has proposed an adjustment of $9,931 to the Repairs and Supplies for the cleaning of a well because the expense is extraordinary and will not be repeated in the foreseeable future. Do you agree with that adjustment?

A. We agree that an adjustment is appropriate because cleaning out a well is maintenance work that will not be done on an annual basis. However, considering the age of the Company's wells we do not agree that the Company will not incur similar well cleaning expenses on this or

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other wells in the future. In fact, I have been advised that the Company expects that within the next 4 years that it will incur similar well cleaning expenses so we feel that this item ought to be normalized over that number of years. Thus, $2,483 of the $9,931 should be allowed to be added to the other repairs and supplies expenses.

Q. The Staff has proposed that Water Testing Expense be adjusted by $752. Do you have a comment on this adjustment.

A. Steve Gay the Operator/Manager of the Las Quintas Serenas will have further comment on this issue in his testimony. The required tests for health purposes are minimum standards to protect the health of the system and there are many instances where the operator may in his judgment make additional tests to better operate the system and assure water quality. There is no assertion by the staff that any of the reported $4,804 of water testing cost was not expended for that purpose, and thus this expense should have been allowed by the staff.

Q. The Staff has proposed adjusting the Rate Case Expense from $6,000 to $2,000. Do you agree with that adjustment?

A. No, for a couple of reasons. First on exhibit C-2 of the Company filing explaining the Company adjustments on exhibit C-1 we explained that the $6,000 was one half of the $12,000 total estimated cost. Consequently the Staff's adjustment (hopefully inadvertently) normalizes the actual cost a second time in effect spreading the cost over six years rather than two or three. Second, we elected to use a two year normalization period rather than a three year because of the high probably that the Company will need to file again for a rate increase within the next year or two. Third, at the time of the audit we discussed with the Staff that the actual expense had already exceeded the $12,000 estimate. Through August 31, 2004 the Company has expended

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$20,058.55 in connection with preparing the application, responding to a number of staff data requests and participating in the staff's field audit. In addition to the amount already expended the Company will incur additional costs related to the preparation for the hearing including our response to the Staffs report and testimony and actual hearing time which is estimated at $12,500. Accordingly, our current estimate of the total cost is $32,558.55. If we adopt the staffs recommended three year normalization period the adjustment should be $10,853.

Q. Staff has adjusted the transportation expense by $2,789. Do you agree with that adjustment?

A. We do not agree with that adjustment. The Staff indicates that the Company had four vehicles, two which were owned by the Company and two which were owned by employees who were paid mileage for the use of those vehicles. Accordingly, they concluded the mileage reimbursement for the vehicle owned by Steve Gay, the Operator/Manager of the system and his wife Janice, should be disallowed. The payments were made to Mrs. Gay because several years ago the Company's former accountant erroneously had included those payments in Mr. Gay's W-2 as part of his taxable income so at that time the Company adopted the policy of writing the checks to Mrs. Gay to avoid confusion.

What the staffs analysis ignores is that the Company acquired the second owned vehicle on June 20, 2003 of the test year that ended September 30, 2003 and terminated the mileage reimbursement arrangement with Mr. Gay at that time. Accordingly, the Company did not operate a fourth vehicle except for the inevitable transition period when moving from one vehicle to another. If an adjustment is going to be made it should include both the removal of Mr. Gay's reimbursement and the annualization of the costs of the truck acquired during the year.

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Q. The Staff recommends an adjustment to the Miscellaneous Expense of $673 for out of state long distance telephone calls. Do you agree with that adjustment?

A. We do not agree with that adjustment for a couple of reasons. First we were unable to determine how the Staff arrived at $673 of out of state long distance charges. The Company created their own analysis of the telephone bills and determined that there were only $102 out of state long distance charges out of total long distance charges of $296 during the test period. Secondly, stating that it is not an appropriate expense for the Company to make out of state long distance calls arbitrarily assumes only in-state calls are business related. A review of the identified telephone calls shows that many were made to customers of the system who were either moving into or out of the Company service area, own rental properties in the service area or had business with the Company because they leave their property for extended periods of time and were out of state at the time. In addition many of the calls were made to vendors such as Symantec an international software company, Rockwell Automation and other venders.

Q. Staff has adjusted the Company Depreciation calculation of $52,949 by $5,082 to a staff proposed amount of $47,867. Do you wish to comment on this adjustment.

A. In the last rate case for the Company in 1984 the Commission had approved the Company use of a composite twenty year life for all assets. As a part of our application we requested that this depreciation method be modified to Arizona Corporation Commission approved current rates. We had already adjusted the depreciation amount for the test year by $14,642 in our exhibit C-1 from the expense under the old rates of $67,591 in anticipation of this change. Accordingly, we agree with this adjustment.

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Q. The staff has adjusted the property taxes by $1. Do you wish to comment on this adjustment.

A. No

Q. The Staff has increased the Federal and State Income Tax Expense by $4,654. Does the Company agree with that adjustment?

A. Yes

RATE OF RETURN

Q. The Staff has determined that the capital structure is 100 percent equity. Do you agree with that determination?

A. I agree that it reflects the current capitalization of the Company. But considering the Company needs for capital investment associated with arsenic treatment and other growth needs I would expect the Company to be requesting a modification of that situation in the near future. In that regard, in his rebuttal testimony, Steve Gay indicates that the Company is considering requesting Commission approval to incur debt to fund its capital facilities investment for arsenic treatment. In addition, as the Company approaches 1,000 customers, with substantial additions in the foreseeable future, it is reasonable that its capital structure will move towards a combination of debt and equity. In this regard, as the staff cost of capital witness has testified, (1) as a company increases its debt, its cost of equity increases, and (2) the average capital structure for the sample water utilities he used in this case is 50.3 percent equity and 49.7 percent debt. These considerations are worth noting in terms of what might be an appropriate capital structure for this company prospectively, as well as its cost of capital.

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Q. The Staff has recommended an overall rate of return of 8.5%. Do you wish to comment on that determination.

A. Yes we agree with a 8.5% rate of return for this rate case.

Q. What would be the Adjusted Operating Income (Loss) be if the modifications to which you have testified above were made to line 2 of staffs exhibit ENZ-1?

A. Operating expenses would be increased by $15,550 which consists of $2,483 of repairs, $752 of water testing, $8,853 of rate case expenses, $2,789 of transportation and $673 of telephone. The total of $15,550 would decrease the Adjusted Operating Income from $13,659 to an $1,891 Adjusted Operating Loss. Under these circumstances, a slight increase in rates would appear to be in order.

Q. Does this conclude your testimony?

A. Yes

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Original and fifteen (15) copies of the foregoing FILED this 17th day of September, 2004 with:

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Copies of the foregoing mailed/emailed this 17th day of September, 2004 to:

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BEFORE THE ARIZONA CORPORATION COMMISSION

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TUCSON, AZ

COMMISSIONERS

MARC SPITZER, Chairman
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
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KRISTIN K. MAYES

IN THE MATTER OF THE APPLICATION OF LAS QUINTAS SERENAS WATER CO. FOR A RATE INCREASE	))))))	DOCKET NO. W-01583A-04-0178 **REBUTTAL TESTIMONY OF STEVE GAY**

MUNGER CHADWICK, P.L.C.
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INTRODUCTION

Q. Please state your name and business address.

A. My name is Steve Gay. My business address is 75 Calle de las Tiendas, Suite 115B, Green Valley Arizona 85614. My business mailing address is P.O. Box 68, Sahuarita Arizona 85629.

Q. By whom are you employed and in what capacity?

A. I am employed by Las Quintas Serenas Water Company (LQS). I am their Operator/Manager.

Q. Please describe your work experience.

A. After graduating from high school I worked for Anaconda/ANAMAX mining company for twenty (20) years as a mechanic and electrician. In this position I worked with hydraulics, water systems, pumping systems, electric and electronic control systems, etc.

In 1983, John Gay and I responded to an RFP for proposals to conduct the operations of LQS and we were awarded the contract by ANAMAX Mining Company to run LQS Water Company. I subsequently attended Pima College for a course on Water and Wastewater; I passed this course and subsequently tested for Grade I Water, Water Treatment, Wastewater and Wastewater Treatment. I passed these tests. A year later, I tested and passed the tests for Grade II in each of these four (4) areas. My operator number is 03833.

From 1983 until approximately ten (10) years ago, my employee responsibilities with LQS were of a part time nature. During this same time period I also worked for Quail Creek Water Company as an Operator for about five (5) years; Rancho Sahuarita Water Company as an Operator/Manager for about seven (7) years; Sahuarita Schools as an Operator for eight (8) years, as well as other small water companies.

During the last ten (10) years, I have served as LQS Operator/Manager on a full time basis. In addition, I continue to devote between eight (8) to ten (10) hours per month towards assisting Sahuarita Schools and other small water systems.

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Q. What is the purpose of your testimony in this proceeding?

A. First, to provide an overview of the LQS system from an operational perspective. Second, to provide certain testimony, which is intended to rebut some of the testimony and conclusions set forth in the Commission Staff's August 20th testimony and exhibits.

SYSTEM OVERVIEW

Q. How does the LQS system work?

A. LQS has three (3) isolated wells all pumping directly into the distribution system. These wells are within one (1) mile of each other.

#5 Well was drilled in 1968 by Anaconda Mining Company to 533 feet using 10" casing. The Well was deepened in 1976 to 807 feet by Anaconda with 8" casing.

#6 Well was drilled in 1971 by Anaconda Mining Company. This well was drilled to 837 feet with a 12" casing.

#7 Well was drilled in 1998 by LQS to a depth of 920 feet with a 12" casing.

There are 90,000 gallons of storage acting as a buffer to the system (i.e. should the pumping capacity of the wells exceed the demand on the system at any given time the storage tanks fill, likewise, should the pumping capacity not meet the demand on the system at any given time, the water stored in the tanks will make up the difference).

The system is controlled by a radio control system (SCADA) that monitors the storage tank level and controls the well pumping activity based on the monitoring data.

The distribution lines of the Company's water system, as set forth in the ACC Annual Report for 2003, is made up of 3,290 ft. of 12" main, 4,228 ft. of 8" main, 55,303 ft. of 6" main, 24,349 ft. of 4" main, and 1,800 ft. of 2" main.

Q. How many customers did LQS have during the test year?

A. There were about 804-metered customers averaged in the test year. This includes 674 services and 130 individually metered standpipe customers. These numbers come from the bill count in the test year.

Q. Does LQS have the well production and storage facilities necessary to serve its current and projected customer load(s)?

A. No.

As illustrated in the tables below, LQS is 72,000 gallons short in meeting the maximum daily demand placed on the system by the current customer base alone should the system lose the production capacity of the #7 Well.

With approximately 900-metered customers (2004) LQS presently has a maximum demand of 750 GPM.

	Bulletin #10 Formula	
900 customers		Instantaneous Demand
176 @ 231 GPM		231 GPM
724 Customers x 0.7	*GPM*	506 GPM
#5 Well	**200 GPM**	

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#6 Well	**425 GPM**
60,000 Gallon Storage (Usable)	**62 GPM**
(60,000/60 Min/*16 hrs = 62.56 GPM)	**687 GPM Capacity (IF #7 Well is down)**
***16 hrs = Nature of Peak Demand**	

737 GPM Minimum Capacity Requirements
687 GPM Maximum Available IF #7 Well is down
50 GPM Short
X 60 Minutes
X 24 Hours
72,000 Gallons Short for Storage (2004)

Current System Capabilities:

Storage (60,000 Gallons Usable)	62 GPM	62 GPM
#5 Well	200 GPM	200 GPM
#6 Well – Electric		325 GPM
#6 Well – Natural Gas	425 GPM	
#7 Well	850 GPM	850 GPM
	1,537 GPM	1,437 GPM

Q. Does the company anticipate growth?

A. Yes.

Q. Please describe the nature and size of the growth anticipated.

A. LQS has a number of existing and projected subdivisions within its franchise in various stages of development and is considering the possibility of expanding its current franchise boundaries. The following table describes the Company's anticipated growth.

Projected Growth (Within LQS Franchise Boundaries)

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Developed Subdivision(s) with Available Lots

Colonias @ La Canada	03 Lots/Year	02 GPM
Rancho Buena Vista	04 Lots/Year	03 GPM
Mesquite Heights	23 Lots/Year	16 GPM
Estates @ La Canada	29 Lots/Year	20 GPM
Various (Old) Subdivisions	15 Lots/Year	11 GPM
Standpipe Customers	07 Lots/Year	05 GPM
Platted Subdivision(s) – Approved to Construct (PDEQ)		
Santa Cruz Meadows	239 Total Lots	167 GPM
Vacant – Undeveloped Land		
Park / Anamax	200 Total Lots	140GPM
AZ State Trust Foundation	80 Total Lots	56 GPM
Second Pressure Zone		
Woodward	50 Total Lots	35 GPM
Kittle/Park Corporation	50 Total Lots	35 GPM
Proposed / Anticipated Growth (Expansion of LQS Franchise Boundaries)		
Third Pressure Zone		
Park/Aries/Ruby Star	3,000 – 5,000 Total Lots	2,800 GPM

Q. What are the indicated increases in storage capacity and production capacity to serve that growth?

A. The Buck Lewis Engineering Report was designed to take the Company to complete build-out of the franchise (1 x 2 mile CC&N with approximately 1,500 service connections including standpipe).

According to Mr. Lewis, the built-out franchise would require either 900,000 gallons of storage or one (1) new well and at least 600,000 of storage. (it has been noted in previous testimony that LQS opted for the additional well (#7) and at least 600,000 gallons of storage).

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Q. Has the Company made proposals to fund portion of additional growth?

A. Yes.

We proposed an increase from $250 to $500 in the Off-Site Facilities Hook-Up Fee to help offset costs.

Q. What has Staff recommended with regard to that proposal?

A. That no increase be made to the Off-Site Facilities Hook-Up Fee.

Q. What was Staff's reasoning?

A. The Staff reasons that the system has adequate production and storage capacity to support the existing customer base, including standpipe customers.

The Staff also refers to a statement made on page 7 of the Buck Lewis Engineering Report provided by the Company at the time of the Staff's Data Request dated June 9, 2004, in which Mr. Lewis notes that "An additional 200,000 gallons of storage is recommended which should consist of two (2) 100,000 gallon tanks", by proposing in their testimony that "...the approved hook-up fee amount of $250 per new connection should be sufficient to fund the purchase and installation of two (2) new 100,000 gallon storage tanks..."

Q. Does the Company believe staff is wrong, and, if so, why?

A. Yes, we believe the Staff is wrong.

The Company currently has only 90,000 gallons of storage (60,000 gallons – usable). In order for us to meet the current demands on the system and the projected growth of the Company's customer base we will need at least 900,000 gallons of storage, as set forth on page 6 of the Buck Lewis Report that states; "...build-out additional storage is about 900,000 gallons. To offset some of the storage, at least one additional well is recommended. Furthermore, a well...can substitute for 500,000 gallons of storage in a multiple well system." The Company opted to satisfy this recommendation by drilling

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the #7 Well in 1998 and offsetting the 900,000 gallon storage recommendation by 500,000 gallons. The two (2) 100,000 gallon tanks proposed by the Staff are in addition to the build-out storage capacity of 900,000 gallons as set forth in the Buck Lewis Report in it's entirety (pages 6 & 7) or the 600,000 gallons needed by the Company. The storage capacities the Company is proposing (i.e. 500,000 gallons and 150,000 gallons equaling 650,000) will replace the existing 90,000 gallons of storage and will support the current customer base and the projected growth.

HOOK UP FEES

Q. Why does the Company want to raise its current Hook-Up Fees?

A. LQS is proposing an increase in the Off-Site Facilities Hook-Up Fees from $250 to $500, for the reasons listed below;

Balance of #7 Well Addition Construction Costs	$	76,000.00
Note: Balance due to the Company for funds provided to pay for #7 Well Construction. There were not enough moneys collected through the current Off-Site Facilities Hook-Up Fees to pay for the Well addition to the system.		
Proposed Additions to Storage – 500,000 Gallons @ #3 Tailings	$	310,000.00
Proposed Additions to Storage – 150,000 Gallons @ #6 Well	$	200,000.00
Note: Storage requirements as per the Buck Lewis Engineering Report dated September 1991 (pages 6-7). Please refer to previous testimony for further detail. Costs for additional storage are projected.		
Total Amount Needed	**$**	**586,000.00**
Estimated Revenue from proposed Off-Site Facilities Hook-Up Fees		
300 Additional homes in approximately next three (3) years		
300 @ $500.00	$	150,000.00
500 Additional homes over the next four (4) to twenty (20) years		
500 @ $500.00	$	250.000.00
Total provided from proposed Off-Site Facilities Hook-Up Fees	**$**	**400,000.00**

WATER TESTING

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Q. Why does the Company test the water?

A. LQS, by law, must take a number of water samples per month. In addition to the required water samples, LQS has opted to take extra bacteria samples throughout the year to assure that any and all repairs to the system do not contaminate the water supply. Should one (1) sample test positive for bacteria an additional five (5) samples are then required to be taken after the water is treated to assure that the bacteria has been removed.

LQS has been tracking the arsenic levels on a monthly basis throughout the system in order to collect data and ultimately record any trends that may appear.

LQS has also been taking the arsenic samples to assist the arsenic media manufacturers in their bids to provide the arsenic remediation for the Company.

LQS is also tracking the sulfates within the system because the water company to the South of LQS (Community Water) is currently dealing with sulfates at high levels, causing complaints.

In my professional judgment, all of the water samples were necessary.

ARSENIC REMOVAL

Q. Does the Company have an arsenic problem that must be remedied by January 2006?

A. Yes.

Arsenic levels have been rising over the last couple of years and now are 11 PPB (#5 Well), 15 PPB (#6 Well), and 13 PPB (#7 Well).

Q. What has the Company done to investigate a remediation program?

A. Because the #5 Well had been historically under 10 PPB arsenic for over fifteen (15) years of testing, LQS was looking into the option of re-drilling #5 Well or drilling a new well next at the #5 Well site. This was discouraged by Errol L. Montgomery & Associates; Consultants in Hydrogeology, Phelps Dodge Sierrita Senior Hydro-geologist Lee Wilkening, and Malcolm Pirnie, Engineering and Consulting. Their joint concern

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was that actually being able to get low arsenic concentrations out of a well at the #5 Well site was not assured and there is a possibility that the #5 Well will be impacted by sulfates in the next few years.

Malcolm Pirnie did a study for the Company in arsenic remediation Spring/Summer 2004. They proposed four (4) different options with the capital associated with these options ranging between $1,080,000 dollars to $1,280,000 dollars and yearly operation expenses ranged from $166,000 dollars to $318,000 dollars.

I might note that Malcolm Pirnie was the engineering company that did the ADEQ Arsenic Master Plan.

In addition, the Company has requested proposals from several other consulting firms, which would involve alternative remediation approaches or using similar approaches with different medias. We have just recently received those proposals and are in the process of reviewing them. LQS is also receiving information from the Arsenic Remediation Coalition, Arizona Small Utilities Association, Arizona Water Utilities Association, Arizona Water and Pollution Control Association, etc.

Q. How does the Company intend to pay for the arsenic remediation treatment methodology it ultimately selects?

A. At present, our thinking is that we will probably request approval from the Commission to borrow the funds for the capital facilities. We may also seek rate authorization to recover projected operating costs in a future proceeding.

Q. Will the Company's arsenic compliance program be in place as of December 2004 as the ACC's Staff witness appears to assume?

A. LQS intends to submit a progress report to the ACC at that time; however, its facilities will probably not be installed at that time. The Company fully expects to be in compliance by January 23, 2006.

Q. Does this conclude your rebuttal testimony?

A. Yes.

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