

ORIGINAL



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MEMORANDUM

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TO: Docket Control

FROM: Ernest G. Johnson  
*for* Director  
Utilities Division

DATE: February 17, 2005

RE: STAFF REPORT FOR AERIE CONSERVANCY, AN ARIZONA NON-PROFIT CORPORATION, FOR ADJUDICATION NOT A PUBLIC SERVICE CORPORATION (DOCKET NO. W-04291A-04-0843)

Attached is the Staff Report for Aerie Conservancy application for adjudication not a public service corporation. Staff recommends the Commission approve the application with conditions.

EGJ:JEF:cal

Originator: Jim Fisher

Attachment: Original and Thirteen Copies

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Arizona Corporation Commission  
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Docket No. W-04291A-04-0843

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**STAFF REPORT  
UTILITIES DIVISION  
ARIZONA CORPORATION COMMISSION**

**AERIE CONSERVANCY  
AN ARIZONA NON-PROFIT CORPORATION**

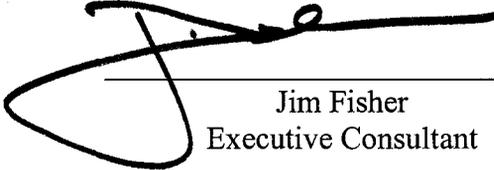
**DOCKET NO. W-04291A-04-0843**

**APPLICATION FOR ADJUDICATION  
NOT A PUBLIC SERVICE CORPORATION**

**FEBRUARY 2005**

## STAFF ACKNOWLEDGMENT

The Staff Report for Aerie Conservancy, an Arizona Non-Profit Corporation, (Docket No. W-04291A-04-0843) was the responsibility of Jim Fisher. Jim Fisher was responsible for the review and analyses of the application.



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Jim Fisher  
Executive Consultant

**EXECUTIVE SUMMARY  
AERIE CONSERVANCY  
DOCKET NO. W-04291A-04-0843**

On November 24, 2004, Aerie Conservancy, (“Aerie” or “Association”) an Arizona Non-Profit Corporation, filed an Application for an Adjudication Not a Public Service Corporation with the Arizona Corporation Commission (“ACC” or “Commission”) to provide potable water service to a proposed subdivision of 78 residents in Yavapai County. The Aerie is requesting a determination that it is not a public service corporation for purposes of utility regulation by the ACC.

The criteria to determine that a provider is not a public service corporation within the meaning of Article XV, Section 2, of the Arizona Constitution was reviewed by the Arizona Supreme Court in Natural Gas Service Company v. Serv-U Cooperative, Inc. The Court provided eight review criteria for the Commission to review. The Commission issued a policy directive for the evaluation of applications for adjudication not a public service corporation on May 7, 1987, in Decision No. 55568.

The Aerie has filed proposed CC&Rs that currently comply with five (5) of the Commission’s seven (7) criteria for adjudication.

The Association is a non-profit corporation requesting adjudication, supported by the current members. The Association provides equal voting rights among the members/customers, and restricts total membership to seventy-eight (78). Further subdivision is prohibited, and the Association is unable to obtain other water service.

However, the Association does not own the utility assets, and the property is not strictly prohibited from expansion. In addition, the Association will need to obtain ADEQ and ADWR approvals for water supply and system construction.

Staff recommends the Commission approve the Aerie Conservancy’s application for adjudication not a public service company subject to the following conditions:

1. That the Aerie Conservancy file with Docket Control a strict prohibition for further expansion of the property to be served by the Association.
2. That the Aerie Conservancy file with Docket Control documentation demonstrating ownership of the utility assets required to serve the Association.
3. That the Aerie Conservancy file with Docket Control a copy of the Arizona Department of Environmental Quality Approval to Construct the proposed water system.
4. That the Aerie Conservancy file with Docket Control a copy of the Arizona Department of Environmental Quality Approval of Construction for the water system.

5. That the Aerie Conservancy file with Docket Control a copy of the Arizona Department of Water Resource's Letter of Adequate Water Supply for service to the Association.
6. That the Aerie Conservancy file with Docket Control a copy of the final recorded plat.
7. That the Aerie Conservancy comply with all of the above requirements prior to obtaining a public report for marketing the property with water service to the public.

Staff further recommends that the Commission's decision granting this adjudication not a public service company to the Aerie Conservancy be considered null and void without further order from the Commission should the Aerie Conservancy fail to file the required documentation by December 31, 2006.

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## **Introduction**

On November 24, 2004, Aerie Conservancy, (“Aerie” or “Association”) an Arizona Non-Profit Corporation, filed an Application for an Adjudication Not a Public Service Corporation with the Arizona Corporation Commission (“ACC” or “Commission”). On December 7, 2004, Staff informed the Association that the application was sufficient for administrative processing.

Aerie is a non-profit corporation, established to provide potable water service to a proposed subdivision of 78 residents, approximately 1 mile south of Boyton Pass, west of the City of Sedona, in Yavapai County. The Aerie is requesting a determination that it is not a public service corporation for purposes of utility regulation by the ACC.

## **Background**

The Aerie is a planned development of Communities Southwest Holdings, LLC, (“Communities Southwest”) a master planned community developer. According to Commission records, Communities Southwest’s directors are Denro Arizona, Inc., Demajeka, LLC, and Athansor, Inc.

Communities Southwest will purchase the proposed development property through an affiliate, Red Rock Aerie, LLC. According to Commission records, Red Rock Aerie, LLC’s directors are the same as Communities Southwest, i.e., Denro Arizona, Inc., Demajeka, LLC, and Athansor, Inc.

Red Rock Aerie, LLC is under contract to purchase 2 parcels of approximately 177 acres total which are currently owned by Sedona Tree Farm Limited Partners, Sedona Red Rock Land Limited Partnership, Pegasus, Arizona General Partners and KFT, LLP.

Red Rock Aerie, LLC is seeking to entitle the property for water service by obtaining a decision by the Commission that the Association’s future water service to 78 connections will not make it a public service corporation for purposes of utility regulation by the ACC. The Association was formed, in part, for the purpose of providing water service to the homeowners who will be residing in the proposed subdivision.

The criteria to determine that a provider is not a public service corporation within the meaning of Article XV, Section 2, of the Arizona Constitution was reviewed by the Arizona Supreme Court in Natural Gas Service Company v. Serv-U Cooperative, Inc. The Court provided eight review criteria for the Commission to review.

1. What the corporation actually does.
2. Whether the service is dedicated to a public use.
3. That the articles of incorporation evidence authorization and purposes.

4. Whether the corporation is dealing with the service of a commodity in which the public has been generally held to have an interest.
5. Whether the corporation is monopolizing or intending to monopolize a territory with a public service commodity.
6. Whether the corporation is accepting of substantially all requests for service.
7. That service is under contract and reserving the right to discriminate is not always controlling.
8. Whether the corporation will have actual or potential competition with other corporations whose business is clothed with the public interest.

The Commission issued a policy directive for the evaluation of applications for adjudication not a public service corporation on May 7, 1987, in Decision No. 55568. The Utilities Division was directed to ensure that all such applications complied with the following seven criteria.

1. Adjudication applications must be submitted by a non-profit homeowners association.
2. The application for adjudication not a public service corporation is a bona fide request by a majority of the membership of the association through a petition signed by 51 percent or more of the then existing members.
3. That all such associations making such application have complete ownership of the system and necessary assets.
4. That every customer is a member/owner with equal voting rights and that each member is or will be a customer.
5. That the service area involved encompasses a fixed territory, which is not within the service area of a municipal utility or public service corporation; or if in such territory, that municipal utility or public service corporation is unable to serve.
6. That there is a prohibition against further sub-division evidenced by deed restrictions, zoning, water restrictions or other enforceable governmental regulations.

7. That the membership is restricted to a fixed number of customers actual or potential.

### **Compliance with Directives 1 and 2**

The Aerie incorporated as an Arizona non-profit corporation on November 3, 2003. The Aerie is a non-profit homeowners association as required by the Commission's policy directive. Staff understands the Commission's policy directive was to ensure the adjudicated system was not for profit, separate from the developer and governed by its members. The Association meets that criteria as understood by Staff.

The directors of the Association are currently the employees of the Communities Southwest. The developer has not sold any lots in the development, therefore, there are no customers/members to support or oppose the application. Currently, the developers are acting on behalf of the eventual customers/members as directors of the Association.

On November 24, 2004, acting in the capacity of directors for the Association, employees of Communities Southwest, Mr Suriano, Mr. Pennypacker and Ms. Schulman adopted a resolution approving this application for adjudication. In addition, Brian De Hegardt, President of Communities Southwest, provided a letter of support dated November 24, 2004. Also, the current property owner filed a letter supporting the request for adjudication. (See Directive #1 and #2 on page 2)

### **Non-Compliance with Directive 3**

A preliminary water design report was prepared to support the developer's request for preliminary plat approval and included in the present application. According to the preliminary design report, an existing well, with a depth of 1,209 feet is located on the site and has a production capacity of 245 gallons per minute ("GPM"). The design report states 60,000 gallons of storage will be included. System demand has been calculated to include 250 gallons per day usage per capita and reflect fire flow of 500 GPM for 2 hours as required by the Sedona Fire Marshall.

The design report also states that the water quality was tested and meets Arizona Department of Water Resources standards. The water quality also meets the new arsenic standard effective in January 2006 according to the same document.

According to Attachment L of the Application, Phase I of the water system is expected to cost \$1,254,234 and Phase II is to cost \$413,210.

In addition to the above, the design report also provides that the property was previously authorized a water demand of 418 acre feet per year when the property was a proposed golf course. As currently designed, the property will use less than 15 percent of that water,

approximately 59 acre feet per year for the domestic and non-potable usage associated with the decorative lake.

The Association is to have wastewater provided separately by each lot owner through a "MicroSeptic" system. Permitting is the responsibility of each lot owner.

The Aerie has provided a copy of an unexecuted bill of sale for the proposed utility assets that are currently planned for construction if the development moves forward. According to the proposed bill of sale, Red Rock Aerie LLC, will transfer the domestic and non-potable water systems to serve the proposed subdivision to the Association. (See Attachment K to the Application)

The Association has not demonstrated compliance with Directive 3 as the assets are not owned by the Association. Staff recommends the Commission condition approval of the application that water is available, deliverable to state standards by a system owned by the Association.

Staff recommends that the Commission require the Association to demonstrate that an appropriate water resource is available to service the expected demand of the proposed subdivision. The Association should be required to file a copy of the appropriate Arizona Department of Water Resources ("ADWR") Letter of Adequate Water Supply by December 31, 2006.

Staff recommends that the Commission require the Association to demonstrate that an appropriate water system is constructed to serve the Association. The Association should be required to file a copy of the Arizona Department of Environmental Quality ("ADEQ") Approval to Construct for the water system by December 31, 2006. Staff also recommends that the Association file a copy of its compliance with ADEQ's capacity development rules by December 31, 2006.

Staff also recommends that the Association should be required to demonstrate that the water system has been conveyed to the Association by December 31, 2006.

#### **Compliance with Directive 4**

The Association filed a draft copy of its proposed Codes, Covenants and Restrictions ("CC&Rs") to govern management and members' rights in the Association. The CC&R's explicitly provide the developer with control of the project until all property is sold, or the developer relinquishes control.

The proposed CC&R's provide complete control to the developer to appoint the board, set regular assessments, special assessments and loan the association funds for improvements.

The water system, however, is treated separate and apart from the rest of the development according to Section 2.22 of the proposed CC&Rs, which states in part:

Water System Matters. Notwithstanding anything contained in this Declaration, the Articles or the Bylaws to the contrary, in the event of any vote with respect to any Water System, each Owner shall be entitled to cast one vote for each Lot owned by such Owner. Notwithstanding the foregoing, Declarant shall not have the right to cast votes with respect to Water System Matters pursuant to Section 2.14 of the Declaration.

Section 2.22 seems to comply with the Commission's policy directive. However, as the developer will appoint the Board of the Association and numerous matters for the water system may be controlled by the Board of the Association, the developer may act contrary to Commission policy for adjudication. (See Directive #4 on page 2).

#### **Non-Compliance with Directive 5**

The requested property is small, approximately 177 acres, with no room to expand as it borders the Coconino National Forest. The property is not within a municipal boundary, nor adjacent to an existing water utility.

In Section 1.1 of the proposed CC&R's, the property subject to the CC&R's the property boundaries are not defined either by general boundaries or a legal description within the document.

Staff believes the property to be served should be defined, and an express prohibition on future expansion should be provided, thereby limiting the size of the development to comply with Commission policy. (See Directive #5 on page 2).

#### **Compliance with Directive 6**

The proposed CC&Rs include Section 11.16 No Further Subdivision which states in part, "following recordation of the Plat for the Parcel, no lot shall be divided or subdivided." (See Directive #6 on page 2).

Staff would recommend that the Association be required to file a copy of the final recorded plat by December 31, 2006.

#### **Compliance with Directive 7**

The membership of the Aerie is restricted to a fixed number of members/customers. According to the proposed CC&R's, Section 2.2, Membership in Association states in part, "the total number of Lots in the Parcel and the total number of votes shall not exceed 78 (See Directive #7 on page 2).

## **Summary**

The Aerie has filed proposed CC&Rs that currently comply with five (5) of the Commission's seven (7) criteria for adjudication.

The Association is a non-profit corporation requesting adjudication, supported by the current members. The Association provides equal voting rights among the member/customers, and restricts total membership to seventy-eight (78). Further subdivision is prohibited and the Association is unable to obtain other water service.

However, the Association does not own the utility assets and the property is not strictly prohibited from expansion. In addition, the Association will need to obtain ADEQ and ADWR approvals for water supply and system construction.

## **Recommendations**

Staff recommends the Commission approve the Aerie Conservancy's application for adjudication not a public service company subject to the following conditions:

1. That the Aerie Conservancy file with Docket Control a strict prohibition for further expansion of the property to be served by the Association.
2. That the Aerie Conservancy file with Docket Control documentation demonstrating ownership of the utility assets required to serve the Association.
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6. That the Aerie Conservancy file with Docket Control a copy of the final recorded plat.
7. That the Aerie Conservancy comply with all of the above requirements prior to obtaining a public report for marketing the property with water service to the public.

Staff further recommends that the Commission's decision granting this adjudication not a public service company to the Aerie Conservancy be considered null and void without further order from the Commission should the Aerie Conservancy fail to file the required documentation by December 31, 2006.