

OPEN MEETING ITEM
ORIGINAL



22

COMMISSIONERS
JEFF HATCH-MILLER - Chairman
WILLIAM A. MUNDELL
MARC SPITZER
MIKE GLEASON
KRISTIN K. MAYES



ARIZONA CORPORATION COMMISSION

DATE: May 9, 2005

Arizona Corporation Commission

DOCKETED

DOCKET NO: WS-02987A-04-0889

MAY - 9 2005

TO ALL PARTIES:

DOCKETED BY	
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Enclosed please find the recommendation of Assistant Chief Administrative Law Judge Dwight D. Nodes. The recommendation has been filed in the form of an Opinion and Order on:

JOHNSON UTILITIES COMPANY
(CC&N EXTENSION)

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:

May 18, 2005

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 Open Meeting to be held on:

MAY 24 and 25, 2005

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

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AZ CORP COMMISSION
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BRIAN C. McNEIL
EXECUTIVE SECRETARY

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 COMMISSIONERS

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

8 IN THE MATTER OF THE APPLICATION OF
9 JOHNSON UTILITIES COMPANY FOR AN
10 EXTENSION OF ITS CERTIFICATE OF
11 CONVENIENCE AND NECESSITY FOR
12 WASTEWATER SERVICE.

DOCKET NO. WS-02987A-04-0889

DECISION NO. _____

OPINION AND ORDER

9 DATE OF HEARING: April 11, 2005
10 PLACE OF HEARING: Phoenix, Arizona
11 ADMINISTRATIVE LAW JUDGE: Dwight D. Nodes
12 APPEARANCES: Mr. Jay Shapiro, FENNEMORE CRAIG, P.C.,
13 on behalf of Applicant; and
14 Mr. Timothy Sabo, Staff Attorney, Legal
15 Division, on behalf of the Utilities Division of
the Arizona Corporation Commission.

16 **BY THE COMMISSION:**

17 On December 14, 2004, Johnson Utilities, LLC, dba Johnson Utilities Company ("Johnson"
18 or "Company") filed with the Arizona Corporation Commission ("Commission") an application for
19 an extension of its Certificate of Convenience and Necessity ("CC&N") to provide wastewater
20 service.

21 On January 5, 2005, the Commission's Utilities Division Staff ("Staff") filed a letter of
22 sufficiency.

23 By Procedural Order issued January 6, 2005, this matter was scheduled for hearing on April
24 11, 2005, and Johnson was ordered to notify all property owners in the affected area of the
25 application and the hearing date.

26 On February 15, 2005, the Company filed a Notice of Compliance with the Customer Notice
27 and Publication requirements set forth in the January 6, 2005 Procedural Order.

28 On March 4, 2005, Staff filed its Staff Report in this matter recommending approval of the

1 application subject to certain conditions.

2 On March 11, 2005, Johnson filed a response to the Staff Report setting forth its areas of
3 disagreement.

4 No requests for intervention were received.

5 On April 11, 2005, a hearing was convened before a duly authorized Administrative Law
6 Judge of the Commission at its offices in Phoenix, Arizona. Johnson and Staff entered appearances
7 through counsel. Representatives of several homebuilders in the proposed CC&N extension area
8 offered comments in support of the extension application and urged expedited consideration. At the
9 conclusion of the hearing, the matter was taken under advisement pending submission of a late-filed
10 exhibit and issuance of a Recommended Opinion and Order.

11 On April 19, 2005, two late-filed exhibits were filed by Johnson.

12 * * * * *

13 Having considered the entire record herein and being fully advised in the premises, the
14 Commission finds, concludes, and orders that:

15 **FINDINGS OF FACT**

16 **Background of Application**

17 1. Johnson Utilities Company is a public service corporation that provides water and
18 wastewater service in Pinal County, Arizona pursuant to an original CC&N granted in Decision No.
19 60223 (May 27, 1997). Subsequent CC&N extensions for water and/or wastewater service were
20 granted to Johnson in a number of other dockets.

21 2. On December 14, 2004, Johnson filed an application seeking to extend its CC&N to
22 provide wastewater service to an area adjacent to the CC&N extension area for which Johnson was
23 recently granted an order preliminary to issuance of a final order. *Arizona Utility Supply & Services,*
24 *LLC/Johnson Utilities Company, Docket No. SW-04002A-02-0837 et al., Decision No. 67586*
25 *(February 15, 2005).* According to representatives of the developers/builders who offered public
26 comment at the hearing, wastewater service in the proposed extension area was originally intended to
27 be provided by Arizona Utility Supply & Services, LLC ("AUSS"). However AUSS was unable to
28 provide service to the extension area due to a number of operational problems that eventually resulted

1 in AUSS filing for bankruptcy (See detailed description of AUSS operational problems in Decision
2 No. 67586, at 4-7).

3 3. The requested extension area includes approximately 640 acres that will be developed
4 into approximately 1,129 lots in four subdivisions, Vineyard Estates (161 lots), Wayne Ranch (423
5 lots), Milagro (140 lots), and Taylor Ranch (405 lots). The extension area is located in Pinal County,
6 and encompasses the entirety of Section 17, Township 2 South, Range 8 East. Johnson currently
7 provides bulk wastewater service to the Vineyard Homeowners Association (“HOA”) on an interim
8 basis due to the inability of AUSS to provide service to the Vineyard Estates subdivision¹.

9 4. Water service for the proposed extension area will be provided by H2O, Inc., which
10 holds a CC&N for water service in the proposed wastewater extension area sought by Johnson.

11 5. By Procedural Order issued January 6, 2005, this matter was scheduled for hearing on
12 April 11, 2005 and Johnson was ordered to publish notice of the hearing and notify all property
13 owners in the affected area of the application and the hearing date.

14 6. On February 15, 2005, the Company filed a Notice of Compliance with the Customer
15 Notice and Publication requirements set forth in the January 6, 2005 Procedural Order.

16 7. No intervention requests were received.

17 8. On March 4, 2005, Staff filed its Staff Report recommending approval of the
18 application subject to compliance with certain conditions.

19 9. On March 11, 2005, Johnson filed a response to the Staff Report proposing an
20 alternative to Staff’s recommendation that the Company should comply with affiliate interest
21 reporting requirements under A.A.C. R14-2-801 (see discussion below regarding affiliate interest
22 reporting requirements).

23 10. A public hearing on the application was held as scheduled on April 11, 2005.
24 Representatives of two homebuilders that are developing property in the proposed extension area
25 appeared at the hearing and offered comments in support of the application (Tr. 5-11). At the
26 conclusion of the hearing, Johnson and Staff were directed to submit a late-filed exhibit following

27 ¹ As indicated in Decision No. 67586, Johnson is currently providing bulk wastewater service to the entirety of the AUSS
28 service area until the conditions described therein are satisfied and a final Order is issued in that docket canceling the
AUSS CC&N and granting Johnson the wastewater CC&N for that service area.

1 negotiations to resolve the disputed affiliate interest reporting issue.

2 11. On April 19, 2005, Johnson and Staff filed a negotiated resolution of the affiliate
3 interest reporting requirements. In response to a directive at the hearing from the administrative law
4 judge, Johnson also filed on April 19, 2005 a copy of a letter sent to an individual who had previously
5 objected to inclusion in the CC&N extension area².

6 **Wastewater Treatment System**

7 12. The proposed extension area will be served by the recently constructed Pecan
8 Wastewater Reclamation Plant ("Pecan Plant"). Wastewater flows from the extension area will be
9 collected by existing 12 inch and 8 inch wastewater lines that will then flow by gravity to the Pecan
10 Plant, which is located approximately one mile south of the extension area.

11 13. The Pecan Plant was issued an Aquifer Protection Permit by the Arizona Department
12 of Environmental Quality ("ADEQ") on May 7, 2004. The Pecan Plant is currently treating
13 wastewater flows at 30 percent of its approximately 1 million gallons per day ("gpd") capacity. At
14 current growth projections, the Pecan Plant is not expected to exceed its current capacity until 2010.
15 However, the Company has filed an application with ADEQ for authority to expand the plant to a
16 capacity of 4 million gpd (Ex. S-1, at 5).

17 14. Pursuant to §208 of the federal Clean Water Act, each state is required to develop and
18 implement area-wide water quality management plans for pollution control purposes. The Central
19 Arizona Association of Governments ("CAAG") has been designated as the area-wide water quality
20 management planning agency for Pinal County. The extension area sought in this proceeding is
21 within the CAAG §208 planning area for Johnson, for service provided by the Pecan Plant, and
22 therefore conforms to the area-wide wastewater plans (*Id.* at 3-4).

23 15. Although the Pecan Plant is still in "start-up mode," initial reports from Staff and
24 ADEQ inspections indicate that the plant is operating in conformance with its design and permit
25 conditions. Staff believes that the wastewater system served by the Pecan Plant can reasonably be
26 expected to develop the necessary sewage treatment capacity to serve the proposed extension area.

27 ² The letter from the Company to Mr. Oliver Wilson stated that Mr. Wilson was not required to take wastewater service
28 from Johnson. Mr. Wilson's property is located within the proposed extension area, but not within any of the
aforementioned subdivisions. Mr. Wilson apparently employs a septic system for wastewater disposal.

1 16. According to Staff, the wastewater utility facilities for the extension area
2 developments will be financed in accordance with A.A.C. R14-2-606, which establishes minimal
3 acceptable criteria for main extension agreements between wastewater utilities and private parties.
4 Main extension agreements generally require the developer of property to design, construct and
5 install necessary backbone facilities, which will then be conveyed to the utility company upon
6 completion and acceptance by the utility. In this case, Johnson and the developers have entered into
7 Line Extension Agreements that set forth detailed plans for construction of the system, as well as
8 specific terms and conditions governing installation, inspection and conveyance of the facilities. The
9 agreement also provides for an annual refund to the developers of five percent of total net revenues
10 from the development until the advance of funds for construction of the facilities is fully refunded.

11 17. Staff indicated that Johnson is in compliance with ADEQ rules for operation, reporting
12 and discharge limits for wastewater facilities; that Johnson has no outstanding compliance issues at
13 the Commission; and that Johnson will serve the extension area under its authorized rates and
14 charges. Staff therefore recommends approval of Johnson's application to provide wastewater
15 service to the requested extension area subject to compliance with Staff's recommendations.

16 **La Osa and Sonoran Litigation**

17 18. In the Staff Report, Staff pointed out that the Arizona Attorney General's Office
18 recently filed a civil lawsuit against the principal owner of Johnson Utilities Company, George
19 Johnson, and against various affiliates of Johnson Utilities³. The allegations against Mr. Johnson and
20 the Johnson affiliates include trespass, breach of a grazing lease, destruction of native plants on state
21 and private land, water quality discharge violations, and unlawful killing of bighorn sheep. Staff
22 states that the litigation is focused primarily on Mr. Johnson's actions as the owner of La Osa Ranch,
23 a 10,000 acre property in southern Gila County which is adjacent to state trust land and the Ironwood
24 National Forest Monument. Johnson Utilities Company is not named in the lawsuit.

25 19. Sonoran Utility Services, LLC, ("Sonoran"), which was previously owned by Mr.
26 Johnson or Johnson affiliates, is also named as a defendant in a civil lawsuit filed by Lennar
27

28 ³ Maricopa County Superior Court Case No. CV2005-002692 ("La Osa litigation").

1 Communities Development, Inc. ("Lennar") related to the formation and operation of the 387 Water
 2 Improvement District and the 387 Wastewater Improvement District⁴. Although Mr. Johnson was
 3 named personally as a defendant in the Sonoran litigation, Johnson Utilities Company is not a party
 4 in the lawsuit.

5 20. Johnson Utilities' executive vice-president, Brian Tompsett, testified that the litigation
 6 will not have any detrimental impact on the ability of Johnson Utilities Company to serve its
 7 customers because Johnson Utilities has no financial interest in any of the affiliates named in the
 8 lawsuits. Mr. Tompsett also stated that Mr. Johnson and the named affiliates have sufficient
 9 insurance protection and liquidity to insulate Johnson Utilities in the event a judgment is entered
 10 against Mr. Johnson or the other affiliates in either of the lawsuits (Tr. 59-60).

11 **Staff Recommendations**

12 21. Staff recommends approval of Johnson's application subject to compliance with the
 13 following conditions:

- 14 a. Johnson must file with Docket Control within 365 days of the
 15 effective date of this Decision a copy of its Pinal County franchise
 16 including the extension area;
- 17 b. Johnson must file with Docket Control by August 1, 2006 a copy
 18 of the ADEQ 4 MGD Aquifer Protection Permit for the Pecan
 19 wastewater treatment plant;
- 20 c. Johnson must file with Docket Control by August 1, 2006 a copy
 21 of the CAAG Section 208 Plan inclusive of the extension area;
- 22 d. Johnson must file with Docket Control a quarterly report on the
 23 status of the pending La Osa litigation; and
- 24 e. In accordance with the April 19, 2005 late-filed "Exhibit 1"
 25 agreement between Johnson and Staff, Johnson must file with
 26 Docket Control within 60 days of the effective date of this
 27 Decision the following:
- 28 i. The name, home office location and description of
 any of the entities that are named as defendants in the La
 Osa litigation, and their relationship to each other and to
 Johnson Utilities Company;

⁴ Maricopa County Superior Court Case No. CV2005-002548 ("Sonoran litigation").

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ii. A brief description of the business activities conducted by any entity in subsection i, above;

iii. A description of plans for the entities identified in subsection i, above, to modify or change business activities, enter into a new business venture or to acquire, merge or otherwise establish a new business entity;

iv. An assessment of the effect of current and planned affiliated activities by each entity identified in subsection i, above, on Johnson Utilities Company's capital structure and its ability to attract capital at fair and reasonable rates;

v. The dollar amount transferred between Johnson Utilities Company and each of the entities identified in subsection i, above, during the previous 12 months and the purpose of each transfer. Johnson shall prepare and submit to Staff an update to this report every 6 months;

vi. Copies of contracts or agreements to receive, or provide management, engineering, accounting, legal, financial or other similar services between Johnson Utilities Company and any of the entities identified in subsection i, above. Johnson shall prepare and submit to Staff an update to this report every 6 months;

vii. Copies of contracts or agreements to purchase or sell goods or real property between Johnson Utilities Company and any of the entities identified in subsection i, above; and

viii. Contracts or agreements to lease goods or real property between Johnson Utilities Company and any of the other entities identified in subsection i, above.

f. Johnson Utilities Company would also be bound by the following conditions:

i. Any transactions between Johnson Utilities Company and any of the defendants in the La Osa litigation would be subject to Commission scrutiny, including allowing Staff to see books and records of Johnson and/or the defendant with whom business was transacted;

ii. Johnson Utilities Company will not obtain a financial interest in any of the defendants in the La Osa litigation or make any loans to, or guarantees for, any of the

1 defendants without prior Commission approval; and

2 iii. Johnson Utilities Company will not make any
3 dividend payments if such payments would have the effect
4 of impairing its financial status, prevent it from attracting
5 capital at fair and reasonable terms or impair Johnson's
6 ability to provide safe, reasonable and adequate service.

5 **Conclusion**

6 22. Staff's recommendation for approval of the application is reasonable and shall be
7 adopted, subject to compliance with the conditions discussed herein. In addition, we will require that
8 the reporting requirements and conditions described above for the La Osa litigation shall also be
9 required with respect to the Sonoran litigation.

10 23. In a prior water and wastewater CC&N extension proceeding involving Palo Verde
11 Utilities Company, LLC, and Santa Cruz Water Company, LLC, we required each company to
12 procure a \$500,000 performance bond due to a substantial judgment that had been entered by a court
13 in Oregon against the president of both companies⁵. The performance bond requirements were
14 imposed as a measure of protection for the companies' customers due to the possibility that the
15 utilities could be affected by the judgment, because of those companies' limited operating experience,
16 and because of rapidly expanding service areas. Although Johnson Utilities Company insists that its
17 operations are well insulated from any judgment that may be entered against Mr. Johnson and the
18 other non-utility affiliates named in the lawsuits, we believe it is prudent at this time to require
19 Johnson to procure a \$1 million performance bond as a means of protection against any potential
20 detrimental impact on customers that may occur as a result of a judgment against Mr. Johnson and/or
21 Johnson affiliates. Proof of the performance bond shall be filed in this docket prior to service being
22 provided to any customers in the CC&N extension area. The bonds shall remain in place until further
23 Order of the Commission.

24 24. Given the rapid expansion of Johnson's service area in the past several years and the
25 fact that Johnson's rates have not been reviewed since they were initially established in 1997, we also

26
27 ⁵ Decision No. 66394 (October 6, 2003), at 11-12. The performance bond requirements for Palo Verde and Santa Cruz
28 were increased to \$750,000 per company in a subsequent CC&N extension proceeding. Decision No. 67240 (September
23, 2004), at 15.

1 believe the Company should be required to file a rate application for both water and wastewater in
2 order to allow Staff to perform a full audit of Johnson's operations and ensure that the established
3 rates are reasonable based on all plant, revenues and expenses. Johnson shall therefore file, by no
4 later than June 1, 2006, a rate application based on a 2005 test year.

5 **CONCLUSIONS OF LAW**

6 1. Johnson is a public service corporation within the meaning of Article XV of the
7 Arizona Constitution and A.R.S. §40-281 *et seq.*

8 2. The Commission has jurisdiction over Johnson and the subject matter of the
9 application.

10 3. Notice of the application was provided in accordance with law.

11 4. There is a public need and necessity for wastewater utility service in the proposed
12 extension area.

13 5. Johnson is a fit and proper entity to receive an extension of its wastewater CC&N to
14 include the service area more fully described in Exhibit A attached hereto, subject to compliance with
15 the conditions set forth above.

16 **ORDER**

17 IT IS THEREFORE ORDERED that the application of Johnson Utilities Company for an
18 extension of the service area under its Certificate of Convenience and Necessity to include the area
19 described in Exhibit A attached hereto and incorporated herein by reference be, and is hereby
20 approved, subject to the conditions more fully described herein.

21 IT IS FURTHER ORDERED that the current rates and charges set forth in the tariffs of
22 Johnson Utilities Company shall be applied to all customers in the CC&N extension area approved
23 herein.

24 IT IS FURTHER ORDERED that Johnson Utilities Company shall file with Docket Control
25 within 365 days of the effective date of this Decision a copy of its Pinal County franchise including
26 the extension area.

27 IT IS FURTHER ORDERED that Johnson Utilities Company shall file with Docket Control
28 by August 1, 2006 a copy of the ADEQ 4 MGD Aquifer Protection Permit for the Pecan wastewater

1 treatment plant.

2 IT IS FURTHER ORDERED that Johnson Utilities Company shall file with Docket Control
3 by August 1, 2006 a copy of the CAAG Section 208 Plan inclusive of the extension area.

4 IT IS FURTHER ORDERED that Johnson Utilities Company shall file with Docket Control,
5 beginning July 1, 2005, quarterly reports on the status of the pending La Osa and Sonoran litigation.

6 IT IS FURTHER ORDERED that Johnson Utilities Company shall comply with affiliated
7 interest reporting requirements and conditions, pursuant to the April 19, 2005 late-filed exhibit
8 described in detail above.

9 IT IS FURTHER ORDERED that Johnson Utilities Company shall procure a \$1 million
10 performance bond, with proof of such performance bond filed in Docket Control prior to retail
11 service being provided to any customers in the CC&N extension area. The performance bond shall
12 remain in place until further Order of the Commission and maintenance of the required bond shall be
13 evidenced by a quarterly filing (by January 15, April 15, July 15, and October 15) of a letter of bond
14 confirmation.

15 IT IS FURTHER ORDERED that Johnson Utilities Company shall file a rate application by
16 no later than June 1, 2006, based on a 2005 test year.

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1 IT IS FURTHER ORDERED that in the event Johnson Utilities Company fails to comply
2 with the above-stated conditions within the times specified, the CC&N extension approved herein
3 shall be deemed null and void without further Order of the Commission.

4 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

5 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.
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8 _____
CHAIRMAN COMMISSIONER COMMISSIONER

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13 _____
COMMISSIONER COMMISSIONER

14
15 IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive
16 Secretary of the Arizona Corporation Commission, have
17 hereunto set my hand and caused the official seal of the
18 Commission to be affixed at the Capitol, in the City of Phoenix,
19 this ____ day of _____, 2005.

20 _____
BRIAN C. McNEIL
EXECUTIVE SECRETARY

21 DISSENT _____
22

23 DISSENT _____
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DDN:mj
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1 SERVICE LIST FOR:

JOHNSON UTILITIES COMPANY

2 DOCKET NO.:

WS-02987A-04-0889

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