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ORIGINAL



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



ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION
DOCUMENT CONTROL

DATE: July 18, 2005
DOCKET NO: W-01825A-04-0546
TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Marc E. Stern. The recommendation has been filed in the form of an Order on:

LAGOON ESTATES WATER COMPANY
(RATES)

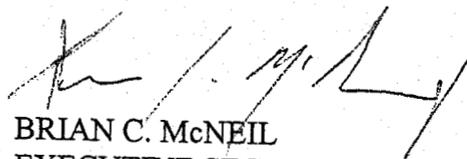
Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and thirteen (13) copies of the exceptions with the Commission's Docket Control at the address listed below by **4:00 p.m.** on or before:

JULY 27, 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 Open Meeting to be held on:

AUGUST 9 AND 10, 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.


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 LAGOON ESTATES WATER COMPANY FOR A
10 RATE ADJUSTMENT.

DOCKET NO. W-01825A-04-0546

11 DECISION NO. _____

12 ORDER

13 Open Meeting
14 August 9 and 10, 2005
15 Phoenix, Arizona

16 **BY THE COMMISSION:**

17 On July 28, 2004, Lagoon Estates Water Company (“Applicant” or “Company”) filed with the
18 Arizona Corporation Commission (“Commission”) an application for a permanent rate increase in its
19 water rates and charges.

20 On August 26, 2004, pursuant to A.A.C. R14-2-103, the Commission’s Utilities Division
21 (“Staff”) issued a notice of deficiency with respect to the Company’s rate application.

22 On September 9, 2004, the Company filed amendments to its rate application and a copy of its
23 proposed Curtailment Tariff for Commission approval.

24 On October 8, 2004, pursuant to A.A.C. R14-2-103, Staff issued a notice of sufficiency and
25 classified the Company as a Class D utility.

26 On December 16, 2004, the Company filed a letter requesting that the timeclock rule be
27 suspended and requested at least a 30 to 60 day suspension of the timeclock rule to file data relative
28 to its arsenic treatment costs.

On March 10, 2005, by Procedural Order, the timeclock was suspended until further Order.

On June 7, 2005, Staff filed its report, recommending that the rates proposed by Staff be approved.

* * * * *

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

FINDINGS OF FACT

1. Pursuant to authority granted by the Commission, Applicant is an Arizona corporation engaged in the business of providing water service in an area approximately 20 miles south of Bullhead City in Mohave County, Arizona.

2. Applicant's present rates and charges for water were approved in Decision No. 62508 (May 4, 2000).

3. On July 28, 2004, the Company filed an application requesting authority to increase its rates and charges for water service.

4. Applicant provided notice to its customers of its proposed rate increase by first class U.S. mail and, in response thereto, two written protests have been received by the Commission opposing Applicant's proposed increase.

5. On September 9, 2004, the Company requested the Commission's approval for its proposed Curtailment Tariff.

6. On October 8, 2004, Staff filed notice that the Company's rate application had met the Commission's sufficiency requirements pursuant to A.A.C. R14-2-103, but processing of the application was delayed at Applicant's request pending the filing by the Company of data relevant to its arsenic treatment costs.

7. During the test year ended December 31, 2003 ("TY"), Applicant served 258 metered customers, the majority of which are residential users who are served by 5/8" x 3/4" meters.

8. Average and median meter usage by residential users during the TY were 7,150 and 5,610 gallons per month, respectively.

9. Staff conducted an investigation of Applicant's proposed rates and charges for water service and filed its Staff Report on the Company's rate application request on June 7, 2005.

10. The water rates and charges for Applicant at present, as proposed in the Application and as recommended by Staff are as follows:

| | Present Rates | Proposed Rates | |
|----|---|----------------|--------------|
| | | <u>Company</u> | <u>Staff</u> |
| 1 | | | |
| 2 | | | |
| 3 | <u>MONTHLY USAGE CHARGE:</u> | | |
| 4 | 5/8" x 3/4" Meter | \$12.25 | \$15.00 |
| 5 | 3/4" Meter | 18.50 | 20.25 |
| 6 | 1" Meter | 30.00 | 35.00 |
| 7 | 1 1/2" Meter | 61.00 | 65.00 |
| 8 | 2" Meter | 98.00 | 108.00 |
| 9 | 3" Meter | 185.00 | 190.00 |
| 10 | 4" Meter | 305.00 | 325.00 |
| 11 | 6" Meter | 612.00 | 625.00 |
| 12 | 8" Meter | 708.75 | 825.00 |
| 13 | Gallons Included in Minimum | 1,000 | 0 |
| 14 | <u>Gallonge Charge Per 1,000 Gallons</u> | \$2.00 | \$3.00 |
| 15 | <u>5/8 x 3/4 Inch Meter</u> | | |
| 16 | Tier one - 0 to 3,000 gallons | | \$2.00 |
| 17 | Tier two - 3,001 to 10,000 gallons | | 2.55 |
| 18 | Tier three - In excess of 10,000 gallons | | 3.25 |
| 19 | <u>1 Inch Meter</u> | | |
| 20 | Tier One - 0 to 10,000 gallons | | 2.55 |
| 21 | Tier Two - all gallons over 10,001 | | 3.25 |
| 22 | <u>2 to 8 Inch Meters</u> | | |
| 23 | Tier One - 0 to 30,000 gallons | | 2.55 |
| 24 | Tier Two - all gallons over 30,001 | | 3.25 |
| 25 | <u>SERVICE LINE AND METER INSTALLATION CHARGES:</u> | | |
| 26 | (Refundable pursuant to A.A.C. R14-2-405) | | |
| 27 | 5/8" x 3/4" Meter | \$350.00 | \$455.00 |
| 28 | 3/4" Meter | 390.00 | 500.00 |
| 29 | 1" Meter | 450.00 | 585.00 |
| 30 | 1 1/2" Meter | 685.00 | 890.00 |
| 31 | 2" Meter | 1,100.00 | 1,430.00 |
| 32 | 3" Meter | 1,500.00 | 1,950.00 |
| 33 | 4" Meter | 2,400.00 | 3,120.00 |
| 34 | 6" Meter | 4,300.00 | 5,600.00 |
| 35 | 8" Meter | 6,600.00 | 8,580.00 |
| 36 | <u>SERVICE CHARGES:</u> | | |
| 37 | Establishment | \$30.00 | \$40.00 |
| 38 | | | \$30.00 |

| | | | | |
|---|------------------------------------|-------|-------|-------|
| 1 | Establishment (After Hours) | 35.00 | 60.00 | 40.00 |
| | Reconnection (Delinquent) | n/a | 45.00 | 30.00 |
| 2 | Meter Test (If Correct) | 30.00 | 40.00 | 30.00 |
| | Deposit | * | * | * |
| 3 | Deposit Interest | * | * | * |
| | Reestablishment (Within 12 Months) | ** | ** | ** |
| 4 | NSF Check | 20.00 | 30.00 | 25.00 |
| 5 | Deferred Payment (Per Month) | 1.5% | 1.5% | *** |
| | Meter Reread (If Correct) | 18.00 | 23.00 | 23.00 |

7 * Per Commission rule A.A.C. R-14-2-403(B).

8 ** Number of months off system times the monthly minimum per Commission rule A.A.C. R14-2-403(D).

9 *** Per Commission rule A.A.C. R14-2-409(G).

10 11. Pursuant to the Staff Report, Applicant's fair value rate base ("FVRB") is determined
11 to be \$159,335 which is the same as its original cost rate base. The Company's FVRB reflects an
12 \$11,237 increase by Staff of Applicant's proposed FVRB due in large part to an increase in
13 Applicant's working capital.

14 12. Staff increased Applicant's TY operating expenses by \$8,687 primarily due to
15 adjustments which increase the following Company expenses: \$1,309 for chemicals; \$7,200 for
16 outside services; and \$2,500 for taxes other than income.

17 13. Applicant's present water rates and charges produced operating revenues of \$106,864
18 and adjusted operating expenses of \$109,087 which resulted in an operating loss of \$2,223 during the
19 TY.

20 14. The water rates and charges Applicant proposed would produce operating revenues of
21 \$133,195 and adjusted operating expenses of \$109,087 resulting in net operating income of \$24,108
22 or a 15.13 percent rate of return on FVRB.

23 15. The water rates and charges Staff recommended would produce operating revenues of
24 \$127,000 and adjusted operating expenses of \$109,087, resulting in net operating income of \$17,913
25 or a 11.24 percent rate of return on FVRB.

26 16. Applicant's proposed rate schedule would increase the average monthly customer
27 water bill by 40.3 percent, from \$24.55 to \$34.45, and the median monthly customer water bill by
28 38.9 percent, from \$21.47 to \$29.83.

1 17. Staff's recommended rates would increase the average monthly customer water bill by
2 28.6 percent, from \$24.55 to \$31.58, and increase the median monthly customer water bill by 28.8
3 percent, from \$21.47 to \$27.66.

4 18. According to the Staff Report, Applicant is in compliance with its Commission
5 compliance action filings and prior Commission Orders. Additionally, according to Staff, Applicant
6 is current on the payment of its property taxes and its sales taxes, and is providing water which meets
7 the requirements of the Safe Drinking Water Act.

8 19. According to the narrative review by Staff, Applicant has two separate water systems
9 which are located approximately one mile apart (Arizona Department of Environmental Quality
10 ("ADEQ") identification numbers 08-021 and 08-046). System 08-021 supplies water to
11 approximately 225 customers from two separate well sites designated "Unit 4" and "Unit 7". System
12 08-046 supplies water to approximately 40 customers from one well site at which two wells are
13 located. Both systems pump water directly to the Company's distribution systems through pressure
14 tanks and comply with ADEQ's storage rule because the systems utilize multiple water sources.

15 20. According to Staff, the Company's 08-021 system meets the new federal arsenic
16 standard effective January 23, 2006, of containing less than 10 parts per billion ("ppb") of arsenic and
17 this system will not require arsenic remediation. However, Applicant's 08-046 system fails to meet
18 the new arsenic standard because it contains 14 ppb of arsenic and will require some form of remedial
19 treatment to remove the excess arsenic.

20 21. Applicant has begun to address the excess arsenic problem for its 08-046 system by
21 seeking a \$35,000 technical assistance grant from the Water Infrastructure Finance Authority
22 ("WIFA") to seek the most cost effective method of treatment.

23 22. In conjunction with this rate proceeding, the Company is requesting the establishment
24 of an Arsenic Remediation Surcharge Mechanism ("ARSM") to address the expected expense of
25 remediating the excess arsenic found on its 08-046 system.

26 23. Applicant is investigating various treatment options which vary in cost from \$325,000
27 up to \$2.3 million which would also address a treatment plan for excess iron and manganese on both
28 of its systems.

1 24. Until a final decision is made on what is the most efficient and cost-effective
2 methodology to remove the excess arsenic from the Company's 08-046 system, the Company will not
3 make a final decision on how the facilities will be financed.¹

4 25. Staff additionally recommended that the Commission order the following:

- 5
- 6 • that Applicant notify its customers of the water rates and charges approved hereinafter
7 and their effective date by means of an insert in its next monthly billing and file a copy
8 of the notice sent to its customers with the Compliance Section of the Utilities
9 Division ("Compliance Section");
 - 10 • that Applicant file, within 30 days of the effective date of this Decision, with the
11 Commission's Docket Control, a copy of the schedule of its approved rates and
12 charges;
 - 13 • that Applicant's proposed Curtailment Tariff be approved and that Applicant file,
14 within 30 days of the effective date of this Decision, with the Commission's Docket
15 Control, a copy of the approved tariff;
 - 16 • that the Company pursue the development of an ARSM as recommended by Staff in
17 this proceeding and a requirement that the ARSM be separately identified on monthly
18 customer billings;
 - 19 • that the Company file with the Commission's Docket Control its plan for arsenic
20 treatment that identifies the intended method for financing any capital improvements
21 included in the treatment plan;
 - 22 • that if the Company's arsenic treatment plan includes obtaining debt financing, it
23 should file concurrently before the Commission an application requesting
24 authorization to incur debt and an application for an arsenic treatment surcharge tariff
25 that would enable it to meet the principle and interest obligations on the proposed debt
26 and income taxes on the surcharge;
 - that the Company postpone the selection and purchase or lease of any arsenic
 treatment facilities or processes until the Commission's Staff reviews and approves the
 selected removal process or arsenic control method;
 - that the Company be required to file a general rate application within 60 months of the
 implementation of its ARSM after its approval by the Commission; and

27 ¹ On August 10, 2004, the Commission, in Decision No. 67163, approved the concept of establishing a
28 methodology for Mountain Glen Water Services, Inc. to institute the development of an ARSM to begin to address how to
resolve the expense of treating excess arsenic found in the water supply of an Arizona water company in an economical
fashion.

- that Applicant, in addition to the collection of its regular rates and charges, collect from its customers their proportionate share of any privilege, sales, or use tax as provided for in A.A.C. R14-2-409(D).

26. We find that Applicant must charge rates that allow it to operate in a viable fashion in order to be able to provide reliable service to its customers. We agree with Staff's recommendations and find that Staff's proposed rates which are projected to provide a rate of return of approximately 11.24 percent are just and reasonable under the circumstances described herein.

27. Our approval of Staff's recommendations includes the concept of an arsenic surcharge mechanism methodology as set forth in detail in the Staff Report and in the attached Engineering Report. However, we make no finding at this time regarding the reasonableness of any specific costs related to arsenic treatment because the Company has not yet determined the most cost-effective means of complying with the new federal arsenic standards.² As described in Staff's recommendations, prior to implementing the surcharge mechanism, the Company must submit a request for financing and for implementation of a surcharge in accordance with Staff's proposed methodology.

28. The above-captioned rate Docket will remain open until December 31, 2005, in order to enable the Company, if necessary, to submit within this Docket a request for the imposition of a surcharge and an application for financing approval once the Company has determined the appropriate arsenic treatment methodology and has ascertained the costs associated with implementing that arsenic compliance plan, and has its plan approved by Staff. The Company's arsenic surcharge request must be made in the above-captioned Docket in order to consider the reasonableness of the specific costs of the Company's plan in the context of the FVRB determined in this Decision. Only after Staff has completed its comprehensive review of such a surcharge application, including an analysis of the surcharge calculation and a determination as to whether the Company's treatment plan is the most efficient and cost-effective means of compliance, will we

² The Company should evaluate carefully whether compliance with the new arsenic standards may be accomplished by blending of water, drilling of a new well, point of use technology, and any other treatment options that would provide compliance at the lowest possible cost to customers. We are concerned that the Company's estimated cost of compliance of \$325,000 to \$2.3 million, for a system that serves only 40 customers, is grossly excessive and would not satisfy a least-cost compliance review.

1 consider Staff's recommendation to approve a specific arsenic surcharge for Applicant. In addition,
2 affected customers must be given notice by the Company of the specific surcharge costs before we
3 will consider approval of the surcharge.

4 29. As previously stated in Decision No. 67163, although we are approving the concept of
5 Staff's proposed ARSM in this Decision, we wish to make clear that we are making no determination
6 as to the appropriate ratemaking treatment that should ultimately be accorded to arsenic treatment
7 costs. If the Commission determines in a later phase of this proceeding that a specific surcharge
8 amount should be assessed to the Company's customers, various ratemaking treatments may be
9 considered in the context of a subsequent rate case, including, but not limited to whether the
10 Company and its customers should share in the burdens associated with arsenic compliance costs, and
11 whether revenues derived from the imposition of an arsenic surcharge should be treated as
12 contributions rather than permitting full rate base recognition of plant purchased with surcharge
13 revenues.

14 CONCLUSIONS OF LAW

15 1. Applicant is a public service corporation within the meaning of Article XV of the
16 Arizona Constitution and A.R.S. §§ 40-250 and 40-251.

17 2. The Commission has jurisdiction over Applicant and the subject matter of the
18 application.

19 3. Notice of the application was provided in the manner prescribed by law.

20 4. Under the circumstances discussed herein, the rates and charges for Applicant as
21 authorized hereinafter are just and reasonable and should be approved without a hearing.

22 5. Staff's recommendations, as set forth in Findings of Fact No. 25, are reasonable and
23 should be adopted, subject to the clarifications discussed in Findings of Fact Nos. 27, 28 and 29,
24 including the requirement that a subsequent request for financing approval must be submitted prior to
25 implementation of an arsenic treatment plan surcharge.

26 6. The Applicant should comply with Staff's recommendations as set forth in Findings of
27 Fact No. 25, as discussed further in Findings of Fact Nos. 27, 28 and 29.

28 7. Approval of the concept of an ARSM, as discussed hereinabove, is consistent with the

1 Commission's authority under the Arizona Constitution, Arizona ratemaking statutes, and applicable
 2 case law.

3 8. The record in this Docket shall remain open until December 31, 2005, for the purpose
 4 of receiving, if necessary, the Company's amended request for financing and for establishment of an
 5 arsenic surcharge once the costs of the Company's arsenic treatment plan are known.

6 9. Based on our findings and in light of Staff's recommendations, no hearing is
 7 necessary.

8 **ORDER**

9 IT IS THEREFORE ORDERED the Lagoon Estates Water Company is hereby directed to file
 10 on or before September 1, 2005, revised rate schedules setting forth the following rates and charges:

11 **MONTHLY USAGE CHARGE:**

| | | |
|----|-------------------|---------|
| 13 | 5/8" x 3/4" Meter | \$15.00 |
| 14 | 3/4" Meter | 20.25 |
| 15 | 1" Meter | 35.00 |
| 16 | 1 1/2" Meter | 65.00 |
| 17 | 2" Meter | 108.00 |
| 18 | 3" Meter | 190.00 |
| 19 | 4" Meter | 325.00 |
| 20 | 6" Meter | 625.00 |
| 21 | 8" Meter | 825.00 |

22 **Gallonage Charge Per 1,000 Gallons**

| | | |
|----|---|--------|
| 23 | <u>5/8 x 3/4 Inch Meter</u> | |
| 24 | Tier One – 0 to 3,000 gallons | \$2.00 |
| 25 | Tier Two – 3,001 to 10,000 gallons | 2.55 |
| 26 | Tier Three– In excess of 10,000 gallons | 3.25 |

| | | |
|----|------------------------------------|------|
| 27 | <u>1 Inch Meter</u> | |
| 28 | Tier One – 0 to 10,000 gallons | 2.55 |
| 29 | Tier Two – all gallons over 10,000 | 3.25 |

| | | |
|----|------------------------------------|------|
| 30 | <u>2 to 8 Inch Meters</u> | |
| 31 | Tier One – 0 to 30,000 gallons | 2.55 |
| 32 | Tier Two – all gallons over 30,000 | 3.25 |

33 ...

34 ...

SERVICE LINE AND METER INSTALLATION CHARGES:

(Refundable pursuant to A.A.C. R14-2-405)

| | |
|-------------------|----------|
| 5/8" x 3/4" Meter | \$455.00 |
| 3/4" Meter | 500.00 |
| 1" Meter | 585.00 |
| 1 1/2" Meter | 890.00 |
| 2" Meter | 1,430.00 |
| 3" Meter | 1,930.00 |
| 4" Meter | 3,120.00 |
| 6" Meter | 5,600.00 |
| 8" Meter | 8,580.00 |

SERVICE CHARGES:

| | |
|------------------------------------|---------|
| Establishment | \$30.00 |
| Establishment (After Hours) | 40.00 |
| Reconnection (Delinquent) | 30.00 |
| Meter Test (If Correct) | 30.00 |
| Deposit | * |
| Deposit Interest | * |
| Reestablishment (Within 12 Months) | ** |
| NSF Check | 25.00 |
| Deferred Payment (Per Month) | *** |
| Meter Reread (If Correct) | 23.00 |

* Per Commission rule A.A.C. R-14-2-403(B).

** Number of months off system times the monthly minimum per Commission rule A.A.C. R14-2-403(D).

*** Per Commission rule A.A.C. R14-2-409(G).

IT IS FURTHER ORDERED that Lagoon Estates Water Company notify its customers of the water rates and charges approved hereinafter and their effective date by means of an insert in its next monthly billing and file a copy of the notice when sent to its customers with the Compliance Section of the Utilities Division.

IT IS FURTHER ORDERED that the above water rates and charges shall be effective for all service provided after September 1, 2005.

IT IS FURTHER ORDERED that Lagoon Estates Water Company is hereby directed to comply with Staff's recommendations as set forth in Findings of Fact No. 25, as more fully described in Findings of Fact Nos. 27, 28 and 29.

IT IS FURTHER ORDERED that Lagoon Estates Water Company shall file, within 30 days

1 of the effective date of this Decision, a copy of the schedule of its approved rates and charges.

2 IT IS FURTHER ORDERED that Lagoon Estates Water Company shall file an arsenic
3 removal treatment plan in this Docket the earlier of December 31, 2005, or within 30 days after
4 receiving preliminary approval of a loan from WIFA for financing arsenic treatment facilities.

5 IT IS FURTHER ORDERED that the record in this Docket shall remain open until December
6 31, 2005, for the purpose of receiving, if necessary, Lagoon Estates Water Company's amended
7 request for financing and for establishment of an arsenic remediation surcharge, once the costs of the
8 proposed arsenic treatment plan are known.

9 IT IS FURTHER ORDERED that, in accordance with Staff's recommendation described
10 hereinabove, Lagoon Estates Water Company shall file in this Docket, within 30 days after receiving
11 preliminary approval of a loan from WIFA for financing arsenic treatment facilities, a request for
12 financing and for approval of an arsenic surcharge mechanism.

13 IT IS FURTHER ORDERED that the determination and collection of any specific arsenic
14 removal surcharge shall require subsequent Commission approval in this docket following a
15 comprehensive review by Staff regarding compliance by Lagoon Estates Water Company with
16 Staff's surcharge calculation methodology and a determination and recommendation by Staff with
17 respect to whether the Lagoon Estates Water Company's proposed treatment plan is the most
18 efficient and cost-effective means of compliance with new federal arsenic standards.

19 IT IS FURTHER ORDERED that Lagoon Estates Water Company shall file, within 60
20 months of the effective date of this Decision, a new rate case application which shall address
21 necessary and appropriate ratemaking treatment for arsenic treatment facilities.

22 IT IS FURTHER ORDERED that in the event Lagoon Estates Water Company fails to file a
23 new rate case application within 60 months of the date of this Decision, any arsenic treatment
24 surcharge then in place shall be terminated without further Order by the Commission.

25 IT IS FURTHER ORDERED that Lagoon Estates Water Company's proposed Curtailment
26 Plan tariff be approved, subject to the requirement that the final approved tariff be filed by the
27 Company within 30 days of the Decision in this matter.

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IT IS FURTHER ORDERED that in addition to collection of its regular rates and charges approved herein, Lagoon Estates Water Company shall collect from its customers their proportionate share of any privilege, sales or use tax pursuant to A.A.C. R14-2-409(D).

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 _____, 2005.

BRIAN C. McNEIL
EXECUTIVE SECRETARY

DISSENT _____

DISSENT _____

1 SERVICE LIST FOR: LAGOON ESTATES WATER COMPANY

2 DOCKET NO.: W-01825A-04-0546

3
4 Stanley Miller
5 Lagoon Estates Water Company
6 2600 North 44th Street, Ste. 203
7 Phoenix, AZ 85008

8 Christopher Kempley, Chief Counsel
9 Legal Division
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