



BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

Arizona Corporation Commission

DOCKETED

OCT 25 2005

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

DOCKETED BY [Signature]

IN THE MATTER OF THE APPLICATION OF
JOHNSON UTILITIES COMPANY FOR AN
EXTENSION OF ITS CERTIFICATE OF
CONVENIENCE AND NECESSITY FOR
WASTEWATER SERVICE.

DOCKET NO. WS-02987A-04-0889

DECISION NO. 68236

OPINION AND ORDER

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

BY THE COMMISSION:

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

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

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

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

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 On May 9, 2005, a Recommended Opinion and Order was issued and Exceptions were due to
13 be filed by May 18, 2005. The Recommended Order was tentatively scheduled for the May 24 and
14 25, 2005 Open Meeting agenda.

15 On May 12, 2005, counsel for Johnson, Jay Shapiro of Fennemore Craig, P.C., filed a "Notice
16 of Withdrawal as Counsel of Record" ("Notice of Withdrawal"). The Notice of Withdrawal stated
17 that Richard Sallquist would be taking over representation of Johnson and all future correspondence
18 should be directed to Mr. Sallquist.

19 On May 13, 2005, Mr. Sallquist filed, on behalf of Johnson, a pleading entitled "Substitution
20 of Counsel and Motion to Continue Open Meeting Matter." As requested by the Company, the
21 matter was pulled from the May 24 and 25, 2005 agenda.

22 On June 2, 2005, Staff filed a Proposed Legal Description for the requested CC&N area.

23 By Procedural Order issued June 3, 2005, Johnson was directed to file an Application for
24 Withdrawal of Counsel, pursuant to the requirements of A.A.C. R14-3-104(E).

25 By Procedural Order issued June 8, 2005, this matter was tentatively rescheduled for the
26 Commission's July 12 and 13, 2005 Open Meeting agenda. The June 8, 2005 Procedural Order also
27 directed that Exceptions to the Recommended Opinion and Order should be filed by no later than
28 June 24, 2005. The Recommended Order was subsequently rescheduled for consideration at the

1 Commission's August 9, 10 and 11, 2005 Open Meeting.

2 On June 8, 2005, Fennemore Craig filed an Application for Withdrawal of Counsel, in
3 accordance with A.A.C. R14-3-104(E).

4 On June 13, 2005, Sallquist & Drummond filed an Application for Substitution of Counsel.

5 On June 21, 2005 a Procedural Order was issued granting Fennemore Craig permission to
6 withdraw as counsel, and authorizing Sallquist & Drummond to appear as counsel for Johnson in this
7 proceeding.

8 On June 24, 2005, Johnson filed Exceptions to the Recommended Opinion and Order.

9 On June 29, 2005, Johnson filed a Master Services Agreement and a Line Extension
10 Agreement between itself and Milagro Investors, LLC.

11 At the Commission's August 11, 2005 Open Meeting, the Recommended Opinion and Order
12 was discussed. During the course of those discussions, Johnson was directed to late-file additional
13 information regarding insurance coverage in place for George Johnson and various Johnson affiliates
14 that are parties to pending litigation in Maricopa County Superior Court.

15 On August 24, 2005, Johnson filed a cover letter and a number of insurance documents that
16 the Company claims supports its contention that a performance bond for Johnson Utilities is not
17 necessary.

18 * * * * *

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

21 **FINDINGS OF FACT**

22 **Background of Application**

23 1. Johnson Utilities Company is a public service corporation that provides water and
24 wastewater service in Pinal County, Arizona pursuant to an original CC&N granted in Decision No.
25 60223 (May 27, 1997). Subsequent CC&N extensions for water and/or wastewater service were
26 granted to Johnson in a number of other dockets.

27 2. On December 14, 2004, Johnson filed an application seeking to extend its CC&N to
28 provide wastewater service to an area adjacent to the CC&N extension area for which Johnson was

1 recently granted an order preliminary to issuance of a final order. *Arizona Utility Supply & Services,*
2 *LLC/Johnson Utilities Company*, Docket No. SW-04002A-02-0837 *et al.*, Decision No. 67586
3 (February 15, 2005). According to representatives of the developers/builders who offered public
4 comment at the hearing, wastewater service in the proposed extension area was originally intended to
5 be provided by Arizona Utility Supply & Services, LLC ("AUSS"). However AUSS was unable to
6 provide service to the extension area due to a number of operational problems that eventually resulted
7 in AUSS filing for bankruptcy (See detailed description of AUSS operational problems in Decision
8 No. 67586, at 4-7).

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

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

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

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

22 7. No intervention requests were received.

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

25 9. On March 11, 2005, Johnson filed a response to the Staff Report proposing an
26 alternative to Staff's recommendation that the Company should comply with affiliate interest

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 reporting requirements under A.A.C. R14-2-801 (see discussion below regarding affiliate interest
2 reporting requirements).

3 10. A public hearing on the application was held as scheduled on April 11, 2005.
4 Representatives of two homebuilders that are developing property in the proposed extension area
5 appeared at the hearing and offered comments in support of the application (Tr. 5-11). At the
6 conclusion of the hearing, Johnson and Staff were directed to submit a late-filed exhibit following
7 negotiations to resolve the disputed affiliate interest reporting issue.

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

12 **Wastewater Treatment System**

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

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

23 14. Pursuant to §208 of the federal Clean Water Act, each state is required to develop and
24 implement area-wide water quality management plans for pollution control purposes. The Central
25 Arizona Association of Governments ("CAAG") has been designated as the area-wide water quality
26 management planning agency for Pinal County. The extension area sought in this proceeding is

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 within the CAAG §208 planning area for Johnson, for service provided by the Pecan Plant, and
2 therefore conforms to the area-wide wastewater plans (*Id.* at 3-4).

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

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

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

22 **La Osa and Sonoran Litigation**

23 18. In the Staff Report, Staff pointed out that the Arizona Attorney General’s Office
24 recently filed a civil lawsuit against the principal owner of Johnson Utilities Company, George
25 Johnson, and against various affiliates of Johnson Utilities³. The allegations against Mr. Johnson and
26 the Johnson affiliates include trespass, breach of a grazing lease, destruction of native plants on state
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28 ³ Maricopa County Superior Court Case No. CV2005-002692 (“La Osa litigation”).

1 and private land, water quality discharge violations, and unlawful killing of bighorn sheep. Staff
2 states that the litigation is focused primarily on Mr. Johnson's actions as the owner of La Osa Ranch,
3 a 10,000 acre property in southern Pinal County which is adjacent to state trust land and the
4 Ironwood National Forest Monument. Johnson Utilities Company is not named in the lawsuit.

5 19. Sonoran Utility Services, LLC, ("Sonoran"), which was previously owned by Mr.
6 Johnson or Johnson affiliates, is also named as a defendant in a civil lawsuit filed by Lennar
7 Communities Development, Inc. ("Lennar") related to the formation and operation of the 387 Water
8 Improvement District and the 387 Wastewater Improvement District⁴. Although Mr. Johnson was
9 named personally as a defendant in the Sonoran litigation, Johnson Utilities Company is not a party
10 in the lawsuit.

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

17 **Staff Recommendations**

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

- 20 a. Johnson must file with Docket Control within 365 days of the
21 effective date of this Decision a copy of its Pinal County franchise
22 including the extension area;
- 23 b. Johnson must file with Docket Control by August 1, 2006 a copy
24 of the ADEQ 4 MGD Aquifer Protection Permit for the Pecan
25 wastewater treatment plant;
- 26 c. Johnson must file with Docket Control by August 1, 2006 a copy
27 of the CAAG Section 208 Plan inclusive of the extension area;
- 28 d. Johnson must file with Docket Control a quarterly report on the

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

1 status of the pending La Osa litigation; and

2 e. In accordance with the April 19, 2005 late-filed "Exhibit 1"
3 agreement between Johnson and Staff, Johnson must file with
4 Docket Control within 60 days of the effective date of this
5 Decision the following:

6 i. The name, home office location and description of
7 any of the entities that are named as defendants in the La
8 Osa litigation, and their relationship to each other and to
9 Johnson Utilities Company;

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

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

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

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

25 vi. Copies of contracts or agreements to receive, or
26 provide management, engineering, accounting, legal,
27 financial or other similar services between Johnson Utilities
28 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

1 conditions:

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

7 ii. Johnson Utilities Company will not obtain a
8 financial interest in any of the defendants in the La Osa
9 litigation or make any loans to, or guarantees for, any of the
10 defendants without prior Commission approval; and

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

11 Conclusion

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

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

6 24. Given the rapid expansion of Johnson's service area in the past several years and the
7 fact that Johnson's rates have not been reviewed since they were initially established in 1997, we also
8 believe the Company should be required to file a rate application for both water and wastewater in
9 order to allow Staff to perform a full audit of Johnson's operations and ensure that the established
10 rates are reasonable based on all plant, revenues and expenses. Johnson shall therefore file, by no
11 later than May 1, 2007, a rate application for both water and wastewater, based on a 2006 test year.
12 In addition, Staff shall commence an audit of Johnson's hook-up fee accounts, for both water and
13 wastewater, by no later than March 31, 2006.

14 CONCLUSIONS OF LAW

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

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

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

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

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

25 ORDER

26 IT IS THEREFORE ORDERED that the application of Johnson Utilities Company for an
27 extension of the service area under its Certificate of Convenience and Necessity to include the area
28 described in Exhibit A attached hereto and incorporated herein by reference be, and is hereby

1 approved, subject to the conditions more fully described herein.

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

5 IT IS FURTHER ORDERED that Johnson Utilities Company shall file with Docket Control,
6 as a compliance item in this case, within 365 days of the effective date of this Decision a copy of its
7 Pinal County franchise including the extension area.

8 IT IS FURTHER ORDERED that Johnson Utilities Company shall file with Docket Control,
9 as a compliance item in this case, by August 1, 2006 a copy of the ADEQ 4 MGD Aquifer Protection
10 Permit for the Pecan wastewater treatment plant.

11 IT IS FURTHER ORDERED that Johnson Utilities Company shall file with Docket Control,
12 as a compliance item in this case, by August 1, 2006 a copy of the CAAG Section 208 Plan inclusive
13 of the extension area.

14 IT IS FURTHER ORDERED that Johnson Utilities Company shall file with Docket Control,
15 as a compliance item in this case, beginning November 1, 2005, quarterly reports on the status of the
16 pending La Osa and Sonoran litigation.

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

20 IT IS FURTHER ORDERED that Johnson Utilities Company shall procure a \$500,000
21 performance bond, with proof of such performance bond filed in Docket Control, as a compliance
22 item in this case, prior to retail service being provided to any customers in the CC&N extension area.
23 If Johnson Utilities Company is named as a defendant in either the La Osa or Sonoran lawsuits, the
24 required bond amount shall be increased to \$1 million. The performance bond shall remain in place
25 until further Order of the Commission and maintenance of the required bond shall be evidenced by a
26 quarterly filing (by January 15, April 15, July 15, and October 15) of a letter of bond confirmation.

27 IT IS FURTHER ORDERED that Johnson Utilities Company shall file a rate application for
28 both water and wastewater by no later than May 1, 2007, based on a 2006 test year.

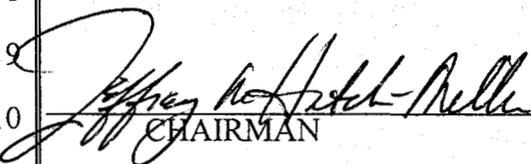
1 IT IS FURTHER ORDERED that Staff shall commence an audit of Johnson Utilities
2 Company's hook-up fee accounts, for both water and wastewater, by no later than March 31, 2006.

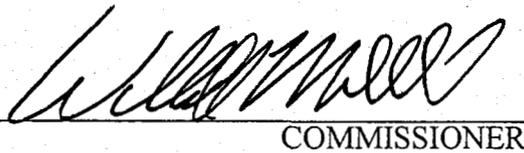
3 IT IS FURTHER ORDERED that in the event Johnson Utilities Company fails to comply
4 with the above-stated conditions within the times specified, the CC&N extension approved herein
5 shall be deemed null and void without further Order of the Commission.

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

7 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.

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10 CHAIRMAN


COMMISSIONER

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15 COMMISSIONER

COMMISSIONER



COMMISSIONER

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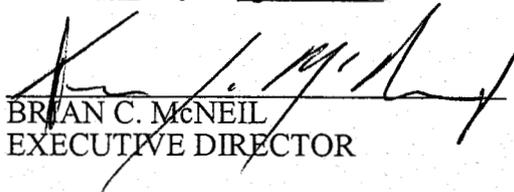
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IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Executive
Director of the Arizona Corporation Commission, have
hereunto set my hand and caused the official seal of the
Commission to be affixed at the Capitol, in the City of Phoenix,
this 25th day of Oct., 2005.

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BRIAN C. McNEIL
EXECUTIVE DIRECTOR

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24 DISSENT _____

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26 DISSENT _____

27 DDN:mj

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SERVICE LIST FOR:

JOHNSON UTILITIES COMPANY

DOCKET NO.:

WS-02987A-04-0889

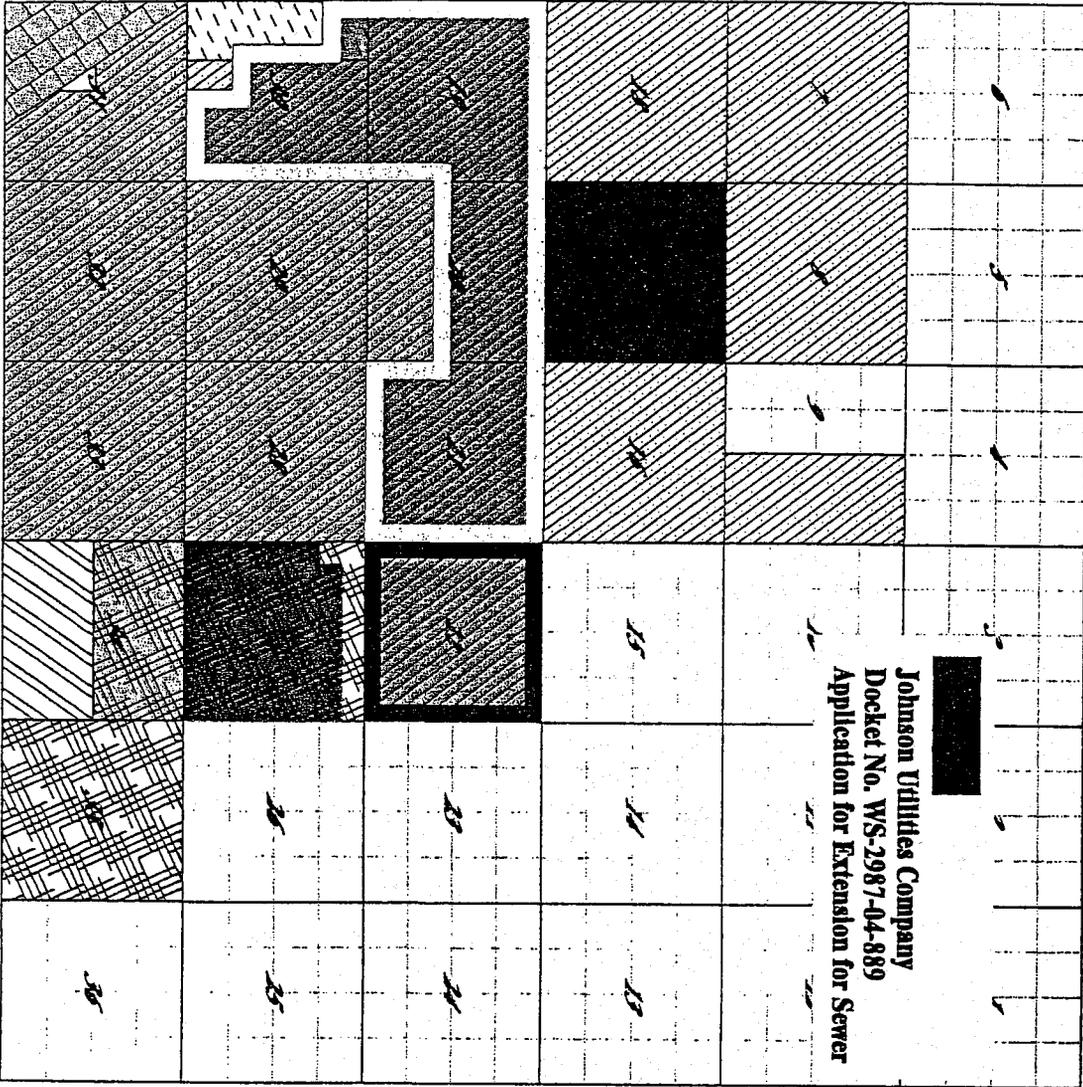
Jay L. Shapiro
Patrick J. Black
FENNEMORE CRAIG
3003 N. Central Avenue, Ste. 2600
Phoenix, AZ 85012

Christopher Kempsey, Chief Counsel
Legal Division
ARIZONA CORPORATION COMMISSION
1200 West Washington Street
Phoenix, Arizona 85007

Ernest G. Johnson, Director
Utilities Division
ARIZONA CORPORATION COMMISSION
1200 West Washington Street
Phoenix, Arizona 85007

COUNTY OF Pinal

RANGE 8 East



Johnson Utilities Company
 Docket No. WS-2987-04-889
 Application for Extension for Sewer

TOWNSHIP 2 South

Map No. 6



WS-2987 (6)

Johnson Utilities Company



Sewer



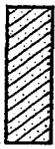
SW-4002 (1)

Arizona Utility Supply & Services, LLC



W-2859 (3)

Diversified Water Utilities, Inc.



W-2234 (2)

H₂O, Inc.



W-1395 (2)

Queen Creek Water Company



W-2425 (2)

Sun Valley Farms Unit VI Water Company



Arizona Utility Supply & Services

Docket No. SW-4002-02-837

Application to Transfer to Johnson Utilities

Docket No. WS-2987-02-837

Arizona Utility Supply & Services

Docket No. SW-4002-04-465

Application to Transfer to Johnson Utilities

Docket No. WS-2987-04-465



Johnson Utilities Company

Docket No. WS-2987-04-501

Application for Extension for Sewer

DECISION NO. 68236

EXHIBIT A

Legal Description

[Area Requested for Application]

Section 17, Township 2 South, Range 8 East in Pinal County, Arizona.